Internal Revenue Bulletin

CUMULATIVE BULLETIN 1961-2

JULY-DECEMBER 1961

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219	Rev. Proc. 60–6	C.B. 1960–1, 880
220	Announcement 60–37	I.R.B. 1960–17, 41
221	Announcement 60–35	I.R.B. 1960–16, 56
222	Rev. Rul. 60–164	C.B. 1960–1, 254
223	Not in Bulletin.	
224	Announcement 60–41	I.R.B. 1960–20, 43
225	Announcement 60–42	I.R.B. 1960–20, 44
226	Announcement 60–47	I.R.B. 1960–23, 55
227	Rev. Proc. 60–12	C.B. 1960–1, 890
228	Announcement 60–41	I.R.B. 1960–20, 43
229	Rev. Rul. 60–214	C.B. 1960–1, 700
230	Rev. Rul. 60–210	C.B. 1960–1, 38
231	Rev. Rul. 60–223	C.B. 1960–1, 57
232	Announcement 60–53	I.R.B. 1960–25, 41
233	Rev. Rul. 60–230	C.B. 1960–1, 688
234	Announcement 60–56	I.R.B. 1960–27, 25
235	Rev. Rul. 60–246	C.B. 1960–2, 462
236	Not in Bulletin.	
237	Announcement 60–63	I.R.B. 1960–28, 30
238	Announcement 60–66	I.R.B. 1960–31, 32
239	Announcement 60–64	I.R.B. 1960–29, 64
240	Announcement 60–74	I.R.B. 1960–35, 72
241	Rev. Rul. 60–278	C.B. 1960–1, 214
242	Announcement 60–70	I.R.B. 1960–31, 37
243	Announcement 60–75	I.R.B. 1960–35, 73
244	Not in Bulletin.	
245	Rev. Rul. 60–285	C.B. 1960–2, 473
246	Not in Bulletin.	
247	Rev. Rul. 60–293	C.B. 1960–2, 163
248	Not in Bulletin.	
249	Rev. Proc. 60–18	C.B. 1960–2, 988
250	Announcement 60–78	I.R.B. 1960–36, 35
251	Rev. Rul. 60–317	C.B. 1960–2, 452
252	Rev. Rul. 60–326	C.B. 1960–2, 32
253	Announcement 60–79	I.R.B. 1960–37, 64
254	Rev. Rul. 60–332	C.B. 1960–2, 463
255	Announcement 60–82	I.R.B. 1960–42, 107
256	Announcement 60–81	I.R.B. 1960–41, 44
257	Rev. Rul. 60–320	C.B. 1960–2, 198
258	Rev. Rul. 60–319	C.B. 1960–2, 501
259	Announcement 60–84	I.R.B. 1960–40, 40
260	Rev. Rul. 60–350	C.B. 1960–2, 394
261	Not in Bulletin.	
262	Announcement 60–96	I.R.B. 1960–47, 66
263	Announcement 60–91	I.R.B. 1960–45, 32
264	Announcement 60–95	I.R.B. 1960–45, 33
265	Announcement 60–98	I.R.B. 1960–49, 45
266	Not in Bulletin.	
267	Rev. Rul. 60–375	C.B. 1960–2, 407
268	Rev. Rul. 60–364	C.B. 1960–2, 382
269	Announcement 60–101	I.R.B. 1960–49, 47
270	Rev. Rul. 60–390	C.B. 1960–2, 463
271	Announcement 60–102	I.R.B. 1960–49, 47
272	Rev. Rul. 61–7	C.B. 1961–1, 166
273	Rev. Rul. 60–370	C.B. 1960–2, 203
274	Rev. Rul. 60–376	C.B. 1960–2, 38
275	Announcement 60–106	I.R.B. 1960–49, 68
276	Rev. Rul. 60–384	C.B. 1960–2, 172
277	Not in Bulletin.	

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278	Announcement 60-105	I.R.B. 1960-52, 68
279	Rev. Rul. 60-391	C.B. 1960-2, 299
	Rev. Rul. 60-392	C.B. 1960-2, 300
280	Announcement 61-2	I.R.B. 1961-3, 28
281	Announcement 60-105	I.R.B. 1960-52, 68
282	Rev. Rul. 61-19	C.B. 1961-1, 715
283	Rev. Rul. 61-103	C.B. 1961-1, 853
284	Rev. Rul. 61-16	C.B. 1961-1, 13
	Superseded by Rev. Rul. 61-136	C.B. 1961-1, 490
285	Announcement 61-7	I.R.B. 1961-5, 44
286	Announcement 61-9	I.R.B. 1961-4, 31
287	Announcement 61-3	I.R.B. 1961-3, 29
288	Announcement 61-16	I.R.B. 1961-7, 29
289	Rev. Rul. 61-17	C.B. 1961-1, 193
290	Announcement 61-10	I.R.B. 1961-4, 30
291	Announcement 61-11	I.R.B. 1961-5, 50
292	Announcement 61-25	I.R.B. 1961-10, 49
293	Announcement 61-18	I.R.B. 1961-8, 150
294	Announcement 61-12	I.R.B. 1961-5, 50
295	Announcement 61-19	I.R.B. 1961-8, 150
296	Announcement 61-22	I.R.B. 1961-8, 151
297	Announcement 61-23	I.R.B. 1961-8, 151
298	Announcement 61-24	I.R.B. 1961-8, 152
299	Announcement 61-14	I.R.B. 1961-6, 85
300	Announcement 61-26	I.R.B. 1961-10, 50
301	Announcement 61-17	I.R.B. 1961-6, 85
302	Rev. Rul. 61-42	C.B. 1961-1, 751
303	Announcement 61-31	I.R.B. 1961-13, 21
304	Rev. Rul. 61-54	C.B. 1961-1, 398
305	Announcement 61-27	I.R.B. 1961-9, 91
306	Rev. Proc. 61-5	C.B. 1961-1, 891
307	Rev. Rul. 61-61	C.B. 1961-1, 492
308	Announcement 61-31	I.R.B. 1961-13, 21
309	Announcement 61-31	I.R.B. 1961-13, 21
310	Announcement 61-31	I.R.B. 1961-13, 21
311	Announcement 61-31	I.R.B. 1961-13, 21
312	Announcement 61-31	I.R.B. 1961-13, 21
313	Announcement 61-37	I.R.B. 1961-16, 52
314	Rev. Rul. 61-95	C.B. 1961-1, 749
315	Not in Bulletin.	
316	Rev. Rul. 61-101	C.B. 1961-1, 715
317	Not in Bulletin.	
318	Announcement 61-42	I.R.B. 1961-22, 26
319	Not in Bulletin.	
320	Rev. Rul. 61-129	Page 150
321	Rev. Rul. 61-134	Page 250
322	Announcement 61-57	I.R.B. 1961-29, 30
323	Announcement 61-58	I.R.B. 1961-29, 32
324	Announcement 61-56	I.R.B. 1961-29, 29
325	Announcement 61-59	I.R.B. 1961-30, 27
326	Announcement 61-66	I.R.B. 1961-31, 4
327	Announcement 61-69	I.R.B. 1961-33, 74
328	Not in Bulletin.	
329	Announcement 61-73	I.R.B. 1961-34, 36
330	Announcement 61-67	I.R.B. 1961-32, 33
331	Announcement 61-78	I.R.B. 1961-36, 34
332	Announcement 61-75	I.R.B. 1961-34, 37
333	Announcement 61-76	I.R.B. 1961-34, 38
334	Announcement 61-77	I.R.B. 1961-36, 34
335	Rev. Rul. 61-195	Page 133

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336	Rev Proc. 61-30	Page 568
337	Rev. Rul. 61-194	Page 121
338	Announcement 61-88	I.R.B. 1961-43, 21
339	Rev. Rul. 61-198	Page 61
340	Rev. Rul. 58-453, Supplement XII.	Page 41
341	Announcement 61-87	I.R.B. 1961-42, 20
342	Announcement 61-91	I.R.B. 1961-45, 67
343	Rev. Proc. 61-36	Page 575
344	Rev. Rul. 61-221	Page 34
345	Announcement 61-103	I.R.B. 1961-49, 15
346	Announcement 61-105	I.R.B. 1961-50, 13
347	Announcement 61-109	I.R.B. 1961-52, 46
348	Rev. Rul. 61-222	Page 58
349	Rev. Rul. 62-12	I.R.B. 1962-5, 38
350	Rev. Proc. 62-1	I.R.B. 1962-1, 11
351	Announcement 62-4	I.R.B. 1962-1, 17
352	Announcement 62-5	I.R.B. 1962-1, 20
353	Announcement 62-7	I.R.B. 1962-2, 15
355	Rev. Rul. 62-5	I.R.B. 1962-3, 7

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.R.R.—Committee on Appeals and Review recommendation.
A.T.—Alcohol and tobacco tax ruling.
B.T.A.—Board of Tax Appeals.
C.B.—Cumulative Bulletin.
C.F.R.—Code of Federal Regulations.
Ct. D.—Court Decision.
Del. Order—Delegation Order.
D.C.—Treasury Department circular.
E.O.—Executive Order.
E.T.—Estate and gift tax ruling.
Em. T.—Employment tax ruling.
F.A.A.A.—Federal Alcohol Administration Act.
F.R.—Federal Register.
G.C.M.—Chief Counsel's memorandum (formerly General Counsel's memorandum).
I.R.B.—Internal Revenue Bulletin.
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.
O.D.—Office Decision.
P.L.—Public Law.
P.S.—Pension, profit-sharing, stock bonus or annuity plan ruling.
Rev. Proc.—Revenue Procedure.
Rev. Rul.—Revenue Ruling.
R.S.—Revised Statute.
S.M.—Solicitor's Memorandum.
Sol. Op.—Solicitor's Opinion.
S.P.R.—Statement of Procedural Rules.
S.R.—Solicitor's Recommendation.
S.S.T.—Social Security Tax.
S.T.—Sales tax ruling.
Stat.—Statutes at Large.
T.C.—The Tax Court of the United States.
T.D.—Treasury Decision.
TIR—Technical Information Release.
U.S.C.—United States Code.
x and *y* used to represent certain numbers and when used with the word "dollars" represents sums of money.

FOREWORD

The Cumulative Bulletin is prepared in five parts, as follows:

I. Part I includes rulings and decisions which are based on the application of provisions of the Internal Revenue Code of 1954 and, unless otherwise stated in the ruling or decision, are published without consideration as to any application of the provisions of the Internal Revenue Code of 1939 or other related public laws.

II. Part II includes rulings and decisions which are based on the application of the Internal Revenue Code of 1939 and other public laws except those pertaining to the various alcohol taxes; and, unless otherwise noted therein, they are published without consideration as to any application of the provisions of the Internal Revenue Code of 1954. Part II is subdivided into two subparts according to matters issued under the Internal Revenue Code of 1939 (Subpart A) and other public laws (Subpart B).

III. Part III contains rulings and decisions pertaining to the various alcohol taxes. This part is subdivided into two subparts according to matters issued under the Internal Revenue Code of 1954 (Subpart A), and the Federal Alcohol Administration Act (Subpart B).

IV. Part IV contains treaties and tax legislation, including related Committee and Conference Reports. This part is subdivided into three subparts according to tax conventions and Treasury Decisions issued with respect thereto (Subart A), legislation (Subpart B), and Committee Reports (Subpart C). House, Senate and Conference Committee Reports printed in the Bulletin do not include the portion entitled "Changes in Existing law."

V. Part V is devoted to administrative, procedural, and miscellaneous matters. The weekly Internal Revenue Bulletins contained Part VI consisting of items of general interest; those items are not reproduced herein.

INTRODUCTION

The Internal Revenue Bulletin is the authoritative instrument of the Commissioner of Internal Revenue for the announcement of official rulings and procedures of the Internal Revenue Service, and for the publication of Treasury Decisions, Executive Orders, tax conventions, legislation, and court decisions pertaining to internal revenue matters. Other items considered to be of general interest are also published in the Bulletin, such as announcements relating to proposed regulations published with notice of proposed rulemaking, announcements relating to decisions of the Tax Court of the United States, announcements of the disbarment and suspension of attorneys and agents from practice before the Treasury Department, supplements to the Cumulative List of Organizations contributions to which are deductible under section 170 of the Internal Revenue Code of 1954, Delegation Orders, etc.

It is the policy of the Service to publish in the Bulletin all substantive and procedural rulings of importance or of 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 and statements of procedures which supersede, revoke, modify, or amend any published ruling or procedure. Except where otherwise indicated, published rulings and procedures apply retroactively. Rulings and statements of procedures relating solely to matters of internal management are not published. However, statements of internal practices and procedures affecting rights or duties of taxpayers, or industry regulation, which appear in internal management documents, are published. Revenue Rulings and Revenue Procedures are based upon rulings and internal management documents prepared in the various divisions of the National Office, including the Office of the Chief Counsel for the Internal Revenue Service. In the preparation of these, caution is exercised to conceal the identity of the taxpayer, as well as any confidential personal and business information.

Revenue Rulings and Revenue Procedures 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 that purpose. No unpublished ruling or decision will be cited or relied upon by any officer or employee of the Internal Revenue Service as a precedent in the disposition of other cases.

Since each published ruling represents the conclusion of the Service as to the application of the law to the entire state of facts involved, Service personnel and others concerned are cautioned against reaching the same conclusions in other cases unless the facts and circumstances are substantially the same. In applying rulings and procedures pub-

lished in the Bulletin, personnel of the Service and others concerned must consider the effect of subsequent legislation, regulations, court decisions, rulings and procedures.

Each published ruling is designated as a "Revenue Ruling," and each published procedure is designated as a "Revenue Procedure." These should be cited by reference to the year of issuance and the Bulletin and page where reported. Thus, Revenue Ruling No. 121 for 1961 should be cited as "Rev. Rul. 61–121, C.B. 1961–2, 65." Similarly, Revenue Procedure No. 16 for 1961 should be cited as "Rev. Proc. 61–16, C.B. 1961–2, 548." Revenue Rulings are keyed to the applicable sections of the Internal Revenue Code and regulations.

Internal Revenue Cumulative Bulletin 1961–2 contains all rulings, decisions, and procedures pertaining to Internal Revenue matters published in the weekly Internal Revenue Bulletins 27–52, inclusive, for the period July 1 to December 31, 1961. It includes an index to all matters published during the year in the weekly Bulletins and consolidated in the Cumulative Bulletins. It also contains a cumulative list of announcements relating to decisions of The Tax Court of the United States published in the Internal Revenue Bulletins.

The contents of this publication are not copyrighted and may be reprinted freely. A citation of the *Cumulative Bulletin* as the source would be appropriate.

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 JANUARY 1, 1961, TO DECEMBER 31, 1961, 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 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 decided adversely to the Government. Actions of the acquiescences in adverse decisions should be relied on by Revenue officers and others concerned as conclusions of the Service only to the application of the law to the facts in the particular case. Caution should be exercised in extending the application of the decision to a similar case unless the facts and circumstances are substantially the same, and consideration should be given to the effect of new legislation, regulations, and rulings as well as subsequent court decisions and actions thereon. Acquiescence in a decision means acceptance by the Service of the conclusion reached, and does not necessarily mean acceptance and approval of any or all of the reasons assigned by the Court for its conclusions. No announcements are made in the Bulletin with respect to memorandum opinions of The Tax Court.

The announcements published in the weekly Internal Revenue Bulletins are consolidated semiannually and annually. The semiannual consolidation appears in the first Bulletin for July and in the Cumulative Bulletin for the first half of the year and the annual consolidation appears in the first Bulletin for the following January and in the Cumulative Bulletin for the last half of the year.

The Commissioner ACQUIESCES in the following decisions:

Taxpayer	Docket No.	Report	
		Volume	Page
Alexander, Creston H., et ux	72452 79736		
Alexander, Creston H., executor of the estate Euna M. Alexander, and Clyde H. Alexander, individually Alexander, Euna M., estate of	79734	34	758
Alexander, Glenn E., et ux	72451 79737		
Arcade Realty Company, Inc	68160	35	33
Atzingen-Whitehouse Dairy, Inc	83717	36	173

ACQUIESCENCES—Continued

Taxpayer	Docket No.	Report	
		Volume	Page
Barber-Greene Americas, Inc.[3]	70334	35	365
Barber-Greene Overseas, Inc.[3]	70335		
Bartmer Automatic Self Service Laundry, Inc	64464	35	317
Baton Rouge Supply Co., Inc	71320	36	1
Bayley, John F., et ux	64616	35	288
Bialock, Harry L., et ux	72360	35	649
Blate, Jerome A., et ux	72589	34	121
Boardwalk National Bank of Atlantic City, The	70527	34	937
Boston and Maine Railroad [4]	5756	16	1517
Bradford, Eleanor A.[1]	70401	34	1059
Bradford, J. C	70400	34	1051
Briggs, Beatrice B.[1]	73242	34	1132
Bunn's Auto Sales, Inc	84453	35	861
Carasso, Max, et ux	73590	34	1139
City Federal Savings and Loan Association	67584	34	333
Coe Laboratories, Inc	50268	34	549
Colt's Manufacturing Co	59184	35	78
Cooper Agency	64669	33	709
Coppola, Samuel J., et ux [5]	77774	35	405
Cowden, Barbara Faye	66945		
Cowden, R. B	66946	34	819
Cowden, R. B., et ux	66947		
Cowley, Robert P., et ux	65397	34	333
Cronstroms, Inc	73894	36	500
Cronstroms Manufacturing, Inc	73893		
Dimit, Charles E., et ux	72453	34	758
	79735		
Dunham, Margaret G	74183	35	705
Dutcher, John W., executor of estate of Leo J. Dutcher [2]	74685	34	918
Dutcher, Leo J., estate of [2]			
Eline Realty Co	68651	35	1
Farwell, Byron H., et ux	71041		
Farwell, Felix H., et ux	71042	35	454
Farwell, Lyman H., et ux	71043		
Ferrer, Jose V.[6]	70957	35	617
First National Bank in Dallas, executor of estate of Lela Barry Vardell [2]	75855	35	50
Funk, Wilfred J., et ux	70665	35	42
Ginsberg, Donald	72469	35	1148
Graham, Donald G., et ux	77126	35	273
Grieb, Leon G	79501	36	156
Guglielmetti, John A., et ux	76118	35	668
Holt, Nat, et ux	71800	35	588
	72675		
Hoover, Reuben B., et ux	80048	35	566
Horner, Harry, et ux	79370	35	231
Kinkead, Inc., Emery	66515	35	152
Klein Chocolate Co	47164	32	437
		36	142

See footnotes at end of table.

ACQUIESCENCES—Continued

Taxpayer	Docket No.	Report Volume	Report Page
Los Angeles & Salt Lake Railroad Co.[7]	106462	4	634
Los Angeles & Salt Lake Railroad Co.[8]	15997	14	401
Loveman & Son Export Corporation, D	71711	34	776
Loveman & Son, Inc., D	71712		
Ludlow, Lewis M., et ux	77570	36	102
Lundeen, Carl W., et ux	67409	33	19
Lynch, Carl C., estate of [2]	82521	35	142
Lynch, Ella M., executrix of estate of Carl C. Lynch [2]			
Mountain Water Company of La Crescenta	71607	35	418
Muste, Abraham J	66835	35	913
Muste, Anna, estate of			
National State Bank of Newark, executor of estate of Arthur H. Squier	75848	35	950
Oregon Short Line Railroad Co.[8]	15995	14	401
Oregon-Washington Railroad & Navigation Co.[8]	15996		
Perpetual Building and Loan Association of Columbia	64575	34	694
Pollnow, Hazel W	82182	35	715
Reisner, William E., et ux	74814	34	1122
St. Joseph & Grand Island Railway Co.[8]	15994	14	401
St. Luke's Hospital, Inc.[9]	72227	35	236
Sharp, Blanche S	81820	35	1168
Squire, Arthur H., estate of	75848	35	950
Standard Lumber Co., formerly Pilot Rock Lumber Co	77900	35	192
Thornton, Helen Comb Smith	64465	35	317
Trappey, Adam S. H., et ux	73076	34	407
Union Pacific Railroad Co.[8]	106473	14	401
	111869		
	15992		
Union Pacific Railroad Co.[10]	51530	32	383
	*70183		
	70219		
United Mercantile Agencies	66537	34	808
Vardell, Lela Barry, estate of [2]	75855	35	50
Walker-Scott Corp	68946	35	34
	71606		
Wheeler's Peachtree Pharmacy, Inc	76627	35	177
Wool Distributing Corp	60841	34	323
Wusich, Nicholas D., et ux	72843	35	279

See footnotes at end of table.

The Commissioner does NOT ACQUIESCE in the following decisions:

Taxpayer	Docket No.	Report	
		Volume	Page
Acampo Winery and Distilleries, Inc.[11]	7637	7	629
Arents, Lena R., estate of [2]	65650	34	274
Dill Co	66217	33	196
Halquist, Albin C., et ux	65794 71133	33	304
Kuckenberg, Harriet, transferee	75198	35	473
Kuckenberg, Henry A., transferee	75197		
Kuckenberg, Lawrence W., transferee	75199		
Laurent, Milton P., Sr., estate of, and Ruby S. Laurent	59767 61340	34	385
Olmsted Incorporated Life Agency	78887	35	429
Rudman, Frank A., et al., independent executors of the estate of Milton P. Laurent, Sr	59767 61340	34	385
Stark, Sidney, et ux	57701	29	122
State-Adams Corp	63743	32	365
United States Trust Company of New York, et al., executors of estate of Lena R. Arents [2]	65650	34	274

[a] United States Board of Tax Appeals.

[1] Gift tax decision.

[2] Estate tax decision.

[3] Acquiescence relates only to the issue whether petitioners' income from commissions or area managers' fees was from sources outside the United States.

[4] Nonacquiescence published in C.B. 1954-1, 8, relating to the issue whether under the retirement method of accounting retirement losses deductible under section 23(l) of the Internal Revenue Code of 1939 must be reduced by pre-1913 depreciation, is withdrawn and acquiescence is substituted therefor.

[5] Acquiescence in result only. Acquiescence "in result only" means acceptance of the decision of the Court but disagreement with some or all of the reasons assigned for the decision.

[6] Acquiescence relates only to the issue whether petitioner, a cash-basis taxpayer, may elect to take as a credit in 1953 foreign taxes accrued for 1953 as well as foreign taxes for prior years paid in 1953.

[7] Nonacquiescence published in C.B. 1945, 8, is withdrawn and acquiescence is substituted therefor.

[8] Nonacquiescence published in C.B. 1950-2, 6, relating to the issue whether amounts claimed on the retirement of assets under the retirement method of accounting must be reduced by pre-1913 depreciation, is withdrawn and acquiescence is substituted therefor.

[9] Acquiescence relates only to the issue concerning the amount of accounts receivable as of December 31, 1952, which are properly excludable from the 1953 taxable income.

[10] Nonacquiescence published in C.B. XV-1, 47 (1936), and C.B. XV-2, 49 (1936), relating to the issue regarding cost of intercompany transportation of material used in construction of capital assets, is withdrawn and acquiescence is substituted therefor. Acquiescenses and nonacquiescenses in the remaining issues in this case are unchanged.

[11] Acquiescence in the issue whether the petitioner is entitled to deductions in fiscal year 1943 for the carryback of net operating losses of the two succeeding years during which the corporation was liquidating, published in C.B. 1949-1, 1, is withdrawn and nonacquiescence is substituted therefor. See Rev. Rul., 61-191, page 251, this Bulletin. Acquiescence, in the issue whether the sale of assets distributed in partial liquidation was for the shareholders or the corporation and the issue relating to the amount of the opening inventory for fiscal year 1943, published in C.B. 1949-1, 1, remains unchanged.

PART I

RULINGS AND DECISIONS UNDER THE INTERNAL REVENUE CODE OF 1954

Rulings and decisions published in Part I of the Internal Revenue Bulletin are based on the application of provisions of the Internal Revenue Code of 1954 and, unless otherwise stated in the rulings or decisions, are published without consideration as to any application of the provisions of the Internal Revenue Code of 1939 or related public laws.

SUBTITLE A.—INCOME TAXES

CHAPTER 1.—NORMAL TAXES AND SURTAXES

SUBCHAPTER A.—DETERMINATION OF TAX LIABILITY

PART IV.—CREDITS AGAINST TAX

SECTION 37.—RETIREMENT INCOME

26 CFR 1.37–4: Limitation on amount of retirement income. (Also Section 101; 1.101–4.) Rev. Rul. 61–141

For purposes of computing the retirement income credit provided by section 37(a) of the Internal Revenue Code of 1954, the retirement income of a surviving spouse need not be reduced by the amount of United States Government Life Insurance proceeds received during the taxable year, because of the death of her husband, provided the proceeds are excludable from the recipient's gross income under section 101 of the Code.

Advice has been requested whether, for purposes of computing the retirement income credit provided by section 37(a) of the Internal Revenue Code of 1954, the retirement income of a taxpayer must be reduced by the amount of United States Government Life Insurance proceeds received by the taxpayer, by reason of the death of her husband.

The taxpayer is above 65 years of age and is the beneficiary of a United States Government Life Insurance policy in the amount of $10,000 on the life of her deceased husband. Under the terms of the contract, settlement was to be made in 180 equal monthly installments. After the death of her husband, and during the taxable year in question, she received twelve monthly payments of $71 under the contract.

The above mentioned insurance contract is the only agreement under which the taxpayer received benefits by reason of the death of her husband.

Section 37 of the Code provides generally that an individual who has received retirement income (as defined by section 37(c) of the Code) during the taxable year, and who has met the eligibility requirements of section 37(b) of the Code, is entitled to a credit against the income tax imposed by chapter 1 of the Code.

Section 37(d) of the Code provides that for purposes of determining the retirement income credit under section 37(a) of the Code, the amount of retirement income shall not exceed $1,200 less, among other items, any amount received by an individual as a pension or annuity which is otherwise excluded from gross income. However, section 37(e) of the Code provides that the reduction in retirement income provided by section 37(d) of the Code shall not apply "to any amount excluded from gross income under section 101 (relating to life insurance proceeds)."

In general, section 101 of the Code provides that gross income does not include amounts received (whether in a single sum or otherwise) under a life insurance contract, if such amounts are paid by reason of the death of the insured.

Section 101(d) of the Code, relating to the payment of life insurance proceeds at a date later than death, provides that the amount of life insurance proceeds held by an insurer with respect to a beneficiary shall be prorated over the period or periods with respect to which the payments are to be made. The amount determined by such proration which is received during the taxable year shall be excluded from the gross income of the beneficiary.

If the taxpayer is a surviving spouse, there is an additional exclusion from gross income of the excess of amounts received in each taxable year under such a life insurance contract over the amount determined by proration but not more than $1,000, provided such amounts were held by an insurer under an agreement provided for in the life insurance contract to be paid on a date later than the death of the insured and were paid by reason of the death of the insured. Section 101(d)(1)(B) of the Code.

In the instant case the insurer held $10,000 with respect to the taxpayer-beneficiary. Proration of that amount as directed by section 101(d)(1)(A) of the Code over the 180 payments to which the taxpayer was entitled results in a section 101(d)(1) exclusion from gross income of $55.55 of each monthly payment of $71, or a total exclusion of $666.60 for the taxable year. In addition, since the taxpayer is the surviving spouse of the insured, she is entitled to an additional exclusion from gross income provided by section 101(d)(1)(B) of the Code of $185.40 ($71−$55.55×12) which is within the $1,000 limitation.

Since section 37(e) of the Code specifically provides that amounts which are excludable from gross income by reason of the application of section 101 of the Code are not included in those items which reduce the $1,200 limitation on retirement income as provided in section 37(d) of the Code, no reduction in the taxpayer's retirement income is required with respect to the amount of insurance proceeds received by her during the taxable year.

Accordingly, it is held that for purposes of computing the retirement income credit provided by section 37(a) of the Code, the retirement income of a surviving spouse need not be reduced by the amount of United States Government Life Insurance proceeds received during the taxable year when, as here, such proceeds are excludable from gross income under section 101 of the Code.

SUBCHAPTER B.—COMPUTATION OF TAXABLE INCOME

PART I.—DEFINITION OF GROSS INCOME, ADJUSTED GROSS INCOME, AND TAXABLE INCOME

SECTION 61.—GROSS INCOME DEFINED

26 CFR 1.61–1: Gross income. Rev. Rul. 61–185
(Also Section 451;1.451–1.)

The proceeds of an embezzlement constitute gross income to the embezzler in the year of embezzlement.

G.C.M. 24945, C.B. 1946–2, 27, revoked; and G.C.M. 16572, C.B. XV–1, 82 (1936), superseded.

The position stated in G.C.M. 24945, C.B. 1946–2, 27 has been reconsidered in the light of the decision in the case of *Eugene C. James* v. *United States*, 366 U.S. 213 (1961), Ct.D 1863, page 9, this Bulletin, handed down by the Supreme Court of the United States on May 15, 1961 .

On the authority of the Supreme Court's decision in *Commissioner* v. *Laird Wilcox, et ux.*, 327 U.S. 404 (1946), Ct.D. 1668, C.B. 1946–1, 6, G.C.M. 24945 holds that the mere act of embezzlement does not, of itself, result in taxable income to the embezzler and that taxable income to the embezzler might result, under certain circumstances, only to the extent that the injured party might condone the taking of the property and forgive the obligation to repay.

In the *James* decision, the Supreme Court expressly overruled its decision in the *Wilcox* case and held that embezzled funds are to be included in the gross income of the embezzler in the year in which the funds are embezzled.

The Internal Revenue Service will apply the *James* decision in its administration of Federal income tax law. Accordingly, G.C.M. 24945 is revoked and, since it modified G.C.M. 16572, C.B. XV–1, 82 (1936), the latter is superseded.

(Also Section 7201.) Ct. D. 1863
(Also Part II, Sections 22(a), 145; Regulations 118, Sections 39.22(a)–1, 39.145–1.)

INCOME TAX—INTERNAL REVENUE CODES OF 1939 AND 1954—DECISION OF COURT

1. Gross Income — Embezzled Funds — Tax Evasion Conviction — Embezzled Funds Not Reported As Income.

Embezzled funds are to be included in the gross income of the embezzler in the year in which the funds are misappropriated under

section 22(a) of the Internal Revenue Code of 1939 and section 61(a) of the Internal Revenue Code of 1954. *Commissioner* v. *Wilcox*, 327 U.S. 404, Ct. D. 1668, C.B. 1946-1, 6, which held that embezzled money was not taxable income, was wrongfully decided and is overruled.

However, since the rule in the *Wilcox* case was in effect at the time taxpayer, a union official, filed the returns for which he was convicted for failure to report funds embezzled from the union and an insurance company during the years 1951 to 1954, the conviction is reversed on the ground that taxpayer lacked the requisite "evil motive and want of justification" in failing to report the money. His reporting failure could not be proven willful so long as the statute contained the gloss placed upon it by *Wilcox* at the time the alleged crime was committed.

2. JUDGMENT REVERSED.

Judgment of the United States Court of Appeals for the Seventh Circuit, 273 Fed.(2d) 5, reversed, and case remanded to District Court with directions to dismiss indictment.

3. CASES CITED AND OVERRULED.

Rutkin v. *United States*, 343 U.S. 130, Ct. D. 1742, C.B. 1952-1, 9, cited

Commissioner v. *Wilcox*, 327 U.S. 404, overruled

SUPREME COURT OF THE UNITED STATES

Eugene C. James, petitioner, v. *United States*

On writ of certiorari to the United States Court of Appeals for the Seventh Circuit

[May 15, 1961.]

MR. CHIEF JUSTICE WARREN announced the judgment of the Court and an opinion in which MR. JUSTICE BRENNAN, and MR. JUSTICE STEWART concur.

The issue before us in this case is whether embezzled funds are to be included in the "gross income" of the embezzler in the year in which the funds are misappropriated under § 22(a) of the Internal Revenue Code of 1939[1] and § 61(a) of the Internal Revenue Code of 1954.[2]

The facts are not in dispute. The petitioner is a union official who, with another person, embezzled in excess of $738,000 during the years 1951 through 1954 from his employer union and from an insurance company with which the union was doing business.[3] Petitioner failed to report these amounts in his gross income in those years and was convicted for willfully attempting to evade the federal income tax due for each of the years 1951 through 1954 in violation of § 145(b) of the Internal Revenue Code of 1939[4] and § 7201 of the

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[1] § 22. Gross Income.
"(a) *General Definition.*—'Gross income' includes gains, profits, and income derived from salaries, wages, or compensation for personal service . . . of whatever kind and in whatever form paid, or from professions, vocations, trades, businesses, commerce, or sales, or dealings in property, whether real or personal, growing out of the ownership of use of or interest in such property; also from interest, rent, dividends, securities, or the transaction of any business carried on for gain or profit, or gains or profits and income derived from any source whatever. . . ." (26 U.S.C. (1952 ed.) § 22(a).)

[2] § 61. Gross Income Defined.
"(a) *General Definition.*—Except as otherwise provided in this subtitle, gross income means all income from whatever source derived. . . ." (26 U.S.C. § 61(a).)

[3] Petitioner has pleaded guilty to the offense of conspiracy to embezzle in the Court of Essex County, New Jersey.

[4] § 145. Penalties.
"(b) *Failure to Collect and Pay Over Tax, or Attempt to Defeat Tax.*—Any person required under this chapter to collect, account for, and pay over any tax imposed by this chapter, who willfully fails to collect or truthfully account for and pay over such tax, and any person who willfully attempts in any manner to evade or defeat any tax imposed by this chapter or the payment thereof, shall, in addition to other penalties provided by law, be guilty of a felony and, upon conviction thereof, be fined not more than $10,000 or imprisoned for not more than five years, or both, together with the costs of prosecution." (26 U.S.C. (1952 ed.) § 145(b).)

Internal Revenue Code of 1954.[5] He was sentenced to a total of three years imprisonment. The Court of Appeals affirmed. 273 F. 2d 5. Because of a conflict with this Court's decision in *Commissioner* v. *Wilcox*, 327 U.S. 404 [Ct. D. 1668, C.B. 1946–1, 6], a case whose relevant facts are concededly the same as those in the case now before us, we granted certiorari. 362 U.S. 974.

In *Wilcox*, the Court held that embezzled money does not constitute taxable income to the embezzler in the year of the embezzlement under § 22(a) of the Internal Revenue Code of 1939. Six years later, this Court held, in *Rutkin* v. *United States*, 343 U.S. 130 [Ct. D. 1742, C.B. 1952–1, 9], that extorted money does constitute taxable income to the extortionist in the year that the money is received under § 22(a) of the Internal Revenue Code of 1939. In *Rutkin*, the Court did not overrule *Wilcox*, but stated:

> "We do not reach in this case the factual situation involved in *Commissioner* v. *Wilcox*, 327 U.S. 404. We limit that case to its facts. There embezzled funds were held not to constitute taxable income to the embezzler under § 22(a)." *Id.*, at 138.[6]

However, examination of the reasoning used in *Rutkin* leads us inescapably to the conclusion that *Wilcox* was thoroughly devitalized.

The basis for the *Wilcox* decision was "that a taxable gain is conditioned upon (1) the presence of a claim of right to the alleged gain and (2) the absence of a definite, unconditional obligation to repay or return that which would otherwise constitute a gain. Without some bona fide legal or equitable claim, even though it be contingent or contested in nature, the taxpayer cannot be said to have received any gain or profit within the reach of § 22(a)." *Commissioner* v. *Wilcox*, *supra*, at p. 408. Since Wilcox embezzled the money, held it "without any semblance of a bona fide claim of right," *ibid.*, and therefore "was at all times under an unqualified duty and obligation to repay the money to his employer," *ibid.*, the Court found that the money embezzled was not includible within "gross income." But, Rutkin's legal claim was no greater than that of Wilcox. It was specifically found "that petitioner had no basis for his claim . . . and that he obtained it by extortion." *Rutkin* v. *United States*, *supra*, at p. 135. Both Wilcox and Rutkin obtained the money by means of a criminal act; neither had a bona fide claim of right to the funds.[7] Nor was Rutkin's obligation to repay the extorted money to the victim any less than that of Wilcox. The victim of an extortion, like the victim of an embezzlement, has a right to restitution. Furthermore, it is inconsequential that an embezzler may lack title to the sums he appropriates while an extortionist may gain a voidable title. Questions of federal income taxation are not determined by such "attenuated subleties." *Lucas* v. *Earle*, 281 U.S. 111, 114; *Corliss* v. *Bowers*, 281 U.S. 376, 378 [Ct. D. 188, C.B. IX–1, 254 (1930)]. Thus, the fact that Rutkin secured the money with the consent of his victim, *Rutkin* v. *United States*, *supra*, at p. 138, is irrelevant. Likewise unimportant is the fact that the sufferer of an extortion is less likely to seek restitution than one whose funds are embezzled. What is important is that the right to recoupment exists in both situations.

Examination of the relevant cases in the courts of appeals lends credence to our conclusion that the *Wilcox* rationale was effectively vitiated by this Court's

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[5] § 7201. Attempt to Evade or Defeat Tax.
"Any person who willfully attempts in any manner to evade or defeat any tax imposed by this title or the payment thereof shall, in addition to other penalties provided by law, be guilty of a felony and, upon conviction thereof, shall be fined not more than $10,000 or imprisoned not more than 5 years, or both, together with the costs of prosecution." (26 U.S.C. § 7201.)

[6] The dissenters in *Rutkin* stated that the Court had rejected the *Wilcox* interpretation of § 22(a). *Id.*, at 140.

[7] The Government contends that the adoption in *Wilcox* of a claim of right test as a touchstone of taxability had no support in the prior cases of this Court; that the claim of right test was a doctrine invoked by the Court in aid of the concept of annual accounting, to determine *when*, not *whether*, receipts constituted income. See *North American Oil Co.* v. *Burnet*, 286 U.S. 417 [Ct. D. 499, C.B. XI–1, 293 (1932)]; *United States* v. *Lewis*, 340 U.S. 590 [Ct. D. 1738, C.B. 1951–1, 21]; *Healy* v. *Commissioner*, 345 U.S. 278 [Ct. D. 1756, C.B. 1953–1, 68]. In view of our reasoning set forth below, we need not pass on this contention. The use to which we put the claim of right test here is only to demonstrate that, whatever its validity as a test of *whether* certain receipts constitute income, it calls for no distinction between *Wilcox* and *Rutkin*.

decision in *Rutkin*.[8] Although this case appears to be the first to arise that is "on all fours" with *Wilcox*, the lower federal courts, in deference to the undisturbed *Wilcox* holding, have earnestly endeavored to find distinguishing facts in the cases before them which would enable them to include sundry unlawful gains within "gross income."[9]

It had been a well-established principle, long before either *Rutkin* or *Wilcox*, that unlawful, as well as lawful, gains are comprehended within the term "gross income." Section II B of the Income Tax Act of 1913 provided that "the net income of a taxable person shall include gains, profits, and income . . . from . . . the transaction of any *lawful* business carried on for gain or profit, or gains or profits and income derived from any source whatever. . . ." (Emphasis supplied.) 38 Stat. 167. When the statute was amended in 1916, the one word "lawful" was omitted. This revealed, we think, the obvious intent of that Congress to tax income derived from both legal and illegal sources, to remove the incongruity of having the gains of the honest laborer taxed and the gains of the dishonest immune. *Rutkin* v. *United States*, *supra*, at p. 138; *United States* v. *Sullivan*, 274 U.S. 259, 263 [T.D. 4028, C.B. VI–2, 177 (1927)]. Thereafter, the Court held that gains from illicit traffic in liquor are includible within "gross income." *Ibid.* See also *Johnson* v. *United States*, 318 U.S. 189 [Ct. D. 1576, C.B. 1943, 1042]; *United States* v. *Johnson*, 319 U.S. 503. And, the Court has pointed out, with approval, that "there has been a widespread and settled administrative and judicial recognition of the taxability of unlawful gains of many kinds," *Rutkin* v. *United States*, *supra*, at p. 137. These include protection payments made to racketeers, ransom payments paid to kidnappers, bribes, money derived from the sale of unlawful insurance policies, graft, black market gains, funds obtained from the operation of lotteries, income from race track bookmaking and illegal prize fight pictures. *Ibid.*

The starting point in all cases dealing with the question of the scope of what is included in "gross income" begins with the basic premise that the purpose of Congress was "to use the full measure of its taxing power." *Helvering* v. *Clifford*, 309 U.S. 331, 334 [Ct. D. 1444, C.B. 1940–1, 105]. And the Court has given a liberal construction to the broad phraseology of the "gross income" definition statutes in recognition of the intention of Congress to tax all gains except those specifically exempted. *Commissioner* v. *Jacobson*, 336 U.S. 28, 49 [Ct. D. 1712, C.B. 1949–1, 40]; *Helvering* v. *Stockholms Enskilda Bank*, 293 U.S. 84, 87–91 [Ct. D. 887, C.B. XIII–2, 299 (1934)]. The language of § 22(a) of the 1939 Code, "gains or profits and income derived from any source whatever," and the more simplified language of § 61 (a) of the 1954 Code, "all income from whatever source derived," has been held to encompass all "accessions to wealth, clearly realized, and over which the taxpayers have complete dominion." *Commissioner* v. *Glenshaw Glass Co.*, 348 U. S. 426, 431 [Ct. D. 1783, C.B. 1955–1, 207]. A gain "constitutes taxable income when its recipient has such control over it that, as a practical matter, he derives readily realizable economic value from it." *Rutkin* v. *United States*, *supra*, at p. 137. Under these broad principles, we believe that petitioner's contention, that all unlawful gains are taxable except those resulting from embezzlement, should fail.

When a taxpayer acquires earnings, lawfully or unlawfully, without the consensual recognition, express or implied, of an obligation to repay and without restriction as to their disposition, "he has received income which he is required

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[8] In *Marienfeld* v. *United States*, 214 F. 2d 632, the Eighth Circuit stated, "We find it difficult to reconcile the Wilcox case with the later opinion of the Supreme Court in Rutkin. . . ." *Id.*, at 636. The Second Circuit announced, in *United States* v. *Bruswitz*, 219 F. 2d 59, "It is difficult to perceive what, if anything, is left of the Wilcox holding after Rutkin. . . ." *Id.*, at 61. The Seventh Circuit's prior decision in *Macias* v. *Commissioner*, 255 F. 2d 23, observed, "If this reasoning [of *Rutkin*] had been employed in Wilcox, we see no escape from the conclusion that the decision in that case would have been different. In our view, the Court in Rutkin repudiated its holding in Wilcox; certainly it repudiated the reasoning by which the result was reached in that case." *Id.*, at 26.

[9] For example, *Kann* v. *Commissioner*, 210 F. 2d 247, was differentiated on the following grounds: the taxpayer was never indicted or convicted of embezzlement; there was no adequate proof that the victim did not forgive the misappropriation; the taxpayer was financially able to both pay the income tax and make restitution; the taxpayer would have likely received most of the misappropriated money as dividends. In *Marienfeld* v. *United States*, *supra*, the court believed that the victim was not likely to repudiate. In *United States* v. *Wyss*, 239 F. 2d 658, the distinguishing factors were that the district judge had not found as a fact that the taxpayer embezzled the funds and the money had not as yet been reclaimed by the victim. See also *Briggs* v. *United States*, 214 F. 2d 699, 702; *Prokop* v. *Commissioner*, 254 F. 2d 544, 554–555. Cf. *J. J. Dix, Inc.* v. *Commissioner*, 223 F. 2d 436.

to return, even though it may still be claimed that he is not entitled to retain the money, and even though he may still be adjudged liable to restore its equivalent." *North American Oil* v. *Burnet*, *supra*, at p. 424. In such case, the taxpayer has "actual command over the property taxed—the actual benefit for which the tax is paid," *Corliss* v. *Bowers*, *supra*. This standard brings wrongful appropriations within the broad sweep of "gross income"; it excludes loans. When a law-abiding taxpayer mistakenly receives income in one year, which receipt is assailed and found to be invalid in a subsequent year, the taxpayer must nonetheless report the amount as "gross income" in the year received. *United States* v. *Lewis*, *supra*; *Healy* v. *Commissioner*, *supra*. We do not believe that Congress intended to treat a law-breaking taxpayer differently. Just as the honest taxpayer may deduct any amount repaid in the year in which the repayment is made, the Government points out that, "if, when, and to the extent that the victim recovers back the misappropriated funds, there is of course a reduction in the embezzler's income. Brief for the United States, p. 24.[10]

Petitioner contends that the *Wilcox* rule has been in existence since 1946; that if Congress had intended to change the rule, it would have done so; that there was a general revision of the income tax laws in 1954 without mention of the rule; that a bill to change it[11] was introduced in the Eighty-sixth Congress but was not acted upon; that, therefore, we may not change the rule now. But the fact that Congress has remained silent or has re-enacted a statute which we have construed, or that congressional attempts to amend a rule announced by this Court have failed do not necessarily debar us from re-examining and correcting the Court's own errors. *Girouard* v. *United States*, 328 U.S. 61, 69–70; *Helvering* v. *Hallock*, 309 U.S. 106, 119–122. There may have been any number of reasons why Congress acted as it did. *Helvering* v. *Hallock*, *supra*. One of the reasons could well be our subsequent decision in *Rutkin* which has been thought by many to have repudiated *Wilcox*. Particularly might this be true in light of the decisions of the Courts of Appeals which have been riding a narrow rail between the two cases and further distinguishing them to the disparagement of *Wilcox*. See notes 8 and 9, *supra*.

We believe that *Wilcox* was wrongly decided and we find nothing in congressional history since then to persuade us that Congress intended to legislate the rule. Thus, we believe that we should now correct the error and the confusion resulting from it, certainly if we do so in a manner that will not prejudice those who might have relied on it. Cf. *Helvering* v. *Hallock*, *supra*, at 119. We should not continue to confound confusion, particularly when the result would be to perpetuate the injustice of relieving embezzlers of the duty of paying income taxes on the money they enrich themselves with through theft while honest people pay their taxes on every conceivable type of income.

But, we are dealing here with a felony conviction under statutes which require that petitioner "willfully" fails to account for his tax or that he "willfully" attempts to evade his obligation. In *Spies* v. *United States*, 317 U.S. 492, 499 [Ct. D. 1571, C.B. 1943, 1038], the Court said that § 145(b) of the 1939 Code embodied "the gravest of offenses against the revenues," and stated that willfulness must therefore include an evil motive and want of justification in view of all the circumstances. *Id.*, at 498. Willfulness "involves a specific intent which must be proven by independent evidence and which cannot be inferred from the mere understatement of income." *Holland* v. *United States*, 348 U.S. 121, 139 [Ct. D. 1769, C.B. 1954–2, 215].

We believe that the element of willfulness could not be proven in a criminal prosecution for failing to include embezzled funds in gross income in the year of misappropriation so long as the statute contained the gloss placed upon it by *Wilcox* at the time the alleged crime was committed. Therefore, we feel that petitioner's conviction may not stand and that the indictment against him must be dismissed.

Since MR. JUSTICE HARLAN, MR. JUSTICE FRANKFURTER, and MR. JUSTICE CLARK agree with us concerning *Wilcox*, that case is overruled. MR. JUSTICE BLACK, MR.

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[10] Petitioner urges upon us the case of *Alison* v. *United States*, 344 U.S. 167 [Ct. D. 1754, C.B. 1953–1, 39]. But, that case dealt with the right of the victim of an embezzlement to take a deduction, under § 23 (e) and (f) of the 1939 Code, in the year of the discovery of the embezzlement rather than the year in which the embezzlement occurred. The Court held only "that the special factual circumstances found by the District Courts in both these cases justify deductions under I.R.C. § 23 (e) and (f) and the long-standing Treasury Regulations applicable to embezzlement losses." *Id.*, at 170. The question of inclusion of embezzled funds in "gross income" was not presented in *Alison*.

[11] H.R. 8854, 86th Cong., 1st Sess.

JUSTICE DOUGLAS, and MR JUSTICE WHITTAKER believe that petitioner's conviction must be reversed and the case dismissed for the reasons stated in their opinions.

Accordingly, the judgment of the Court of Appeals is reversed and the case is remanded to the District Court with directions to dismiss the indictment.

It is so ordered.

MR. JUSTICE BLACK, whom MR. JUSTICE DOUGLAS joins, concurring in part and dissenting in part.

MR. JUSTICE CLARK, concurring in part and dissenting in part as to the opinion of THE CHIEF JUSTICE.

MR. JUSTICE HARLAN, whom MR. JUSTICE FRANKFURTER joins, concurring in part and dissenting in part as to the opinion of THE CHIEF JUSTICE.

MR. JUSTICE WHITTAKER, whom MR. JUSTICE BLACK and MR. JUSTICE DOUGLAS join, concurring in part and dissenting in part.

Treatment of pay received by a member of the armed forces while attending a university to satisfy the residence requirements for a college degree. See Rev. Rul. 61–133, page 35.

Strike and lockout benefit payments made to workers by a labor union. See Rev. Rul. 61–136, page 20.

The amount of a reimbursement to an employee by his employer for a premium paid to an insurer for medical and hospital insurance is excludable from gross income. See Rev. Rul. 61–146, page 25.

A gain on recoveries which previously had been deducted for Federal income tax purposes. See Rev. Rul. 61–214, page 60.

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26 CFR 1.61–2: Compensation for services, including fees, commissions, and similar items.

Amounts received by individuals for services performed incident to a research project involving methods of teaching ninth grade algebra supported by a grant under Title VII of the National Defense Education Act of 1958. See Rev. Rul. 61–174, page 28.

PART II.—ITEMS SPECIFICALLY INCLUDED IN GROSS INCOME

SECTION 71.—ALIMONY AND SEPARATE MAINTENANCE PAYMENTS

26 CFR 1.71–1: Alimony and separate maintenance payments; income to wife or former wife.

Treatment of alimony payments and payments for support of children. See Ct. D. 1862, page 24.

SECTION 72.—ANNUITIES: CERTAIN PROCEEDS OF ENDOWMENT AND LIFE INSURANCE CONTRACTS

26 CFR 1.72–11: Amounts not received as annuity payments.

Loss sustained upon the original purchaser's surrender of a single premium refund annuity contract for a cash consideration. See Rev. Rul. 61–201, page 46.

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26 CFR 1.72–15: Applicability of section 72 to accident or health plans. (Also Section 101; 1.101–2.) Rev. Rul. 61–161

A United States Civil Service employee retired because of a disability and subsequently died before reaching "retirement age." The employee elected to receive a smaller monthly payment under a joint and survivor's annuity option, in order that his spouse might receive an annuity if he predeceases her. After his death the employee's widow and children under 18 years of age began receiving annuity benefits. *Held*, the widow and children are primary annuitants and the employee death benefit exclusion provided by section 101(b) of the Internal Revenue Code of 1954 is applicable to the benefits payable. The amount of the exclusion constitutes additional consideration paid for the annuity for purposes of section 72 of the Code.

Advice has been requested whether the employee death benefit exclusion provided by section 101(b) of the Internal Revenue Code of 1954 is applicable to a joint and survivor annuity benefit where the employee, retired on disability, died before attaining "retirement age."

A United States Civil Service employee retired, under the provisions of the Civil Service Retirement Act, 46 Stat. 468, 5 U.S.C. 691, because of disability before attaining "retirement age" as defined in Revenue Ruling 57–76, C.B. 1957–1, 66, as modified by Revenue Ruling 61–6, C.B. 1961–1, 15. Under a joint and survivor annuity option, he elected to receive smaller monthly payments in order that his surviving wife might receive benefits if he predeceases her. He died before reaching "retirement age." After his death his widow began receiving annuity benefits in accordance with the joint and survivor annuity option, and the children, under 18 years of age, began receiving temporary life annuity benefits under separate provisions of the Act.

Section 101(b)(1) of the Code provides that amounts received by the beneficiary or the estate of an employee shall be excluded from gross income if such amounts are paid by or on behalf of an employer and are paid by reason of the death of the employee. Section 101(b)(2) limits the amount of such exclusion to $5,000 in the aggregate. However, section 101(b)(2)(C) of the Code states that amounts received by a surviving annuitant, under a joint and survivor's annuity contract, after the first day of the first period for which an amount was received as an annuity by the employee, do not qualify for the death benefit exclusion.

Section 101(b)(2)(D) of the Code provides that, in the case of any amount to which section 72 (relating to annuities, etc.) applies, the amount which is excludable under section 101(b)(1) shall be de-

termined by reference to the value of such amount as of the day on which the employee died, and shall, for purposes of section 72, be treated as additional consideration paid by the employee.

Where accident or health benefits are attributable to employer contributions under an employer-established plan which provides for payment of pensions at retirement and the payment of an earlier pension in the event of permanent disability, section 1.72–15(d) of the Income Tax Regulations provides, in part, that the amounts of such benefits are includible in gross income except to the extent that such amounts are excludable from gross income under section 105(d) of the Code and the regulations thereunder. In this connection, section 1.105–4(a)(3)(i) of the regulations states that the exclusion from gross income allowed by section 105(d) of the Code applies only to amounts attributable to periods during which the employee would be at work were it not for the disability. Thus, an employee is not absent from work if he is not expected to work because, for example, he has reached retirement age. If a plan provides that an employee, who is absent from work on account of personal injury or sickness, will receive a disability pension for as long as he is disabled, the exclusion under section 105(d) is applicable to any payments which such an employee receives under the plan before he reaches retirement age but such exclusion is not applicable to the payments which such an employee receives after reaching retirement age.

Section 1.72–15(c)(2) of the regulations provides, in part, that in the case of an employer-established contributary pension plan (as here involved), it will be presumed that the disability pension is provided by employer contributions, unless the plan expressly provides otherwise. The Civil Service Retirement Act does not expressly provide that any portion of a disability pension is provided in whole or in part by employee contributions. Consequently, the amount of the employee's contribution to the retirement fund is not reduced by the amount of disability pension previously received by the disabled employee.

In view of the foregoing, it is apparent that prior to reaching "retirement age" the payments received by the retired employee, in the instant case, did not constitute an annuity within the concept of section 72 of the Code, but were disability payments, excludable from gross income as "sick pay" to the extent provided by section 105(d) of the Code. Consequently, the annuity payments made to the widow and children, by reason of the employee's death which occurred before the retired employee had reached "retirement age," constitute payments to primary annuitants rather than payments to secondary annuitants under a joint and survivor annuity contract.

In view of the foregoing, it is held that where, under the United States Civil Service Retirement System, an employee who has elected to receive a joint and survivor annuity benefit retires on account of disability and dies before reaching retirement age, the widow and children (if any) are considered to be primary beneficiaries in applying the rules of sections 72 and 101(b) of the Code.

Accordingly, the death benefit exclusion provided by section 101(b) of the Code is applicable to the benefits payable to the widow and children, limited to (1) $5,000 or (2) the excess of the total present value of the annuities over the amount to which the employee had

a nonforfeitable right, whichever is the lesser. The amount of such an exclusion constitutes additional consideration paid for the annuity by the employee for purposes of computing excludable amounts under section 72 of the Code. See section 101(b)(2)(D) of the Code.

PART III.—ITEMS SPECIFICALLY EXCLUDED FROM GROSS INCOME

SECTION 101.—CERTAIN DEATH BENEFITS

26 CFR 1.101–1: Exclusion from gross income of proceeds of life insurance contracts payable by reason of death.

Proceeds of insurance on the life of an officer of a closely held corporation paid directly to shareholders of the corporation. See Rev. Rul. 61–134, page 250.

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26 CFR 1.101–2: Employee's death benefits.

Applicability of death benefit exclusion to joint and survivor annuity benefits payable to a widow and to the separate benefits of children of deceased employee who had retired on account of disability and died prior to attaining "retirement age." See Rev. Rul. 61–161, page 15.

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26 CFR 1.101–3: Interest payments. T. D. 6577 [1]

TITLE 26—INTERNAL REVENUE.—CHAPTER I, SUBCHAPTER A, PART 1.—INCOME TAX; TAXABLE YEARS BEGINNING AFTER DECEMBER 31, 1953

Amendment of the Income Tax Regulations under section 101 of the Internal Revenue Code of 1954 to provide rules for the taxation of amounts received under family income riders.

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

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

On April 7, 1961, notice of proposed rulemaking regarding amendment of the Income Tax Regulations under section 101 of the Internal Revenue Code of 1954 to provide rules for the taxation of amounts received under family income riders was published in the Federal Register (26 F.R. 2987). After consideration of all such relevant matter as was presented by interested persons regarding the rules proposed, the following regulations are hereby adopted.

PARAGRAPH 1. Paragraph (a) of § 1.101–3 is amended to read as follows:

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[1] The publication of this Treasury Decision in 26 F.R. 10127, dated October 28, 1961, contains (1) instructions for modifying the notice of proposed rulemaking in 26 F.R. 2987, dated April 7, 1961, and (2) the full context of the regulations with such modifications. As here published, the Treasury Decision reflects the full context of such regulations, with modifications. The individual instructions have been omitted.

§ 1.101–3 INTEREST PAYMENTS.—(a) *Applicability of section 101(c).*—Section 101(c) provides that if any amount excluded from gross income by section 101(a) (relating to life insurance proceeds) or section 101(b) (relating to employees' death benefits) is held under an agreement to pay interest thereon, the interest payments shall be included in gross income. This provision applies to payments made (either by an insurer or by or on behalf of an employer) of interest earned on any amount so excluded from gross income which is held without substantial diminution of the principal amount during the period when such interest payments are being made or credited to the beneficiaries or estate of the insured or the employee. For example, if a monthly payment is $100, of which $99 represents interests and $1 represent diminution of the principal amount, the principal amount shall be considered held under an agreement to pay interest thereon and the interest payment shall be included in the gross income of the recipient. Section 101(c) applies whether the election to have an amount held under an agreement to pay interest thereon is made by the insured or employee or by his beneficiaries or estate, and whether or not an interest rate is explicitly stated in the agreement. Section 101(d), relating to the payment of life insurance proceeds at a date later than death, shall not apply to any amount to which section 101(c) applies. See section 101(d)(4). However, both section 101(c) and section 101(d) may apply to payments received under a single life insurance contract. For provisions relating to the application of this rule to payments received under a permanent life insurance policy with a family income rider attached, see paragraph (h) of § 1.101–4.

PAR. 2. Paragraph (h) of § 1.101–4 is amended to read as follows:

§ 1.101–4 PAYMENT OF LIFE INSURANCE PROCEEDS AT A DATE LATER THAN DEATH.

* * * * * * *

(h) *Applicability of both section 101(c) and 101(d) to payments under a single life insurance contract.*—(1) *In general.* Section 101(d) shall not apply to interest payments on any amount held by an insurer under an agreement to pay interest thereon (see sections 101(c) and 101(d)(4) and § 1.101–3). On the other hand, both section 101(c) and section 101(d) may be applicable to payments received under a single life insurance contract, if such payments consist both of interest on an amount held by an insurer under an agreement to pay interest thereon and of amounts held by the insurer and paid on a date or dates later than the death of the insured. One instance when both section 101(c) and section 101(d) may be applicable to payments received under a single life insurance contract is in the case of a permanent life insurance policy with a family income rider attached. A typical family income rider is one which provides additional term insurance coverage for a specified number of years from the register date of the basic policy. Under the policy with such a rider, if the insured dies an any time during the term period, the beneficiary is entitled to receive (i) monthly payments of a specified amount commencing as of the date of death and continuing for the balance of the term period, and (ii) a lump sum payment of the proceeds under the basic policy to be paid at the end of the term period. If the insured dies after the expiration of the term period, the beneficiary receives only the proceeds under the basic policy. If the insured dies before the expiration of the term period, part of each monthly payment received by the beneficiary during the term period consists of interest on the proceeds of the basic policy (such proceeds being retained by the insurer until the end of the term period). The remaining part consists of an installment (principal plus interest) of the proceeds of the term insurance purchased under the family income rider. The amount of term insurance which is provided under the family income rider is, therefore, that amount which, at the date of the insured's death, will provide proceeds sufficient to fund such remaining part of each monthly payment. Since the proceeds under the basic policy are held by the insurer until the end of the term period, that portion of each monthly payment which consists of interest on such proceeds is interest on an amount held by an insurer under an agreement to pay interest thereon and is includible in gross income under section 101(c). On the other hand, since the remaining portion of each monthly payment consists of an installment payment (principal plus interest) of the proceeds of the term insurance, it is a payment of an amount held by the insurer and paid on a date later than the death of the insured to which section 101(d) and this section applies

(including the $1,000 exclusion allowed the surviving spouse under section 101(d)(1)(B). The proceeds of the basic policy, when received in a lump sum at the end of the term period, are excludable from gross income under section 101(a).

(2) *Example of tax treatment of amounts received under a family income rider.* The following example illustrates the application of the principles contained in subparagraph (1) of this paragraph to payments received under a permanent life insurance policy with a family income rider attached:

Example. The sole life insurance policy of the insured provides for the payment of $100,000 to the beneficiary (the insured's spouse) on his death. In addition, there is attached to the policy a family income rider which provides that, if the insured dies before the 20th anniversary of the basic policy, the beneficiary shall receive (i) monthly payments of $1,000 commencing on the date of the insured's death and ending with the payment prior to the 20th anniversary of the basic policy, and (ii) a single payment of $100,000 payable on the 20th anniversary of the basic policy. On the date of the insured's death, the beneficiary (surviving spouse of the insured) is entitled to 36 monthly payments of $1,000 and to the single payment of $100,000 on the 20th anniversary of the basic policy. The value of the proceeds of the term insurance at the date of the insured's death is $28,409.00 (the present value of the portion of the monthly payments to which section 101(d) applies computed on the basis that the interest rate used by the insurer in determining the benefits to be paid under the contract is 2¼ percent). The amount of each monthly payment of $1,000 which is includible in the beneficiary's gross income is determined in the following manner:

(*a*) Total amount of monthly payment	$1,000.00
(*b*) Amount includible in gross income under section 101(c) as interest on the $100,000 proceeds under the basic policy held by the insurer until 20th anniversary of the basic policy (computed on the basis that the interest rate used by the insurer in determining the benefits to be paid under the contract is 2¼ percent)	185.00
(*c*) Amount to which section 101(d) applies ((*a*) minus (*b*))	815.00
(*d*) Amount excludable from gross income under section 101(d) ($28,409 ÷ 36)	789.14
(*e*) Amount includible in gross income under section 101(d) without taking into account the $1,000 exclusion allowed the beneficiary as the surviving spouse ((*c*) minus (*d*))	25.86

The beneficiary, as the surviving spouse of the insured, is entitled to exclude the amounts otherwise includible in gross income under section 101(d) (item (*e*)) to the extent such amounts do not exceed $1,000 in the taxable year of receipt. This exclusion is not applicable, however, with respect to the amount of each payment which is includible in gross income under section 101(c) (item (*b*)). In this example, therefore, the beneficiary must include $185 of each monthly payment in gross income (amount includible under section 101(c)), but may exclude the $25.86 which is otherwise includible under section 101(d). The payment of $100,000 which is payable to the beneficiary on the 20th anniversary of the basic policy will be entirely excludable from gross income under section 101(a).

(3) *Limitation on amount considered to be an "amount held by an insurer".*—See paragraph (b)(3) of this section for a limitation on the amount which shall be considered an "amount held by an insurer" in the case of proceeds of life insurance which are paid subsequent to the transfer of the policy for a valuable consideration.

(4) *Effective date.*—The provisions of this paragraph are applicable only with respect to amounts received during taxable years beginning after October 28, 1961, irrespective of the date of the death of the insured.

PAR. 3. Paragraph (a) of § 1.101–6 is amended to read as follows:

§ 1.101–6 EFFECTIVE DATE.—(a) Except as otherwise provided in paragraph (h)(4) of § 1.101–4, the provisions of section 101 of the Internal Revenue Code of 1954 and §§ 1.101–1, 1.101–2, 1.101–3, 1.101–4, and 1.101–5 are applicable only with respect to amounts received by reason of the death of an insured or an employee occurring after August 16, 1954. In the case of such amounts, these sections are applicable even though the receipt of such amounts occurred in a

taxable year beginning before January 1, 1954, to which the Internal Revenue Code of 1939 applies.

(This Treasury Decision is issued under the authority contained in section 7805 of the Internal Revenue Code of 1954 (68A Stat. 917; 26 U.S.C. 7805).)

BERTRAND M. HARDING,
Acting Commissioner of Internal Revenue.

Approved October 24, 1961.

STANLEY S. SURREY,
Assistant Secretary of the Treasury.

(Filed by the Division of the Federal Register for October 27, 1961, 8:47 a.m., and published in the issue of the Federal Register for October 28, 1961, 36 F.R. 10127)

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26 CFR 1.101–4: Payment of life insurance proceeds at a date later than death.

Effect upon retirement income of amounts received by the beneficiary of a life insurance policy. See Rev. Rul. 61–141, page 7.

SECTION 102.—GIFTS AND INHERITANCES

26 CFR 1.102–1: Gifts and inheritances. (Also Section 61; 1.61–1.) Rev. Rul. 61–136

In cases presenting facts substantially like those presented in *United States* v. *Allen Kaiser*, strike benefit payments and lockout benefit payments made by labor unions will be regarded as gifts and, therefore, excludable from the gross incomes of the recipients. Other cases will be scrutinized to determine whether the payments constitute gross income for Federal income tax purposes. However, the fact that benefits are paid only to union members will not, in and of itself, be considered a determinative factor.

O.D. 552, C.B. 2, 73 (1920); Revenue Ruling 57–1, C.B. 1957–1, 15; Revenue Ruling 58–139, C.B. 1958–1, 14, modified; and Revenue Ruling 61–16, C.B. 1961–1, 13, superseded.

Reconsideration has been given to O.D. 552, C.B. 2, 73 (1920), and Revenue Ruling 57–1, C.B. 1957–1, 15, relating to strike benefit payments, and Revenue Ruling 58–139, C.B. 1958–1, 14, relating to lockout benefit payments, in the light of the decision of the Supreme Court of the United States in *United States* v. *Allen Kaiser*, 363 U.S. 299 (1960), Ct. D. 1851, C.B. 1960–2, 33.

O.D. 552 holds that benefits received from labor unions by individuals while on strike are to be included in their gross incomes for Federal income tax purposes.

Revenue Ruling 57–1 holds that strike benefit payments made by a labor union to unemployed members, as well as nonmembers, as the result of a labor strike are includible in the gross incomes of the recipients in the year received even though distributed on the basis of need and irrespective of the nature and form of the benefit payments received.

Revenue Ruling 58–139 holds that lockout benefit payments are includible in the gross incomes of the recipients under the principles

applicable to strike benefit payments. Therefore, any change in the tax treatment of strike benefit payments affects the tax treatment of lockout benefit payments.

In the *Kaiser* case a labor union furnished strike benefits, by way of room rent and food vouchers, to a needy worker participating in a strike although he was not a member of the union during the early period of the strike. The Supreme Court held that, on consideration of all of the circumstances presented, the jury in the lower court acted within its province in concluding that the strike benefits were gifts within the meaning of section 102(a) of the Internal Revenue Code of 1954 and, hence, were not includible in the worker's gross income. Emphasizing that the question in such cases is essentially a factual one to be resolved by the trier of facts, the Supreme Court noted that the lower court had taken into account such factors as the form and the amount of the benefits, the conditions of personal need, the lack of other sources of income, and the availability of public assistance.

In view of the foregoing, it is held that in cases presenting facts substantially like those in the *Kaiser* case, strike benefit payments will be regarded as gifts and, therefore, exempt from Federal income tax. Other cases will be scrutinized to determine whether the payments constitute gross income for Federal income tax purposes. However, the fact that benefits are paid only to union members will not, in and of itself, be considered determinative of whether such benefits will be regarded as gifts or as gross income.

O.D. 552, C.B. 2, 73 (1920), Revenue Ruling 57–1, C.B. 1957–1, 15, and Revenue Ruling 58–139, C.B. 1958–1, 14, are hereby modified to the extent that they hold that strike benefit payments and lockout benefit payments are includible in the gross income of the recipient irrespective of the circumstances under which such payments are made.

Revenue Ruling 61–16, C.B. 1961–1, 13, is superseded.

SECTION 103.—INTEREST ON CERTAIN GOVERNMENTAL OBLIGATIONS

26 CFR 1.103–1: Interest upon obligations of a State, Territory, etc. — Rev. Rul. 61–145

Turnpike revenue bonds issued by the Department of Highways of the Commonwealth of Kentucky, under chapter 177 of the Kentucky Revised Statutes, constitute obligations of a political subdivision of the State within the meaning of section 103(a) of the Internal Revenue Code of 1954. Accordingly, interest from such bonds is excludable from gross income for Federal income tax purposes. See Rev. Rul. 55–76, C.B. 1955–1, 239.

Rev. Rul. 61–181

So-called "dividends" paid on Los Angeles Metropolitan Transit Authority Equipment Trust Certificates, Series A, are excludable from the gross income of the recipient as interest on the obligations of a political subdivision of a State within the meaning of section 103(a)(1) of the Internal Revenue Code of 1954.

Advice has been requested whether so-called "dividends" paid on Los Angeles Metropolitan Transit Authority Equipment Trust Cer-

tificates, Series A, are excludable from the gross income of the recipient as interest upon obligations of a political subdivision of a State.

The Los Angeles Metropolitan Transit Authority was created by the Los Angeles Metropolitan Transit Authority Act of 1957, Chapter 547 of the Statutes of California, 1957, as a public corporation of the State of California. The term "public corporation" as it is used in the Act means any county, city and county, city, town, municipal corporation, district of any kind or class, authority, or political subdivision of the State. The Authority, composed of seven members appointed by the Governor of California, was created to acquire or construct, establish, develop, and operate a mass rapid transit system for the county of Los Angeles. For this purpose it has the power of eminent domain, but has no power to levy taxes. Funds of the Authority may be deposited in such banks in the State of California as may be authorized to receive deposits of public funds and its funds may be invested only in accordance with the general laws of the State relating to investments of county funds.

Section 4.13 of the Act provides, in part, as follows:

> * * * The authority may acquire rolling stock or other property under conditional sales contracts, leases, equipment trust certificates, or any other form of contracts, leases, equipment trust certificates, or any other form of contract or trust agreement. * * *

The Authority and a trust and savings association, as trustee, entered into an "Equipment Trust Agreement" by the terms of which the trustee issued trust certificates maturing serially over a period of eight years and bearing "dividends" at the rate of four and one-half percent per annum. The agreement provides, moreover, that the trustee will hold title to the equipment and lease the same to the Authority until the principal, dividends and trust expenses have been paid in full. In addition, it stipulates that payments of principal and dividends are payable solely from a portion of the revenues which is derived by the Authority from the operation of the transit system and paid over by the Authority to the trustee as rental for the use of the equipment. The payments characterized as "rent" are to be sufficient to pay, among other things, the necessary and reasonable expenses of the trust including compensation of the trustee, and the amounts of dividends appurtenant to the trust certificates as well as the principal thereof when and as the same shall become payable. At the termination of the lease and after all payments due or to become due from the Authority have been made to the trustee, any moneys remaining in the hands of the trustee after providing for all outstanding trust certificates and dividends and after payment of the expenses of the trustee, including its reasonable compensation, are to be paid to the Authority. Each certificate carries with it the Authority's guaranty for the payment of principal and dividends, but this obligation is limited to the revenues derived from operating the transit system of the Authority.

Section 103 of the Internal Revenue Code of 1954 provides, in part, as follows:

> (a) * * * Gross income does not include interest on * * *
> (1) the obligations of a State, * * * or a possession of the United States, or any political subdivision of any of the foregoing, or of the District of Columbia; * * *.

Section 1.103–1 of the Income Tax Regulations explains that the term "political subdivision" denotes "any division of the State, * * * or possession of the United States * * * to which has been delegated the right to exercise part of the sovereign power of the State * * *" and that obligations issued on behalf of such a political subdivision are considered the obligations of the political subdivision.

The Authority, a public corporation of the State of California, has been delegated certain sovereign powers of the State by the legislature of California to enable it to furnish mass transportation in Los Angeles County. These political powers have been limited only with reference to the purpose for which the Authority was created. Although the nominal issuer of the equipment trust certificates is the trustee, the obligations of the trustee are ministerial and the real obligor is the Authority. The trustee, moreover, is not liable for making any payments except out of the amounts received by it from the Authority as rent on the equipment. The guaranty of payment on each certificate is primarily the obligation of the Authority and not of the trustee.

It is clear from the foregoing that the certificates are issued on behalf of the Authority and constitute obligations of a political subdivision of the State. Although called "dividends," the amounts received by the certificate holders are in reality interest, being computed as, and otherwise having all the characteristics of, interest.

Accordingly, it is held that dividends paid on Los Angeles Metropolitan Transit Authority Equipment Trust Certificates, Series A, are excludable from the gross income of the recipient as interest on the obligations of a political subdivision of a State within the meaning of section 103(a)(1) of the Code.

SECTION 105.—AMOUNTS RECEIVED UNDER ACCIDENT AND HEALTH PLANS

26 CFR 1.105–4: Wage continuation plans. Rev. Rul. 61–192

> The "sick pay" exclusion provided under section 105(d) of the Internal Revenue Code of 1954, relating to wage continuation plans, may be allowable to an individual employee even though he has passed normal "retirement age," provided he is regularly employed and would be at work if it were not for a personal injury or sickness.

Advice has been requested whether the "sick pay" exclusion provided under section 105(d) of the Internal Revenue Code of 1954 is allowable to an individual who has passed the normal "retirement age," under the circumstances described.

In the instant case, *A* at age 75, an employee of a company for many years, was injured as he left his place of employment. Until the accident, *A* had enjoyed good health and worked regularly. He was absent from work for eight months, during which time he performed no services for his employer. Pursuant to a written agreement, *A* continued to receive his regular salary during this period. Other employees in *A*'s age group had similar arrangements with the company. At the end of the eight month period, *A* returned to work.

Normal retirement age under the company's pension plan is 65 years, although retirement at that age is not compulsory. *A* and certain other employees were not covered by the regular pension plan because of their advanced ages. It is the company's practice, in consideration of loyal and faithful service, to retain such employees regardless of age, so long as they are able to work regularly.

Section 105(a) of the Code provides that, except as otherwise provided in section 105 of the Code, amounts received by an employee through accident or health insurance for personal injuries or sickness shall be included in gross income to the extent such amounts are attributable to contributions by the employer which were not includible in the gross income of the employee or are paid by the employer.

Section 105(d) of the Code provides that within certain limitations gross income does not include amounts referred to in section 105(a) if such amounts constitute wages, or payments in lieu of wages, for a period during which the employee is absent from work on account of personal injuries or sickness.

Section 1.105–4(a) of the Income Tax Regulations provides, in part, as follows:

* * * (1) Subject to the limitations provided in this section, section 105(d) provides an exclusion from gross income with respect to amounts referred to in section 105(a) which are paid to an employee through a wage continuation plan and which constitute wages or payments in lieu of wages for a period during which the employee is absent from work on account of personal injuries or sickness.

(2)(i) Section 105(d) is applicable only if the wages or payments in lieu of wages are paid pursuant to a wage continuation plan. The term "wage continuation plan" means an accident or health plan, as defined in section 1.105–5, under which wages, or payments in lieu of wages, are paid to an employee for a period during which he is absent from work on account of a personal injury or sickness. * * *.

(ii) Section 105(d) is applicable if, and only if, the employee is absent from work and such absence is due to a personal injury or sickness. * * *.

(3)(i) Section 105(d) applies only to amounts attributable to periods during which the employee would be at work were it not for a personal injury or sickness. Thus, an employee is not absent from work if he is not expected to work because, for example, he has reached retirement age. If a plan provides that an employee, who is absent from work on account of personal injury or sickness, will receive a disability pension as long as he is disabled, section 105(d) is applicable to any payments which such an employee receives under this plan before he reaches retirement age, but section 105(d) does not apply to the payments which such an employee receives after he reaches retirement age.

Section 1.105–5 of the regulations states in part that, in general, an accident or health plan is an arrangement for the payment of amounts to employees in the event of personal injuries or sickness. A plan may cover one or more employees, and there may be different plans for different employees or classes of employees.

Clearly, an individual who has not retired should not be denied the benefits of section 105(d) solely because he has passed the normal retirement age established under his employer's pension or retirement plan. For instance, if an employee who has reached normal retirement age does not retire, but continues his employment, and if he thereafter becomes sick or is injured so that he is unable to work for a certain period of time, following which he returns to work, it is obvious that he "is expected to work" and has been "absent from work"

within the meaning of section 1.105–4(a)(3)(i) of the regulations in spite of the fact that he is beyond the normal retirement age. The references to "retirement age" in section 1.105–4(a)(3)(i) of the regulations were intended primarily to establish the point at which an individual actually retired on disability, and receiving disability pension payments, would cease to receive the benefits of section 105(d).

Accordingly, in the circumstances of this case, it is held that *A* is entitled to exclude from gross income, to the extent provided by section 105(d) of the Code, the salary or wages that he received from his employer during the eight month period of his absence from work on account of personal injury.

SECTION 106.—CONTRIBUTIONS BY EMPLOYER TO ACCIDENT AND HEALTH PLANS

26 CFR 1.106–1: Contributions by employer to accident and health plans. (Also Section 61; 1.61–1.) Rev. Rul. 61–146

Reimbursements by an employer to his employees for his share of premiums for hospital and medical insurance for them may be considered as contributions by the employer to accident or health plans for his employees so as to result in the exclusion of such payments from the gross income of the employees under section 106 of the Internal Revenue Code of 1954.

Revenue Ruling 57–33, C.B. 1957–1, 303, distinguished.

Advice has been requested whether amounts paid by an employer, under the circumstances below, as his share of premiums for hospital and medical insurance for his employees are excludable from the gross income of the employees under section 106 of the Internal Revenue Code of 1954.

In the instant case, the employer pays a share of the premiums for hospital and medical insurance for his employees. For those employees who are covered by a group policy through their employment, the employer pays his share of the premium directly to the insurance company. For those employees who are not covered by the employer's group policy but have other types of hospital and medical insurance for which they pay the premiums directly to the insurers, the employer pays a part of such premiums upon proof that the insurance is in force and is being paid for by the employees.

To facilitate payment of his share of the premiums paid directly by the employees to the insurers, the employer uses the following methods:

(1) reimburses each employee directly once or twice a year for the employer's share of the insurance premiums upon proof of prior payment of the premiums by the employee;

(2) issues to each employee a check payable to the particular employee's insurance company, the employee being obligated to turn over the check to the insurance company; or

(3) issues a check as in method (2) except the check is made payable jointly to the insurance company and the employee.

Section 106 of the Code provides that gross income does not include

contributions by the employer to accident or health plans for compensation (through insurance or otherwise) to his employees for personal injuries or sickness.

Section 1.106–1 of the Income Tax Regulations provides that the employer may contribute to an accident or health plan either by paying the premium (or a portion of the premium) on a policy of accident or health insurance covering one or more of his employees, or by contributing to a separate trust or fund, which provides accident or health benefits directly or through insurance to one or more of his employees.

In this case it is clear that in method (2) the employer is actually paying accident or health insurance premiums directly to the insurer of the particular employee, utilizing the employee as his agent for the delivery of the checks to the insurer. Method (3) is not substantially different, inasmuch as the employee there is obligated to turn the checks over to the insurer and can in no event divert the payments to other uses. Although method (1) involves direct payment to the employee, in practical effect it does not differ from methods (2) or (3), since proof is required by the employer that hospital and medical insurance is in force for the employee and that premiums for the period involved have been paid by the employee and because the employer's payment is stated to be in reimbursement for the employer's share of the insurance premiums.

Under the circumstances of this case, it is held that the amounts paid by the employer under methods (2) or (3) above constitute payments of premium or portions of premiums on policies of accident or health insurance covering one or more employees within the meaning of section 1.106–1 of the regulations. Similarly, the payments under method (1) constitute employer payments of accident or health insurance premiums for employees if the payments are shown to be in reimbursement of premiums actually paid by the employees to the insurers. Accordingly, amounts paid as above are excludable from the gross income of the employees under section 106 of the Code.

Revenue Ruling 57–33, C.B. 1957–1, 303, holds that certain weekly payments made by employers direct to employees, pursuant to a union contract of employment, for the purpose of purchasing individual hospitalization and surgical insurance coverage, are "wages" for Federal employment tax purposes and are includible in the gross income of the employees.

Under the facts in that case, the employers had no accident or health plan of their own in effect and, with respect to the payments which they made direct to the employees, did not require an accounting either by the employees or the employees' union that the funds were expended in the acquisition of insurance coverage. Revenue Ruling 57–33, accordingly, is distinguishable from the instant case.

SECTION 107.—RENTAL VALUE OF PARSONAGES

26 CFR 1.107–1: Rental value of parsonages. Rev. Rul. 61–213

An individual who performs the duties of a "Cantor" at a Jewish Community Center is not entitled to exclude the portion of his remuneration received as a rental allowance from his gross income under section 107 of the Internal Revenue Code of 1954, where he is not an ordained minister of the gospel.

Advice has been requested whether an individual who is employed as a "Cantor" at a Jewish Community Center is entitled to exclude from his gross income the part of his compensation which is paid to him as a rental allowance to the extent such amount is expended to provide himself with a home.

The taxpayer in the instant case is employed as a "Cantor" by a Jewish Community Center. He has not been ordained by any theological seminary. His duties require him to lead the worship at all religious services conducted at the Center and to officiate as Cantor at weddings, at funerals, and at the naming of children in the Synagogue. A portion of the compensation paid to the individual is paid to him as a rental allowance to provide him with a home.

Section 107 of the Internal Revenue Code of 1954 provides that in the case of a minister of the gospel, gross income does not include the rental value of a home furnished to him as part of his compensation; or the rental allowance paid to him as part of his compensation to the extent used by him to rent or provide a home.

Section 1.107–1(a) of the Income Tax Regulations provides, in part, that in order to qualify for the exclusion, the home or rental allowance must be provided as remuneration for services which are ordinarily the duties of a minister of the gospel and that, in general, the rules provided in section 1.1402(c)–1(e) of the regulations will be applicable to such determination.

The regulations state that whether services performed by a minister constitute the conduct of religious worship or the ministration of sacerdotal functions depends on the tenets and practices of the particular religious body constituting his church or church denomination. Section 1.1402(c)–1(e)(ii)(a) of the regulations.

The scope of the phrase "minister of the gospel" as used in section 107 of the Code has been interpreted as meaning an "individual who is a duly ordained, commissioned, or licensed minister of a church." See Revenue Ruling 59–270, C.B. 1959–2, 44, and the authorities cited therein, in which it was held that neither a "minister of music" nor a "minister of education" was entitled to exclude the rental value of a dwelling house or a rental allowance from gross income where neither of them was an ordained minister of the gospel.

That holding may be contrasted with the position taken in Revenue Ruling 58–221, C.B. 1958–1, 53, where an exclusion under section 107 of the Code was permitted to an individual who was employed at a Jewish Community Center and Temple and whose duties constituted the conduct of religious worship or the ministration of sacerdotal functions according to the tenets and practices of the Jewish faith. The individual concerned, however, had been ordained by a theological seminary.

Notwithstanding the nature of the duties and services performed by the instant taxpayer as a "Cantor," he was not an ordained, commissioned, or licensed minister of the gospel as required by the term "minister of the gospel" as used in section 107 of the Code.

Accordingly, it is held that the instant taxpayer is not entitled to exclude any amount from his gross income under section 107 of the Code because he was not a "minister of the gospel" within the meaning of that term as used in the Code.

SECTION 117.—SCHOLARSHIPS AND FELLOWSHIP GRANTS

26 CFR 1.117–4: Items not considered as scholarships or fellowship grants. (Also Section 61; 1.61–2.) Rev. Rul. 61–174

Amounts received by persons providing services in connection with a research project supported by a grant made under Title VII of the National Defense Education Act of 1958 are not excludable from the gross income of the recipients as amounts received as scholarships or fellowship grants under section 117(a) of the Internal Revenue Code of 1954. Such amounts are compensation for services rendered and are includible in the gross income of the recipients.

Advice has been requested whether amounts received by individuals in connection with a research project designed to develop and evaluate an individualized approach to the teaching of ninth-grade algebra, which is supported by a grant under Title VII of the National Defense Education Act of 1958, are excludable from the gross income of the recipients as scholarships or fellowship grants under section 117(a) of the Internal Revenue Code of 1954.

After submitting an application, a college was awarded a financial grant by the United States Office of Education under Title VII of the National Defense Education Act of 1958, 20 U.S.C. 541–563 (1958 Edition). The grant was made for the purpose of aiding the college in conducting a research project designed to develop and evaluate an individualized approach to the teaching of ninth-grade algebra by means of a variety of perceptual devices and techniques in use in communications media. The project required the services of a number of individuals on a part-time basis and was expected to take approximately two and one-half years for its completion.

The staff of the project was composed of a chief investigator, a project director and certain clerical personnel. In addition, ten ninth-grade algebra teachers employed in areas surrounding the grantee college had agreed to cooperate in the project by teaching classes using the experimental approach, methods and devices developed by project personnel. The teachers attended a six-week summer institute where they determined the materials to be covered in the experimental classes, familiarized themselves with the method to be used and contributed to the design and construction of various devices to be employed.

Members of the project staff were paid from project funds according to the time actually devoted to project activities. The ten coop-

erating teachers, however, received payment from the granted funds only while attending the six-week summer institute. During the regular school year, they were paid by their respective employing school authorities.

In the proposed budget submitted by the college with its grant application, the college referred to the amounts to be paid to the project staff and cooperating teachers as "salaries." Under the conditions of the grant, such amounts were based upon the rates of pay normally paid for the same or similar services. The funds granted included an amount to cover the expenses of employee insurance, pension payments, and Federal employment taxes, as well as travel allowances.

Section 117(a) of the Code provides generally that, in the case of an individual, gross income does not include amounts received as a scholarship at an educational institution, or as a fellowship grant. However, section 1.117–4(c) of the Income Tax Regulations provides, in part, that amounts paid as compensation for services, either past, present or future, and amounts paid for services which are primarily for the benefit of the grantor, are not considered as amounts received as scholarships or fellowship grants for the purposes of section 117 of the Code.

In the instant case, there is no indication that the amounts paid by the college out of granted funds were regarded by either the college or the recipients as scholarships or fellowship grants. However, there is ample evidence that the payments were made to the recipients in return for services performed which advanced the progress of the project. That such was the intention of the college is clearly indicated by the reference made in the grant application to the amounts concerned as "salaries." Although it is possible that some of the individuals engaged in project activities increased their professional abilities and skills, there is nothing to suggest that any such benefit was anything more than an incidental result of association with the project. There is no indication that the education or training of project personnel was the primary or even an important aim of the college when it made the payments. All the facts and circumstances support a conclusion that the amounts were both paid and received as compensation for services.

Such services included both the direct staff duties performed by some individuals and the training undergone by the cooperating teachers during the summer institute.

In circumstances similar to those in the instant case, it has been held that amounts received by teachers instructing students in mathematics using experimental text material produced by a group supported by the National Science Foundation were compensation for services which was includible in the gross income of the recipients. See Revenue Ruling 60–274, C.B. 1960–2, 39. The same principle is applicable in the instant case.

Accordingly, it is held that the amounts received by the abovementioned project staff members and by teachers cooperating in the project were compensation for services and not received by them as scholarships or fellowship grants within the meaning of section 117(a) of the Code. Such amounts are, therefore, includible in the gross income of the recipients under section 61(a) of the Code.

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PART V.—DEDUCTIONS FOR PERSONAL EXEMPTIONS

SECTION 151.—ALLOWANCE OF DEDUCTIONS FOR PERSONAL EXEMPTIONS

26 CFR 1.151–2: Additional exemptions for dependents. Rev. Rul. 61–186
(Also Section 152;1.152–1.)

Where a state institution for the mentally retarded, or division thereof, which qualifies as an educational institution under section 151(e)(4) of the Internal Revenue Code of 1954, accepts a minor child for purposes of education and training and certifies that it is making an effort to educate or train him to use his faculties to the extent that he is physically or mentally able to do so, the child will qualify as a "student" under section 151(e)(4) of the Code, regardless of the education or training received or the extent of his disability. If such certification is made, the amounts expended by the institution for the room, board and tuition of the child will be considered a scholarship which will not be taken into account in determining whether such child received more than one-half of its support from its parent for the purpose of determining exemption for dependents for Federal income tax purposes.

Revenue Ruling 60–190, C.B. 1960–1, 51, modified.

Advice has been requested whether amounts expended by a state mental institution for the room, board and tuition of handicapped children under the circumstances described below should be taken into account in determining whether the children qualify as dependents of their parents for Federal income tax purposes.

A state maintains an institution which specializes in the care, treatment, education and training of minor children who are severely handicapped, both physically and mentally. The institution provides free room, board and tuition to the children while they are in residence. The parents of the children pay for all other expenses, including those for clothing, medical care, incidental expenses and transportation to and from the institution. Because of the extent of their handicaps, the children reside at the institution most of the year.

In connection with the education and training of the children, a division of the institution, which qualifies as an educational institution under section 151(e)(4) of the Internal Revenue Code of 1954, conducts formal classes which are attended by those children who are physically and mentally able to do so. However, some of the children are so severely handicapped, both physically and mentally, that they cannot attend the formal classes. The educational division attempts to train the children in this latter group to the limit of their capacities in such areas as self-help, personal hygiene and occupational activities.

Revenue Ruling 59–379, C.B. 1959–2, 51, holds that amounts expended by a state for the training and education of handicapped children should not be taken into account in determining whether such children receive more than one-half of their support from the parent for the purpose of determining exemption for dependents for Federal income tax purposes. However, Revenue Ruling 60–190, C.B. 1960–1, 51, holds that Revenue Ruling 59–379 is not applicable to any residents of state institutions for mentally retarded children unless the state institution qualifies as an educational institution and such residents

qualify as students, that is, they are enrolled in and attend regularly the classes which comprise the curriculum of the institution.

Upon reconsideration of Revenue Ruling 60–190, it is concluded that that portion thereof which holds, in effect, that only those mentally retarded children who are enrolled in and attending regularly the classes which comprise the curriculum of the state institution may qualify as students for purposes of the special support test set forth in section 152(d) of the Code is unduly restrictive in cases where certain of the mentally retarded children are too severly handicapped to take part in the formal classes of the institution, or division therof, but who are, nevertheless, receiving education or training commensurate with their physical or mental capacities as a part of the educational curriculum of the qualified institution or division.

Accordingly, it is held that where a state institution for the mentally retarded, or division thereof, which qualifies as an educational institution under section 151(e)(4) of the Code, accepts a minor child for purposes of education and training and certifies that it is making an effort to educate or train him to use his faculties to the extent that he is physically or mentally able to do so, the child will qualify as a student under section 151(e)(4) of the Code, regardless of the education or training received or the extent of his disability. If such certification is made, the amounts expended by the institution for the room, board and tuition of the child will be considered a scholarship grant which will not be taken into account in determining whether such child received more than one-half of its support from its parent for the purpose of determining exemption for dependents for Federal income tax purposes.

Revenue Ruling 60–190, *supra*, is modified to remove the implication that only those mentally retarded children who are enrolled in and attending regularly the classes which comprise the curriculum of the qualified state institution may qualify as students for purposes of the special support test set forth in section 152(d) of the Code.

SECTION 152.—DEPENDENT DEFINED

26 CFR 1.152–1: General definition of a dependent.

Handicapped child residing in a state mental institution. See Rev. Rul. 61–186, page 30.

PART VI.—ITEMIZED DEDUCTIONS FOR INDIVIDUALS AND CORPORATIONS

SECTION 162.—TRADE OR BUSINESS EXPENSES

26 CFR 1.162–1: Business expenses. Rev. Rul. 61–210

Amounts paid by a taxpayer for years beginning on and after January 1, 1952, as penalties for failure to make timely payment of mercantile taxes imposed by the City of Pittsburgh and the School District of Pittsburgh are not deductible.

Advice has been requested whether, in view of the decision in the case of *Keystone Metal Company* v. *Commissioner*, 264 Fed. (2d) 561

(1959), the amount paid by a taxpayer as a penalty for failure to make timely payment of the mercantile license tax levied by the City of Pittsburgh and the School District of Pittsburgh is deductible.

In 1947, the Pennsylvania School Mercantile License Tax Act, Title 24, section 582.1 to 582.13, Public Law 745, dated June 20, 1947, authorized the School District of Pittsburgh to levy and collect a mercantile tax effective January 1, 1948. Pursuant to that authority the School District imposed such a tax on all sales made by firms situated therein. The City of Pittsburgh by ordinance imposed a similar tax.

Both the City and the School District promulgated regulations governing the administration of the mercantile tax. Contained in the regulations adopted by each in 1947 was a provision which stated generally that if the tax was not paid when due interest thereon would be charged in the amount of six percent per annum. It was also provided that a "penalty" of one percent of the amount remaining unpaid would be added and collected for each month, or fraction thereof, during which the tax due remained outstanding.

The regulations were amended in each case, effective January 1, 1952, to provide that a taxpayer who disputed the validity or amount of the tax alleged to be due was entitled to pay the tax "under protest" and obtain a refund if it was later judicially determined that an overpayment had been made. Prior to the adoption of that amendment, a taxpayer disputing liability for the tax was required to subject himself to the risk of the "penalty" for failure to pay the tax when due, because payment of the tax extinguished the right of a taxpayer to contest his liability for it.

The mercantile tax provisions of both the City and the School District of Pittsburgh imposed a higher rate of tax upon transactions made at retail than those made at wholesale.

The taxpayer in the instant case is a Pennsylvania corporation which, during the period in question, maintained its principal place of business in the City of Pittsburgh. It is engaged in the business of selling various industrial supplies. During the year 1957, after an examination of the taxpayer's business records, the City of Pittsburgh notified the taxpayer that it had failed to pay the proper amount of mercantile taxes for the years 1953 through 1956. It was asserted by the City that the taxpayer had erroneously reported a number of sales made during those years as having been made at wholesale, when under prevailing State law such sales should have been reported as retail transactions. The taxpayer, in 1957, paid the amount of taxes asserted to be due, the interest owing thereon and the "penalty" imposed for late payment of such taxes. The taxpayer deducted all three items on its 1957 Federal income tax return as an ordinary and necessary business expense.

Section 162(a) of the Code provides that there shall be allowed as a deduction all the ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business. That is not to say, however, that all expenses attributable to business activity are deductible.

Deduction of expenses, the allowance of which would frustrate sharply defined national or state policies, has been denied. See *Tank Truck Rentals, Inc.* v. *Commissioner*, 356 U.S. 30 (1958), Ct. D. 1819, C.B. 1958–1, 502, and *Hoover Motor Express Co.* v. *United States*,

356 U.S. 38 (1958), Ct. D. 1820, C.B. 1958–1, 505, and companion cases, in which the deduction of amounts paid as fines by a trucking operator for violation of state maximum weight laws was disallowed.

The reasoning behind the rule denying a deduction for statutory penalties is that a penalty is a punitive measure inflicted upon those who violate expressed law or regulation and that to permit a tax advantage by allowance of a deduction of a penalty for such a violation results in a mitigation of the punishment and, thus, serves to frustrate the purpose and effectiveness of public policy. See *Commissioner* v. *Longhorn Portland Cement Co.*, 148 Fed. (2d) 276 (1945), certiorari denied, 326 U.S. 728, Ct.D. 1665, C.B. 1946–1, 53; I.T. 1174, C.B. I–1, 269 (1922); S.R. 1448, C.B. IV–1, 140 (1923), and *Great Northern Ry. Co.* v. *Commissioner*, 40 Fed. (2d) 372 (1930), certiorari denied, 282 U.S. 855.

In the case of *Keystone Metal Company* v. *Commissioner*, 264 Fed. (2d) 561 (1959), the United States Court of Appeals for the Third Circuit reversed the Tax Court of the United States and permitted the deduction of amounts paid by a taxpayer as penalties, like those in the instant case, for failure to make timely payment of mercantile taxes to the City of Pittsburgh and the School District of Pittsburgh for the year 1948. Under the local taxing regulations, as then constituted, the taxpayer who paid such taxes, liability for which he disputed, lost his right to contest the issue by making payment. Thus, in order to contest the question of liability the taxpayer was required to subject himself to the risk of being penalized for late payment if he lost in a later judicial determination.

The United States Court of Appeals took that fact into consideration and, in weighing the effect of allowing a deduction to the taxpayer for the penalty, noted that the Pennsylvania State Supreme Court in sustaining the penalty earlier had "clearly indicated that it is not the policy of Pennsylvania to prevent or deter a taxpayer from postponing the payment of a tax beyond the due date where such delay is necessary for a bona fide test of a doubtful question as to the validity or applicability of the tax." The court cited the case of *Keystone Metal Co.* v. *City of Pittsburgh*, 374 Pa. 323 (1953), 97 A. 2d 797, certiorari denied, 346 U.S. 887, rehearing denied, 346 U.S. 917.

The circumstances surrounding the imposition of a penalty upon the instant taxpayer are materially different from those in the Keystone Metal Company case. Here, the tax liability arose in the years 1953 through 1956, years in which the taxpayer was able to preserve its right to contest the taxes claimed to be due by paying the taxes "under protest" and, thus, avoid the penalty imposed for late payment. No reasonable ground is evident upon which an exception to the general rule that statutory penalties are not deductible may be based. The penalties here involved are clearly an expression of the policy of the City of Pittsburgh directed toward the discouragement of late payment of taxes. Allowance of a deduction for those penalties would mitigate their severity and thus reduce in some degree the effectiveness of the measures adopted to assure the prompt collection of revenue.

Accordingly, it is held, that the amounts paid by the instant taxpayer as penalties for the late payment of mercantile license taxes to the City of Pittsburgh and the School District of Pittsburgh are not

deductible under section 162(a) of the Code as ordinary and necessary expenses of carrying on a trade or business, or under any other provision of the Code.

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26 CFR 1.162–2: Traveling expenses. Rev. Rul. 61–221 [1]

The Internal Revenue Service will follow the recent decision of the United States Court of Appeals for the Fifth Circuit in *F. M. Williams* v. *George D. Patterson*, 286 Fed. (2d) 333 (1961).

The issue in that case was whether a railroad conductor who was assigned to regularly scheduled trains running between his home terminal in Montgomery, Alabama, and Atlanta, Georgia, and whose round trips usually required a 16-hour absence from Montgomery and included a six-hour layover in Atlanta—during which he habitually ate two meals and rented a hotel room where he slept and bathed before starting his return trip—could deduct the cost of such meals, lodging and tips as traveling "away from home" expenses under section 162(a)(2) of the Internal Revenue Code of 1954.

The Service had contended that the taxpayer was not away from home on such trips because they were not "overnight" trips, as that term is explained in Revenue Ruling 54–497, C.B. 1954–2, 75, at 78–79, for the reason that Williams' trips did not necessitate his absence from his home terminal for a minimum period which lasted substantially longer than an ordinary days' work and during which his duties required him to obtain necessary sleep in Atlanta.

The court concluded, however, that Williams had satisfied the dual test prescribed by the Service since his 16-hour absence on such round trips (including one hour for discharging his duties before leaving, and after returning to, his home terminal) was substantially longer than an ordinary workday, and it was reasonably necessary for Williams to sleep during his layover in order to carry out his assignment, even though there was no statute, regulation or railroad order requiring him to sleep and rest prior to his return run.

The Service agrees with the court in interpreting Revenue Ruling 54–497 as allowing the deduction in this case and concurs in general with the court's understanding that the "correct rule" governing the deductibility of such expenses is as follows:

> If the nature of the taxpayer's employment is such that when away from home, during released time, it is reasonable for him to need and to obtain sleep or rest in order to meet the exigencies of his employment or business demands of his employment, his expenditures (including incidental expenses, such as tips) for the purpose of obtaining sleep or rest are deductible traveling expenses under section 162(a)(2) of the 1954 Code.

However, the Service does not consider the brief interval during which an employee may be released from duty for the purpose of eating rather than sleeping as constituting an adequate rest period to satisfy the "overnight" rule as a test for the deductibility of meal expenses on business trips completed within one day. See *Sam J. Herrin, et ux.* v. *Commissioner*, 28 T.C. 1303(1957); and *Allan L. Hanson, et ux.* v. *Commissioner*, 35 T.C. 413(1960).

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[1] Based on Technical Information Release 344, dated November 2, 1961.

26 CFR 1.162–5: Expenses for education. Rev. Rul. 61–133
(Also Sections 61, 262; 1.61–1, 1.262–1.)

The expenses incurred by an Army captain, an instructor in the gunnery department of an Army artillery school, in taking courses in psychology, public administration, foreign relations, history, government, and photography while meeting the residence requirements of a university in order to obtain a degree, under a plan authorized by Army Regulations No. 621–5, as amended, are not expenditures for education of the type described in section 1.162–5(a) of the Income Tax Regulations and are not deductible under section 162 of the Internal Revenue Code of 1954. Such expenses are nondeductible personal expenses. The regular pay received by the officer while attending the university is includible in his gross income.

Advice has been requested concerning (1) the deductibility as expenditures for education, for Federal income tax purposes, of the expenses incurred by an Army captain, an instructor in the gunnery department of an Army artillery school, while attending a university under the General Educational Development program established under and authorized by Army Regulations No. 621–5, as amended, and (2) the treatment of the regular pay received by the Army captain while attending the university.

The goal of the General Educational Development program as provided in Army Regulations No. 621–5, as amended, as far as commissioned personnel are concerned, is the completion of programmed college level studies in subject areas of functional importance to the military profession.

To enable selected officers to satisfy the traditional residence requirement for the baccalaureate or higher degree of accredited civilian colleges and universities, a "final semester plan" has been established. Under the plan the officer must be able to obtain the degree through residence at a university or college within one semester or two quarters. He must agree to remain on active duty for four years subsequent to such schooling and agree to bear all expenses incurred in connection with such schooling, including tuition, fees, books, and travel. While in attendance at the university, an officer-participant in the plan continues to receive his regular authorized pay.

In the instant case, pursuant to Army Regulations No. 621–5, as amended, the Army captain applied for and was granted permission to attend a university in order to obtain a baccalaureate degree. While there, he took courses in psychology, public administration, foreign relations, history, government, and photography; he received his regular authorized pay; and he paid all of his expenses for books, tuition, etc.

Section 162(a) of the Internal Revenue Code of 1954 provides for the deduction of all the ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business.

Section 1.162–5(a) of the Income Tax Regulations provides, in pertinent part, that expenditures made by a taxpayer for his education are deductible if they are for education undertaken primarily for the purpose of (1) maintaining or improving skills required by the taxpayer in his employment or other trade or business, or (2) meeting the express requirements of a taxpayer's employer imposed as a condition to the retention by the taxpayer of his salary, status, or employment.

A study of Army Regulations No. 621–5, as amended, discloses that the educational goals established by the education and training program for various groups are merely desired levels and do not represent increased educational requirements.

Thus, the expenses incurred by the Army captain in the instant case in attending the university were not undertaken pursuant to any requirement of the taxpayer's employer imposed as a condition to the retention by the taxpayer of his salary, status, or employment within the meaning of section 1.162–5(a)(2) of the regulations.

Neither do the expenses relate to education undertaken for the purpose of maintaining or improving skills required by the taxpayer in his employment within the meaning of section 1.162–5(a)(1) of the regulations. There is no evidence to the effect that it is customary for other established Army officers to undertake education of the type entered into by the officer in the instant case and it has not otherwise been shown that the courses in psychology, public administration, foreign relations, history, government, and photography are so closely related to this officer's duties as to maintain or improve his needed skills.

Accordingly, it is held that the expenses incurred by the Army officer under the above described circumstance are not deductible under section 162 of the Code, but, rather, are personal expenses not deductible by reason of section 262 of the Code. Further, the regular pay he received while attending the university is includible in his gross income, the consideration therefor being, among other things, his agreement to remain on active duty with the Armed Forces for a specified period of time.

The principles expressed in this ruling are equally applicable to members of other branches of the Armed Forces who attend a university or college to obtain a degree under similar programs.

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26 CFR 1.162–9: Bonuses to employees. Rev. Rul. 61–127
(Also Section 461; 1.461–1.)

Bonuses, under a plan whereby the employer, using the accrual method of accounting, is obligated to pay to its employees at least two percent but not more than three percent of the company's profits for a taxable year, but under which the exact percentage cannot be determined until after the close of such year, are accruable and allowable as a deduction only to the extent of two percent of the company's profit for such year, subject to the test of "reasonableness." The portion of the bonuses paid in the following taxable year in excess of the minimum two percent are deductible in that year to the extent that such bonuses constitute reasonable compensation for services rendered.

Revenue Ruling 55–446, C.B. 1955–2, 531, modified.

Advice has been requested regarding the amount of bonuses which may be accrued and deducted in a taxable year by an employer under the circumstances described below.

For many years the taxpayer, employing the accrual method of accounting, has paid bonuses to its administrative employees. The bonuses were paid in March or April based upon the profits for the previous taxable year ending January 31. Previously, the taxpayer issued bonus letters to each eligible employee before the end of the

taxable year notifying him of the percentage of the total bonuses to be awarded to him, pursuant to Revenue Ruling 55–446, C.B. 1955–2, 531.

That ruling holds, in part, that bonuses are accruable and deductible for the taxable year to which they relate, provided the taxpayer has obligated himself prior to the end of the taxable year to pay the bonuses, by delivery to each employee concerned a written or oral notice of the percentage of the total award he is entitled to receive.

In order to reduce the cost of preparing letters to each employee specifying his or her percentage share of the bonus fund, the taxpayer adopted a new bonus plan for its administrative employees. The plan provides that bonuses shall be paid not later than April 15 of the following fiscal year, in an aggregate amount of not less than two percent nor more than three percent of the company's profits for the taxable year just ended, with certain adjustments not here material. The plan further provides that the bonuses will be paid only to those administrative employees who are on the payroll on the last day of the taxable year and who otherwise qualify under the terms of the plan. Continued employment after the end of the taxable year is not required under the plan, nor is payment of the bonus to the employee otherwise conditional. The taxpayer communicated the terms of the plan to the administrative employees as a group prior to the close of the taxable year. Under the plan, the percentage of the bonus fund in excess of two percent cannot be determined until after the close of the taxable year.

Section 162(a) of the Internal Revenue Code of 1954 provides, in part, that there shall be allowed as a deduction 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.

Section 461(a) of the Code provides the general rule for determining the taxable year in which allowable deductions should be taken. Section 1.461–1(a)(2) of the Income Tax Regulations provides, in part, that under an accrual method of accounting, an expense is deductible for the taxable year in which all the events have occurred which determine the fact of the liability and the amount thereof can be determined with reasonable accuracy.

Under the above stated facts, there was a minimum amount payable to the employees qualifying under the taxpayer's bonus plan, which amount was determinable by means of a formula in effect prior to the end of the taxable year. Since the terms of the plan were communicated to the employees involved before the end of the taxable year, in view of the foregoing facts, an obligation arose to pay at least the minimum amount of bonuses which could have been enforced by the employees involved. Thus, all the events had occurred prior to the end of the taxable year in question which determined the fact and the minimum amount (two percent of the profits) of the taxpayer's liability under the bonus plan.

Accordingly, it is held that the bonuses based on two percent of the company's "profits" are accruable and deductible for Federal income tax purposes for the year to which they relate, subject to the test of "reasonableness" under section 162 of the Code. How-

ever, since the taxpayer is not legally obligated prior to the close of the taxable year to pay an amount in excess of two percent of the "profits," any excess is deductible only in the following taxable year, provided the amounts so paid meet the "reasonableness" test.

Revenue Ruling 55–446, C.B. 1955–2, 531, is modified to the extent that it may be interpreted as requiring delivery of an individual notice to each employee of the percentage of the total amount accrued as bonuses to which he is entitled in order to properly deduct the payments under section 162 of the Code.

The instant ruling has no bearing on situations such as those considered in Revenue Ruling 54–608, C.B. 1954–2, 8, since the taxpayer in the instant case has incurred a minimum liability, the amount of which is fixed at the end of its taxable year.

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26 CFR 1.162–15: Excepted contributions.

Provisions for notifying an exempt organization involved in the examination and appeals procedure regarding the conclusions of the Internal Revenue Service. See Rev. Proc. 61–32, page 572.

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26 CFR 1.162–17: Reporting and substantiation of traveling and other business expenses of employees.

Rev. Rul. 58–453 Supplement XI

Revenue Ruling 58–453, C.B. 1958–2, 67, relating to certain fixed mileage allowances or per diem allowances received by employees, refers to the Standardized Government Travel Regulations in connection with the maximum per diem allowance in lieu of subsistence authorized to be paid by the Federal Government while traveling outside the continental United States. The following rates, obtained from official Government sources, are published as a supplement to Revenue Ruling 58–453 and may be amended or supplemented from time to time.

STANDARDIZED GOVERNMENT TRAVEL REGULATIONS

Appendix I, Revised—Maximum Per Diem Rates in Lieu of Subsistence for Travelers Beyond the Limits of the Continental United States

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The changes, identified by asterisks, are effective August 1, 1961.

Locality	*Maximum per diem rates*
Aden	$16
*Afghanistan:	
Kabul	16
*Other	9
*Alaska:	
Anchorage	21
Fairbanks	21
Juneau	21
Nome	21
*Umiat	24
Other	15
Albania	$10
Algeria	15
American Samoa	11
Andorra (See "Other Localities")	
Angola	13
Argentina	14
*Australia:	
Melbourne	17
Sydney	17
*Other	13

Locality	Maximum per diem rates
Austria:	
Vienna	$16
Other	13
Bahamas:	
(Apr. 15–Dec. 14, incl.)	17
(Dec. 15–Apr. 14, incl.)	24
Bahrein Island	14
Basutoland (See "Other Localities")	
Bechuanaland (See "Other Localities")	
Belgium	16
Bermuda	20
Bolivia	13
Bonin Islands (See "Other Localities")	
Brazil:	
Belem	18
Brasilia	18
Rio de Janeiro	18
Sao Paulo	18
Other	13
British Guiana	15
British Honduras	16
British Somaliland (See "Other Localities")	
Brunei	13
Bulgaria	14
*Burma:	
*Mandalay	11
Rangoon	19
Other	6
Cambodia	14
Cameroun	17
Canada	17
Canary Islands	10
Canton Island	15
Central African Republic [1]	26
Ceylon:	
Colombo	20
Other	12
Chad, Republic of [1]	28
*Chile:	
*Santiago	18
Other	13
China:	
Taipei	16
Other	11
Columbia	16
*Congo, Republic of [1]	23
Congo, Republic of the [3] (*See* separate listing for Ruanda-Urundi)	14
Costa Rica	15
Cuba:	
Havana	17
Other	14
Cyprus	12
Czechoslovakia	12
Dahomey, Republic of [2]	28
Denmark	12
Dominican Republic:	
Cuidad Trujillo:	
(Apr. 16–Dec. 15 incl.)	$22
(Dec. 16–Apr. 15 incl.)	25
Other	11
*Ecuador:	
Guayaquil	18
*Quito	14
Other	12
El Salvador	20
Eritrea	13
Estonia	16
Ethiopia	13
Fiji Islands	16
Finland	20
France:	
Alpes Maritimes Department (including Nice)	15
Fontainebleau	15
Marseilles	15
Seine Department (including Paris)	17
Seine et Oise Department	17
Other	13
French Guiana	13
French Somaliland	15
French West Indies	18
Gabon, Republic of [1]	21
*Gambia	17
Germany:	
Saarland	13
Other	13
*Ghana:	
*Accra	22
Other	15
Gibraltar	7
Great Britain and North Ireland:	
London, including Middlesex County, Bushey Hall, and Denham	15
Other	13
Greece	14
Greenland (See "Other Localities")	
Guam	15
Guatemala	16
Guinea	23
Haiti:	
Cap-Haitien	11
Port-au-Prince:	
(Apr. 16–Dec. 15 incl.)	13
(Dec. 16–Apr. 15 incl.)	16
Other	8
Hawaii	16
*Honduras	15
*Hong Kong	16
Hungary	7
Iceland	13
India:	
Bombay	13
Calcutta	15
New Delhi	13
Other	9

See footnotes at end of table.

Locality	Maximum per diem rates
Indonesia	$6
Iran:	
Khoramshahr	15
Tehran	20
Other	11
Iraq:	
Baghdad	18
Other	15
*Ireland:	
*Dublin	15
*Other	12
Israel	14
Italy:	
Florence	15
Genoa	15
Milan (including Vergiate and Gallarate)	18
Naples	15
Palermo	15
Rome	18
Trieste	15
Turin	18
Venice	15
Other	12
*Ivory Coast:[2]	
Abidjan	23
*Other	18
Iwo Jima (See "Other Localities")	
Japan	14
Jerusalem	14
Jordan	10
*Kenya	12
Korea:	
Seoul	19
Other	9
Kuwait	14
Laos	15
Latvia	16
Lebanon	13
Liberia:	
Monrovia	25
Roberts Field	18
Other	8
Libya:	
Benghazi	16
Tripoli	16
Wheelus Field	9
Other	12
Liechtenstein	12
Lithuania	16
Luxembourg	14
Malagasy Republic (formerly Madagascar)	18
Malaya	14
Mali, Republic of [2] (formerly Soudanese Republic)	28
Mauritania [2]	13
Malta	12
Mexico:	
Acapulco	15
Mexico, D.F.	15
Other	12
Midway	$15
Monaco	15
Morocco	12
Mozambique	10
Nepal	11
Netherlands:	
The Hague	16
Other	14
Netherlands Antilles	20
New Caledonia	14
New Zealand:	
Auckland	12
Wellington	12
Other	9
Nicaragua	18
Niger, Republic of [2]	19
*Nigeria:	
*Lagos	21
Other	13
North Borneo	13
Norway	15
Nyasaland (*See* "Rhodesia and Nyasaland, Federation of")	
Pakistan	11
Panama:	
Panama City	17
Other (including Canal Zone)	13
Paraguay	12
Peru	13
Philippines:	
Manila	13
Other	9
Poland	6
Portugal:	
Azores	7
Madeira Islands	7
Other	12
Portuguese Guinea	10
Puerto Rico:	
San Juan	24
Other	18
Qatar	25
Rhodesia and Nyasaland, Federation of	14
Ruanda-Urandi [3]	16
Rumania	14
Ryukyu Islands (*See* "Other Localities")	
Saarland (*See* Germany)	
Sarawak	16
*Saudi Arabia	
*Jidda	18
Riyadh	25
Other	10
Senegal, Republic of [2]	19
Sierra Leone	18
Singapore	18
*Society Islands:	
*Tahiti	18
Other	9
Somali Republic	10
Southwest Africa	8

See footnotes at end of table.

Locality	Maximum per diem rates
Spain (*see also* Canary Islands)	
Madrid	$13
Other	10
Spanish Sahara (*See* "Other Localities")	
Sudan	15
*Surinam	18
Swaziland (*See* "Other Localities")	
Sweden	16
Switzerland	15
*Tanganyika	10
Thailand:	
Bangkok	19
Other	8
*Togo:	
Lome	20
*Other	9
Trust Territories Pacific Islands	11
Tunisia	15
Turkey:	
Ankara	13
Istanbul	15
Other	9
Uganda	10
Union of South Africa:	
Capetown	12
Johannesburg	12
Other	10
*Union of Soviet Socialist Republics	18
United Arab Republic:	
Egypt:	
Cairo	$13
Other	10
Syria	11
Upper Volta, Republic of [2]	17
*Uruguay	15
Venezuela:	
Caracas	23
Maracaibo	23
Other	18
*Viet-Nam:	
Saigon-Cholon Area	16
*Other	9
Virgin Islands:	
(May-Nov. incl.)	20
(Dec.-Apr. incl.)	30
Volta (See Upper Volta) Wake	15
*West Indies:	
Jamaica:	
(Apr. 16-Dec. 14 incl.)	14
(Dec. 15-Apr. 15 incl.)	18
Trinidad	17
*Other:	
*(Apr. 16-Dec. 14 incl.)	13
*(Dec. 15-Apr. 15 incl.)	18
Yugoslavia	8
Zanzibar (See "Other Localities")	
Other Localities	9

[1] Formerly a part of French Equatorial Africa.
[2] Formerly a part of French West Africa.
[3] Formerly listed under Belgian Congo.

Rev. Rul. 58–453 [1]
Supplement XII

Public Law 87–139, effective August 14, 1961, increased the maximum mileage allowance to be paid by the Federal Government for use of a personal automobile on official business to 12 cents per mile and the maximum per diem allowance in lieu of subsistence while traveling in the continental United States, other than Alaska, to $16 per day.

In determining whether an employee in a travel status on official business on August 14, 1961, is deemed to have been required to account to his employer for mileage and subsistence allowances for purposes of section 1.162–17(b) of the Income Tax Regulations, the new maximum rates of mileage and per diem allowances authorized to be paid by the Federal Government for travel within the continental United States are effective only with respect to allowances for travel performed on or after August 14, 1961.

Public Law 87–139, approved August 14, 1961, increased the maximum mileage allowance authorized to be paid by the Federal Government for use of a personal automobile on official business from 10 cents to 12 cents per mile and the maximum per diem allowance in lieu of subsistence authorized to be paid while traveling on official business within the continental United States (other than Alaska) from $12 to $16 per day.

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[1] Based on Technical Information Release 340, dated October 9, 1961.

Revenue Ruling 58–453, C.B. 1958–2, 67, sets forth the rules under which mileage allowances for travel and per diem allowances in lieu of subsistence paid by an employer to his employee while in a travel status will be approved by the Commissioner of Internal Revenue, in the exercise of his discretion under section 1.162–17(b)(4) of the Income Tax Regulations, as constituting reasonable business practice which will be regarded as equivalent to an accounting by the employee to his employer for purposes of section 1.162–17(b) of such regulations. The payment of a fixed mileage allowance or per diem allowance in lieu of subsistence at rates not in excess of 125 percent of the rates authorized to be paid by the Federal Government in the locality in which the travel is performed is deemed to be a reasonable business practice for this purpose.

At the time of issuance of Revenue Ruling 58–453, the Federal Government's authorized maximum mileage allowance and per diem allowance while traveling within the continental United States was 10 cents per mile and $12 per day, respectively. Accordingly, it was held that for purposes of section 1.162–17(b) of the Income Tax Regulations an employee was deemed to have been required to account to his employer in cases where the rates of mileage allowance and per diem allowance in lieu of subsistence paid by the employer were not in excess of 12½ cents per mile and $15 per day, respectively. Also, it was held that whenever the maximum mileage and per diem allowances authorized to be paid by the Federal Government are changed, the 12½ cents per mile and the $15 per day will likewise at such time be adjusted to 125 percent of the changed amounts.

Accordingly, in view of the increases authorized by Public Law 87–139, for purposes of section 1.162–17(b) of the Income Tax Regulations an employee will be deemed to have been required to account to his employer in cases where the rates of mileage allowance or per diem allowance in lieu of subsistence paid by the employer for travel performed on or after August 14, 1961, are not in excess of 15 cents per mile and $20 per day, respectively.

It is emphasized that the new rates are effective only for allowances paid for travel performed on or after August 14, 1961, and that the former rates of 12½ cents per mile and $15 per day are still effective for allowances paid for travel performed prior to August 14, 1961.

SECTION 164.—TAXES

26 CFR 1.164–1: Deduction for taxes. Rev. Rul. 61–152

> Charges imposed by the City of Wheeling, West Virginia, for the continuance, maintenance, and improvement of the police and fire departments of that city are "taxes" within the meaning of section 164 of the Internal Revenue Code of 1954, even though the charges are denominated as "service charges."

Advice has been requested whether charges imposed by the City of Wheeling, West Virginia, for the continuance, maintenance and improvement of the police and fire departments of that city are "taxes" within the meaning of section 164 of the Internal Revenue Code of 1954.

Section 504 of the West Virginia Code of 1955 as amended, provides, in part, as follows:

> The governing authority of every municipal corporation that furnishes any essential or special municipal service, including police and fire protection, parking facilities on the streets or otherwise, recreational facilities, street cleaning, street lighting, sewerage and sewer disposal, and the collection and disposal of garbage, ashes or other waste materials, may by ordinance provide for the continuance, maintenance, installation or improvement of such service, may make reasonable regulations with respect thereto, may impose upon the users of such service reasonable rates, fees and charges to be collected in the same manner as municipal taxes are collected or in some other manner specified in the ordinance, and may provide penalties for any violation of such ordinance.

Under a similar provision in an earlier statute, the council of the City of Wheeling passed Ordinance No. 1812 on August 28, 1951, which provided generally for the continuance, maintenance and improvement of the fire department of the city as an essential municipal service. It imposed charges upon the "users of such service" and provided for the manner of collecting charges. The ordinance was amended by Ordinance No. 1942, of September 30, 1952, and was further amended and reenacted by Ordinance No. 2674, of August 18, 1959. A similar ordinance providing for like charges upon the "users" of services of the police department is currently imposed by Ordinance No. 2672, of August 18, 1959.

The current ordinances each provide that an annual charge of 20/100 of one percent of the value of all buildings, whether residential, commercial, or industrial, and all tangible personal property within the city is imposed upon the owner, or owners thereof. In each case the minimum charge is one dollar, the charge being payable to the city treasurer. Each year the municipal council of the City of Wheeling determines the value of the property. The funds collected are commingled with the general revenue funds of the city, to be disbursed as the municipal authorities direct. No earmarking or hypothecation of the funds collected takes place. All funds used for the operation of the two departments come from the general revenue funds of the city, and the amount used is not limited to, nor determined by, the amounts collected under the above-mentioned ordinances.

The "service charges" are exacted at a uniform rate from all owners of designated property, with the exception of property owned by the United States, the State, the County, the City, or by religious, charitable, fraternal or non-profit organizations exempt from payment of real and personal property taxes under the laws of the State.

Section 164(a) of the Internal Revenue Code of 1954 provides that, except as otherwise provided, there shall be allowed as a deduction taxes paid or accrued within the taxable year.

Section 1.164–1 of the Income Tax Regulations provides, among other things, that except as otherwise provided. taxes imposed by the United States, any State, Territory, possession of the United States, or a political subdivision of any of the foregoing, are deductible for the taxable year in which paid or accrued.

I.T. 3511, C.B. 1941–2, 90, provides, in part, as follows:

> In general, the term "tax" includes every burden that may lawfully be laid upon the citizen by virtue of the taxing power, but its application in statutory provisions varies with the intent and purpose of the particular provision. A tax is an enforced contribution, exacted pursuant to legislative authority in the exercise of the taxing power. and imposed and collected for the purpose of

raising revenue to be used for public or governmental purposes, and not as a payment for some special privilege granted or service rendered. Taxes are, therefore, distinguishable from various other charges imposed for particular purposes under particular powers or functions of government. In view of such distinctions, the question whether a particular charge is to be regarded as a tax depends upon its real nature. If it is in the nature of a tax, it is not material that it may be called by a different name; conversely, if it is not in the nature of a tax, it is not material that it may be so called.

Nothing in the facts of the instant case supports the view that the charges are payments for a special privilege. Also, there is nothing which indicates any reasonable relationship between the "service charge" and the extent of the services provided to those on whom the charges are imposed, even though they are stated to be levied upon the "users of such service." Intangible personal property, as well as individual citizens, are afforded protection, but neither is subjected to the "service charge." The charges are imposed irrespective of whether an individual owner wishes or avails himself of such services, and even though he may have procured similar services from private sources.

Further, no variation is made in the rate of the charges to allow for properties subject to varying degrees of risk. Neither is there an adjustment in the rates although experience may have shown that particular kinds of construction, or certain areas, or activities demand a higher level of services than the average.

The instant situation is distinguishable from situations in which municipal charges for services are measured by the benefits which may be, or have been derived therefrom, as was the case in *Benjamin Mahler* v. *Commissioner*, 119 Fed. (2d) 869 (1941), certiorari denied, 314 U.S. 660 (1941), in which water charges were based on front footage of buildings, number of tenants, baths, hose connections, particular use, etc. It was there held that such charges on property owned and occupied as a personal residence, could not be deducted as taxes. Also, see O.D. 719, C.B. 3, 139 (1920).

Accordingly, it is held that the above-described charges imposed upon the owners of buildings and tangible personal property within the City of Wheeling, West Virginia, for fire and police department services are "taxes" within the meaning of section 164(a) of the Code, and are, therefore, deductible as such, notwithstanding their local characterization as "charges for services upon the users thereof."

Rev. Rul. 61–182

Deductibility for Federal income tax purposes of the taxes imposed upon the sale at retail or the use of tangible personal property within the State of Kentucky under section 139.200 and section 139.310, respectively, of chapter 139, Kentucky Revised Statutes, July, 1960.

Advice has been requested regarding the deductibility for Federal income tax purposes of the taxes imposed upon the sale at retail or the use of tangible personal property within the State of Kentucky under section 139.200 and section 139.310, respectively, of chapter 139, Kentucky Revised Statutes, July, 1960.

Chapter 139 of the Kentucky Revised Statutes contains the following pertinent provisions:

139.100 * * * (1) "Retail sale" or "sale at retail" means:

(a) 1. A sale for any purpose other than resale in the regular course of business of tangible personal property, or

2. The furnishing of the facilities and services mentioned in subsection (2) of this section;

(b) The delivery in this state of tangible personal property by an owner * * * if the delivery is to a consumer or person for redelivery to a consumer pursuant to a retail sale made by a retailer not engaged in business in this state. * * *.

(2) "Retail sale" or "sale at retail" shall include but shall not be limited to the following:

(a) The rental of any room or rooms * * * in which rooms, * * * are regularly furnished to transients for a consideration * * *;

(b) The furnishing of sewer services and intrastate telephonic and telegraphic communications and services:

(c) The sale of admissions * * *.

Section 139.200 imposes a tax upon all retailers at the rate of three percent of the gross receipts of any retailer derived from "retail sales" made within the State after June 30, 1960. Section 139.310 imposes an excise tax on the storage, use, or other consumption of tangible personal property purchased on or after July 1, 1960, for storage, use, or other consumption in the State at the rate of three percent of the sales price of the property.

Section 139.210 states that the taxes may be collected by the retailer from the consumer. Section 139.330 provides that every person storing, using, or otherwise consuming tangible personal property purchased from the retailer is liable for the use tax levied under section 139.310; that his liability is not extinguished until the tax has been paid except that a receipt from a retailer is sufficient to relieve the purchaser from further liability for the tax to which the receipt refers. Section 139.340 and section 139.360 emphasize that the tax due is the retailer's debt to the State. In accordance with section 139.380, the tax required to be collected by the retailer from the purchaser must be displayed separately from the list price, the price advertised in the premises, or other price on the sales check. It is unlawful for any retailer to advertise, or hold out or state to the public or any customer, directly or indirectly, that the sales tax or the use tax levied will be absorbed by the retailer, or that it will not be added to the selling price of the property sold, or that, if added, it or any part thereof will be refunded. See section 139.220 and section 139.370.

Section 164(a) of the Internal Revenue Code of 1954 provides that, in computing taxable income, there shall be allowed as a deduction taxes paid or accrued within the taxable year, with certain exceptions not here material.

Section 164(c)(1) of the Code relates to the deduction of retail sales taxes and gasoline taxes in computing taxable income. Such section provides that, in the case of any State or local sales tax, if the amount of the tax is separately stated, then, to the extent that the amount so stated is paid by the consumer (otherwise than in connection with the consumer's trade or business) to his seller, such amount shall be allowed as a deduction to the consumer as if it constituted a tax imposed on, and paid by, such consumer.

Section 164(c)(2) of the Code provides that, as used therein, the term "State or local sales tax" means a tax imposed by a State, Territory, a possession of the United States, or a political subdivision

of any of the foregoing, or by the District of Columbia, which tax (A) is imposed on persons engaged in selling tangible personal property at retail (or on persons selling gasoline or other motor vehicle fuels at wholesale or retail) and is a stated sum per unit of property sold or is measured either by the gross sales price or by the gross receipts from the sale; or (B) is imposed on persons engaged in furnishing services at retail and is measured by the gross receipts for furnishing such services.

Section 1.164–1 of the Income Tax Regulations provides that, in general, taxes are deductible only by the persons upon whom they are imposed.

Accordingly, it is held that the sales tax imposed by the State of Kentucky pursuant to section 139.200 of the Kentucky Revised Statutes, July, 1960, constitutes a "retail sales" tax within the meaning of section 164(c) of the Code. The retail sales tax collected by a vendor from a purchaser is includible in the vendor's income for Federal income tax purposes and is deductible by him under section 164(a) of the Code in computing his taxable income.

To the extent that such tax is paid by an individual otherwise than in connection with his trade or business, it is deductible by him as a retail sales tax under section 164(c) of the Code, provided he does not elect to use the standard deduction or compute his tax liability from the optional tax table.

If the tax is paid with respect to property used in a trade or business, such tax becomes a part of the cost of the article purchased, and in the case of an individual is deductible in accordance with section 162(a) and section 62 of the Code, unless the expenditure is properly chargeable to capital account. In the case of a purchaser other than an individual engaged in a trade or business, the deduction is allowable as a business expense unless the amount thereof is properly chargeable to capital accounts.

It is also held that the use tax imposed by the State pursuant to section 139.310 of the Kentucky Revised Statutes, July, 1960, is deductible by the purchaser under section 164(a) of the Code. In the case of an individual who elects to use the optional standard deduction or the optional tax table, no deduction is allowable unless the use tax is attributable to a trade or business carried on by him. (See section 62 of the Code.) In the case of taxpayers, other than individuals, engaged in a trade or business, the use tax is deductible as a tax in computing taxable income.

SECTION 165.—LOSSES

26 CFR 1.165–1: Losses. Rev. Rul. 61–201
(Also Section 72; 1.72–11.)

In determining the amount of loss sustained by the original purchaser upon his surrender of a single premium refund annuity contract for a cash consideration, the basis of the contract is its cost, less the amounts previously received under the contract which were properly excluded from the gross income of the recipient under the law applicable at the time of receipt. The excess of the basis, thus determined, over the amount received upon surrender of the contract constitutes an ordinary loss.

I.T. 3567, C.B. 1942–2, 105, modified.

Advice has been requested with respect to the method of computing the basis of a single premium refund annuity contract for the purpose of determining the amount of loss sustained by the original purchaser upon his surrender of the annuity contract for a cash consideration.

The taxpayer purchased a single premium refund annuity policy for $25x$ dollars. In 1956, he surrendered the policy for a cash consideration of $10x$ dollars. The annuity payments received during prior years totaled $15x$ dollars of which $7x$ dollars were excluded from gross income under the law applicable at the time of receipt.

I.T. 3567, C.B. 1942–2, 105, holds, insofar as pertinent here, that the amount of a loss allowable upon the surrender of a single premium refund annuity contract, is the cost less the aggregate of the amount received on its surrender plus all other amounts received under the contract by the annuitant. Under I.T. 3567 no distinction is made between annuity payments which were included in the annuitant's gross income when received and annuity payments which were excluded from the annuitant's gross income.

Section 1.72–11(d)(1) of the Income Tax Regulations promulgated under section 72 of the Internal Revenue Code of 1954, provides, in part, as follows:

> Any amount received upon the surrender, redemption or maturity of a contract to which section 72 applies, which is not received as an annuity under the rules of section 1.72–2(b), shall be included in the gross income of the recipient to the extent that it, when added to amounts previously received under the contract and which were excludable from the gross income of the recipient under the law applicable at the time of receipt, exceeds the aggregate of premiums or other consideration paid. * * *

It is clear that the contract under consideration is one to which section 72 of the Code applies and that the $10x$ dollars received by the taxpayer, upon surrender of the contract, was "an amount not received as an annuity" under section 72(e) of the Code. It is likewise clear that, where the transaction results in a loss, the same treatment should be afforded the taxpayer as is afforded where the transaction results in a gain. Further, the amount of $7x$ dollars excluded from gross income in the instant case merely represents a recovery of "basis" (investment) for which adjustment is required under section 1016(a)(1) of the Code, which provides, as far as here pertinent, that proper adjustment in respect of property shall in all cases be made for receipts properly chargeable to capital account.

Accordingly, in determining the amount of loss sustained in the instant case by the original purchaser upon his surrender of a single premium refund annuity contract for a cash consideration, the basis of the contract is its cost ($25x$ dollars) less the amounts previously received under the contract which were properly excludable from the gross income of the recipient under the law applicable at the time of receipt ($7x$ dollars). The excess of the basis thus determined ($18x$ dollars) over the amount received upon surrender of the contract ($10x$ dollars) constitutes an ordinary loss ($8x$ dollars).

I.T. 3567, *supra*, is modified to remove therefrom the implication that the entire amounts of the annuity payments received by the annuitant are deducted from his cost of the annuity contract in computing the amount of loss sustained upon its surrender.

Nothing in this ruling should be construed as permitting a loss deduction on the surrender of any contract other than a refund annuity.

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26 CFR 1.165–2: Obsolescence of nondepreciable property.

Treatment of amounts expended in drilling a test hole to ascertain existence of adequate supply of water for a business. See Rev. Rul. 61–206, page 57.

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26 CFR 1.165–6: Farming losses.

Losses due to the death of livestock from disease. See Rev. Rul. 61–216, page 134.

SECTION 167.—DEPRECIATION

26 CFR 1.167(a)–1: Depreciation in general. Rev. Rul. 61–162
(Also Section 216; 1.216–1.)

> The entire cost of stock in a corporation, qualifying as a cooperative housing corporation under section 216(b) of the Internal Revenue Code of 1954, represents an investment in such stock only, and no part of the investment may be allocated to the lease rights acquired with such stock. A tenant-stockholder who subleases his apartment in a building owned or leased by such a corporation may not depreciate or amortize any portion of such investment as an amount allocable to his lease rights.

Advice has been requested whether the cost of stock in a corporation, qualifying as a cooperative housing corporation under section 216(b) of the Internal Revenue Code of 1954, represents an investment in such stock only, or whether a portion of the investment may be allocated to the tenant-stockholder's right to occupy an apartment in a building owned by such a corporation.

A taxpayer subscribed for and purchased stock in a corporation qualifying as a cooperative housing corporation under section 216(b) of the Code. At the same time the taxpayer and the corporation entered into an agreement termed a "proprietary lease" under which the taxpayer, as a stockholder, was entitled to the use of an apartment in the building owned by the corporation.

Although the majority of the tenant-stockholders of the corporation occupied their apartments for dwelling purposes, they were not obligated to do so. The instant taxpayer, among others, subleased his apartment to a third person after the sublessee chosen was approved by the corporation.

Section 167(a) of the Code provides that as a general rule there shall be allowed as a depreciation deduction a reasonable allowance for the exhaustion, wear and tear (including a reasonable allowance for obsolescence) of property used in the trade or business, or held for the production of income.

Section 216(b) of the Code defines a cooperative housing corporation as a corporation:

(A) having one and only one class of stock outstanding,

(B) each of the stockholders of which is entitled, solely by reason of his ownership of stock in the corporation, to occupy for dwelling purposes a house, or an apartment in a building, owned or leased by such corporation,

(C) no stockholder of which is entitled (either conditionally or unconditionally) to receive any distribution not out of earnings and profits of the corporation except on a complete or partial liquidation of the corporation, and

(D) 80 percent or more of the gross income of which for the taxable year in which the taxes and interest described in subsection (a) are paid or incurred is derived from tenant-stockholders.

The corporation was the owner of the apartment building in question. The taxpayer contended, however, that he was the owner of a leasehold on an apartment and that he was entitled to depreciate or amortize a portion of his investment in the corporation, while his apartment was subleased, as an amount paid for a leasehold.

When the taxpayer paid money to the corporation in return for stock of the corporation, he established a basis in the stock for tax purposes. He was entitled to the occupancy or use of the apartment as a dwelling solely by virtue of the fact that he owned the stock, and upon disposing of the stock his rights would terminate. Since the right to occupy an apartment was conditioned upon continued ownership of the stock, it was inseverable therefrom, and the taxpayer established no tax basis in his rights with respect to the apartment as distinguished from the stock.

For tax purposes, the taxpayer is in the same position as any other owner of stock in a corporation except insofar as he is able to qualify for the deduction provided by section 216 of the Code with respect to real estate taxes and interest paid or incurred by the corporation during the taxable year. The fact that the taxpayer chose to sublease his apartment rather than occupy it himself does not change the nature of the property in which he invested.

Accordingly, it is held that the entire cost of stock in a corporation, qualifying as a cooperative housing corporation under section 216(b) of the Code, represents an investment in such stock only, and no part of the investment may be allocated to the tenant-stockholder's right to occupy a dwelling unit which was acquired with such stock. Therefore, the instant taxpayer may not depreciate or amortize any portion of his investment in the stock of the cooperative as an amount allocable to his right to occupy an apartment in the building owned by such corporation.

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26 CFR 1.167(a)–4: Leased property. Rev. Rul. 61–217

Where a long-term lessee erected at his cost a commercial building on land leased to him and then subleased the improved realty to a third party, the lessee's capital investment in the building is recoverable by him through allowances for depreciation or amortization in accordance with the provisions of section 1.167(a)–(4) of the Income Tax Regulations.

Where a long-term lessee erected at his cost a commercial building on land leased to him and then assigned his entire interest in the improved realty to a third party, who later assigned his remaining interest to a fourth party, who later assigned his remaining interest to a fifth party, the capital investment of each assignee in such interest is similarly recoverable by him but only to the extent appropriate during the period he owns it.

Advice has been requested regarding how, when, and by whom costs of leasehold improvements are recoverable, for Federal income tax purposes, particularly where (1) a long-term lessee erected at his cost a commercial building on land leased to him and then subleased the improved realty to a third party, and (2) a long-term lessee erected at his cost a commercial building on land leased to him and then assigned his entire interest in the improved realty to a third party, who later assigned his remaining interest to a fourth party, who later assigned his remaining interest to a fifth party.

In the first case, *A*, an owner of unimproved land, granted a 99-year lease thereof, at a stipulated periodic rental, to *B*, who erected at his cost a commercial building thereon, which had an estimated useful life of 50 years, and then subleased the improved realty for the remaining period of the lease, at a much higher stipulated periodic rental, to *C*, who uses it for business purposes. Under such circumstances, it is evident that *B*, the lessee, made a capital investment in the building and that, upon subleasing the improved realty, he retained his interest therein, since, while required to continue to pay rent for use of the land to *A* under the lease, he is entitled to collect much higher rent for use of the improved realty from *C* under the sublease.

In the second case, *M*, an owner of unimproved land, granted a 99-year lease thereof, at a stipulated periodic rental, to *N*, who erected at his cost a commercial building thereon, which had an estimated useful life of 50 years, and then assigned his entire interest in the improved realty to *O*, for a substantial stipulated sum and the latter's agreement to pay *M* the periodic rent stipulated in the lease. Under such circumstances, it is evident that *N*, the lessee, did not retain his capital investment or any economic interest in the building but assigned his interest therein, as well as his leasehold of the land, to *O*. After using the improved realty five years for business purposes, *O* assigned his remaining interest therein to *P* for a substantial stipulated sum and the latter's agreement to pay *M* the periodic rent stipulated in the lease. After using the improved realty two years for business purposes, *P* assigned his remaining interest therein to *Q* for a substantial stipulated sum and the latter's agreement to pay *M* the periodic rent stipulated in the lease. *Q* is using the improved realty for business purposes.

Section 167(a) of the Internal Revenue Code of 1954 provides as follows:

> GENERAL RULE.—There shall be allowed as a depreciation deduction a reasonable allowance for the exhaustion, wear and tear (including a reasonable allowance for obsolescence)—
>
> (1) of property used in the trade or business, or
> (2) of property held for the production of income.

Section 1.167(a)–4 of the Income Tax Regulations provides, in part, as follows:

> *Leased property.*—Capital expenditures made by a lessee for the erection of buildings or the construction of other permanent improvements on leased property are recoverable through allowances for depreciation or amortization. If the useful life of such improvements in the hands of the taxpayer is equal to or shorter than the remaining period of the lease, the allowances shall take the form of depreciation under section 167. See sections 1.167(b)–0, 1, 2, 3, and 4 for methods of computing such depreciation allowances. If, on the other hand, the

estimated useful life of such property in the hands of the taxpayer, determined without regard to the terms of the lease, would be longer than the remaining period of such lease, the allowances shall take the form of annual deductions from gross income in an amount equal to the unrecovered cost of such capital expenditures divided by the number of years remaining of the term of the lease. Such deductions shall be in lieu of allowances for depreciation. See section 162 and the regulations thereunder. * * * * Capital expenditures made by a lessor for the erection of buildings or other improvements shall, if subject to depreciation allowances, be recovered by him over the estimated life of the improvements without regard to the period of the lease.

As indicated in the last sentence of the above regulations, where an owner of land erected a commercial building thereon at his cost and then leased the improved realty to another party, such lessor has invested capital in the building which generally is recoverable by him through allowances for depreciation, under section 167, during its useful life regardless of the period of the lease. Compare G.C.M. 11933, C.B. XII–2, 52 (1933). In such a case, neither the lessee nor any assignee of his leasehold has made any investment of capital in the building, or investment of that nature, so recoverable by him. See *Weiss* v. *J. Harry Wiener*, 279 U.S. 333, Ct.D. 60, C.B. VIII–1, 257 (1929); and *David Dab* v. *Commissioner*, 28 T.C. 933, affirmed 255 Fed. (2d) 788. However, any sum paid by such a lessee or his assignee in acquisition of the leasehold is recoverable by him under section 1.162–11(a) of the regulations which provides that he "* * * may take as a deduction in his return an aliquot part of such sum each year, based on the number of years the lease has to run."

In the first case here presented, where a long-term lessee erected at his cost a commerical building on land leased to him and then subleased the improved realty, at a much higher rental than that which he is required to pay for use of the land, the lessee made a capital investment in the building and retained such interest therein upon subleasing the improved realty. Since the estimated useful life to him of the building is not longer than the remaining period of the lease, his capital investment in the building is recoverable by him in accordance with the aforestated provisions of section 1.167(a)–4 of the regulations through allowances for *depreciation* under section 167 of the Code, during the period of its useful life. If the remaining period of the lease is shorter than the estimated useful life of the building, his capital investment in the building would be recoverable by him, under the principles of the aforestated provisions of section 1.167(a)–4, through allowances for *amortization* over the remaining period of the lease.

In the second case here presented, where a long-term lessee erected at his cost a commercial building on land leased to him and then assigned his entire interest in the improved realty to a third party for a stipulated sum and the latter's agreement to pay the rent stipulated in the lease for use of the land, and there were similar assignments to a fourth and a fifth party of such interest remaining after several-year intervals of use, the capital investment of each assignee in such interest may wholly represent capital investment in the building of the same nature as that of the original lessee therein. Consequently, such investments of the assignees would be likewise recoverable by them under the principles of the aforestated provisions of section 1.167(a)–4.

However, since the second and third assignments here were made many years after the lease was entered into, a substantial part of the capital investment of each assignee thereunder in such interest may represent consideration for increased rental value of the leased land and, hence, would represent leasehold acquisition cost (payment for use of the leased land in addition to the rent payable periodically under the lease), and the balance of the investment would represent each such assignee's capital investment in the building. In such event, the last mentioned part (investment in the building) of his capital investment in such interest would be recoverable by him under the principles of the aforestated provisions of section 1.167(a)–4, through allowances for *depreciation or amortization*, depending on whether the remaining useful life of the building is within or longer than the remaining period of the lease, and the first heretofore mentioned part (land acquisition cost) of his capital investment therein would be recoverable by him, under the principles of the aforestated provisions of section 1.162–11(a) of the regulations, *only* through allowances for *amortization* over the remaining period of the lease regardless of the remaining useful life of the building. Recoveries by assignees of such interest of their capital investments therein through allowances for depreciation, amortization, or both, are, of course, permissible to each assignee only to the extent appropriate during the period he owns it.

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26 CFR 1.167(a)–8: Retirements.

Treatment of amounts expended in drilling a test hole to ascertain existence of adequate supply of water for a business. See Rev. Rul. 61–206, page 57.

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26 CFR 1.167(g)–1: Life tenants and beneficiaries of trusts and estates.

Trust or estate as member of a partnership or beneficiary of another trust. See Rev. Rul. 61–211, page 124.

SECTION 170.—CHARITABLE, ETC., CONTRIBUTIONS AND GIFTS

26 CFR 1.170–2: Charitable deductions by individuals; limitations.

Amounts paid to a trust created for both a private and a charitable purpose. See Rev. Rul. 61–223, page 125.

SECTION 172.—NET OPERATING LOSS DEDUCTION

26 CFR 1.172–1: Net operating loss deduction.

The principles enunciated in Revenue Ruling 61–191, page 251, this Bulletin, relating to the applicability of the "de facto liquidation" doctrine in cases involving corporate net operating loss carryovers and

carrybacks under the Internal Revenue Code of 1939, is equally applicable under the Internal Revenue Code of 1954.

Treatment of consolidated net operating loss of an affiliated group filing a consolidated return upon termination of the affiliation during the taxable year. See Rev. Rul. 61–224, page 145.

SECTION 179.—ADDITIONAL FIRST-YEAR DEPRECIATION ALLOWANCE FOR SMALL BUSINESS

26 CFR 1.179–3: Definitions and special rules. Rev. Rul. 61–142

> Parts for a grain bin for the use of farmers are delivered prefabricated and assembled on the ground by bolting the pieces together. The foundation is a bed of compacted gravel or a circular concrete slab. Cement blocks are spaced on top of the foundation but are not cemented thereto. The assembled bin rests upon the blocks and is anchored to the ground by guy wires. The bin may vary in size from a diameter of fourteen feet, eleven feet high, to a diameter of twenty-four feet, twenty-one feet high. *Held*, the assembled bin does not constitute "tangible personal property" and, therefore, is not subject to the additional first-year depreciation allowance under section 179 of the Internal Revenue Code of 1954.

Farmers have inquired whether the prefabricated grain bin, described below, will qualify as tangible personal property subject to the additional 20 percent first-year depreciation allowance provided by section 179 of the Internal Revenue Code of 1954.

Parts for the grain bin are delivered prefabricated and are assembled on the ground by bolting the pieces together. The foundation may be either a bed of compacted gravel or a circular concrete slab. Cement blocks are spaced according to plan on top of the foundation but are not cemented thereto. The assembled bin rests upon the cement blocks without being fastened to them or to the foundation and is anchored to the ground by guy wires passing through holes in cleats which are bolted to the sides of the bin. The floor of the bin is made of perforated metal strips channeled together and also rests upon the cement blocks. The sides of the bin are made of corrugated metal plates without any framework. The roof consists of overlapping metal panels. The bin ranges in size from a diameter of fourteen feet, eleven feet high, to a diameter of twenty-four feet, twenty-one feet high.

To facilitate the drying of the grain and to control the humidity, a ventilating system consisting of a high pressure fan with a supplemental heater and humidistat control is attached to the underside of the bin. The air from the fan is forced up through the grain through the perforations in the floor.

Under the provisions of section 179 of the Code, a taxpayer, other than a trust, may elect, for the first year in which depreciation is allowable on tangible personal property, to take an additional allowance of 20 percent of the cost or of a portion of the cost of such property. This allowance is in addition to the depreciation allowable under section 167 of the Code computed on the balance of the unrecovered cost of the property after adjustment for this 20 percent allowance. See section 1.179–1(a) of the Income Tax Regulations. To be eligible,

the property must have a useful life of six years or more and must have been acquired by purchase after December 31, 1957.

Section 1.179–3(b) of the Income Tax Regulations provides, in part, that, independent of local law definition, the term "tangible personal property," for purposes of section 179 of the Code, includes any tangible property except land and improvements thereto, such as buildings or other inherently permanent structures thereon (including items which are structural components of such buildings or structures).

Because of the size of the grain bin, it is cumbersome and not adaptable for shifting from one location to another like farm machinery. In fact, under ordinary circumstances, there would be no occasion to move it. The ventilating system, although movable, is an integral part of the facility. However, even though the smallest bin would be difficult to move intact with the equipment generally found around a farm, it could be taken apart and reassembled with ordinary tools. Nevertheless, the fact that it is thus demountable, and thereupon movable, does not change its assembled structural character from that of a building of an inherently permanent nature and as a part of improved real property to that of personal property.

In view of the foregoing, it is held that a grain bin, as described above, is inherently a permanent structure on land and, as such, is not "tangible personal property" within the purview of section 179 of the Code. Therefore, it is not subject to the additional first-year depreciation allowable under that section.

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26 CFR 1.179–4: Time and manner of making election. T. D. 6579[1]

TITLE 26—INTERNAL REVENUE.—CHAPTER I, SUBCHAPTER A, PART 1.—INCOME TAX; TAXABLE YEARS BEGINNING AFTER DECEMBER 31, 1953

Amendment of the Income Tax Regulations under section 179 of the Internal Revenue Code of 1954.

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

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

To simplify the manner of making the election to take additional first-year depreciation allowance, the Income Tax Regulations (26 CFR Part 1) under section 179 of the Internal Revenue Code of 1954 are hereby amended as hereinafter set forth. Except as otherwise specifically provided therein, such regulations as amended are effective for taxable years ending after June 30, 1958.

PARAGRAPH 1. Section 1.179–2 is amended by revising paragraph (c) thereof to read as follows:

§ 1.179–2 DOLLAR LIMITATION.

* * * * * * *

(c) *Affiliated group.*—Taxpayers which constitute an affiliated group, as defined in paragraph (e) of § 1.179–3, shall be treated as one taxpayer in applying the $10,000 limitation of this section. The allowance may be taken by any one such member or allocated among the several members in any manner,

[1] 26 F.R. 10477.

pursuant to allocation by the common parent corporation if a consolidated return is filed, or in accordance with an agreement entered into by the members of the group if separate returns are filed. The amount of the allowance allocated to any member, however, shall not exceed 20 percent of the cost of section 179 property actually purchased by the member in the taxable year. If a consolidated return is filed, the common parent corporation shall file a separate statement attached to the income tax return in which an election is made to claim an additional first-year depreciation allowance. (See § 1.179–4.) If separate returns are filed, each member of an affiliated group to which is allocated any part of the deduction under section 179 shall file a separate statement attached to the income tax return in which an election is made to claim an additional first-year depreciation allowance. (See § 1.179–4.) Such statement shall include the names of all the members of the affiliated group, the taxable year of the common parent corporation, and a description of the manner in which the deduction under section 179 has been divided among them. An allocation among the members of an affiliated group of the allowance under section 179 shall not, if a consolidated return is filed, be revoked after the due date of the return (including extensions of time) of the common parent corporation for a taxable year for which an election to take the allowance is made. If the members of an affiliated group do not file a consolidated return for a taxable year for which an election to take the allowance is made, the allocation as to all members of the group shall not be revoked after the due date of the return (including extensions of time) of the common parent corporation. For the purpose of the preceding sentence, the taxable years of the other members of the affiliated group ending with or within the taxable year of the common parent shall be considered as corresponding to the taxable year of the common parent. Thus, where a common parent's taxable year ends November 30, 1960, the allowance will apply with respect to section 179 property purchased in August 1959 by an affiliated corporation whose taxable year ends June 30, 1960 (a taxable year ending within the taxable year of the parent).

PAR. 2. Section 1.179–4 is amended to read as follows:

§ 1.179–4 TIME AND MANNER OF MAKING ELECTION.—(a) *Election.*—A separate election must be made for each taxable year in which an additional first-year depreciation allowance is claimed with respect to section 179 property. The election under section 179 and § 1.179–1 to claim an additional first-year depreciation allowance on section 179 property shall be made on the taxpayer's income tax return for the taxable year to which the election applies. For the election to be valid, the return must be filed not later than the time prescribed by law (including extensions thereof) for filing the return for such taxable year. The election shall be made by showing as a separate item on the taxpayer's income tax return the additional first-year depreciation claimed with respect to each piece of section 179 property selected. The additional first-year depreciation claimed with respect to section 179 property must not be included in the depreciation claimed under section 167 with respect to such property. The taxpayer shall maintain records which permit specific identification of section 179 property and reflect how and from whom such property was acquired. The election to claim an additional first-year depreciation allowance under this section with respect to any property is irrevocable and shall be binding on the taxpayer with respect to such property for the taxable year for which the election is made and for all subsequent taxable years, unless the Commissioner gives his consent to revoke the election. Similarly, the selection of section 179 property by the taxpayer to be subject to the additional first-year depreciation allowance must be adhered to in computing the taxpayer's taxable income for the taxable year for which the selection is made and for all subsequent taxable years, unless consent to change the selection of property is given by the Commissioner.

(b) *Revocation.*—A request to revoke an election under section 179 and § 1.179–1 or to change the property selected for the additional first-year depreciation allowance shall be in writing and shall be addressed to the Commissioner of Internal Revenue, Washington 25, D.C. The request shall include the name and address of the taxpayer and shall be signed by the taxpayer or his duly authorized representative. It must be filed no later than 6 months after the date prescribed by law (without regard to extensions of time) for filing the income tax return for the year in which the allowance under § 1.179–1 was claimed, shall be accompanied by a statement showing the year and property involved, and

shall set forth in detail the reasons for the request to revoke the election or to change the selection of property. Ordinarily, a request for consent to revoke the election or to change the selection of property will not be granted if it appears from all the facts and circumstances that the only reason for the desired change is to obtain a tax advantage.

(c) *Effective date.*—The provisions of this section apply to all taxable years ending after June 30, 1958. Elections made under the provisions of Treasury Decision 6335, approved November 13, 1958 (23 F.R. 8979) [C.B. 1958–2, 1112], and elections, changes in selection of property, and revocations made under the regulations under section 179, as promulgated in Treasury Decision 6507, approved November 29, 1960 (25 F.R. 12340) [C.B. 1960–2], continue in effect.

Because this Treasury Decision merely simplifies certain election requirements, 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 limitation of section 4(c) of said Act.

This Treasury Decision is issued under the authority contained in section 7805 of the Internal Revenue Code of 1954 (68A Stat. 917; 26 U.S.C. 7805).

BERTRAND M. HARDING,
Acting Commissioner of Internal Revenue.

Approved November 2, 1961.

STANLEY S. SURREY,
Assistant Secretary of the Treasury.

(Filed by the Division of the Federal Register on November 6, 1961, 8:50 a.m., and published in the issue of the Federal Register for November 7, 1961, 26 F.R. 10477)

PART VII.—ADDITIONAL ITEMIZED DEDUCTIONS FOR INDIVIDUALS

SECTION 215.—ALIMONY, ETC., PAYMENTS

26 CFR 1.215–1: Periodic alimony, etc., payments.

Treatment of alimony payments and payments for support of children. See Ct. D. 1862, page 241.

SECTION 216.—AMOUNTS REPRESENTING TAXES AND INTEREST PAID TO COOPERATIVE HOUSING CORPORATION.

26 CFR 1.216–1: Amounts representing taxes and interest paid to cooperative housing corporation.

Depreciation or amortization of a portion of the amount paid for stock of a cooperative housing corporation. See Rev. Rul. 61–162, page 48.

PART IX.—ITEMS NOT DEDUCTIBLE

SECTION 262.—PERSONAL, LIVING, AND FAMILY EXPENSES

26 CFR 1.262–1: Personal, living, and family expenses.

Treatment of expenses paid by an army captain in attending a university in order to obtain a degree. See Rev. Rul. 61–133, page 35.

SECTION 263.—CAPITAL EXPENDITURES

26 CFR 1.263(a)–1: Capital expenditures; in general. Rev. Rul. 61–206

(Also Sections 165,167; 1.165–2, 1.167(a)–8.)

Where a test hole or holes are drilled to determine the existence of water and a well is thereafter drilled to accommodate the taxpayer's business needs, the mere abandonment of the test hole or holes does not give rise to a deductible loss.

Revenue Ruling 56–599, C.B. 1956–2, 122, amplified.

Advice has been requested with respect to the treatment for Federal income tax purposes of amounts expended in drilling a test hole or holes to ascertain the existence of an adequate supply of water for a business. Advice has also been requested as to the application of Revenue Ruling 56–599, C.B.1956–2, 122, upon the abandonment of the test hole or holes whether or not sufficient water for business needs is found.

Revenue Ruling 56–599 reads as follows:

Amounts expended for drilling a water well to be used for irrigation and other agricultural purposes by a taxpayer engaged in the business of farming constitute capital expenditures and are not deductible from gross income. See Rev. Rul. 55–367, C.B. 1955–1, 25. Any loss incurred upon the abandonment of the well for bona fide business reasons indicated by some overt act or identifiable event, such as by filling or sealing the well excavation or casing, resulting in the termination of the existence of the well and all economic benefits therefrom, is deductible by the taxpayer as a business loss within the purview of section 165 of the Internal Revenue Code of 1954 in the taxable year in which such action is actually taken. Rev. Rul. 54–581, C.B. 1954–2, 112.

Since a water well containing components which are subject to wear and tear constitutes depreciable property, a loss attributable to the abandonment of such a well would be deductible under section 165(a) of the Internal Revenue Code of 1954 provided it meets the conditions prescribed in section 1.167(a)–8 of the Income Tax Regulations. See section 1.165–2(c) of the regulations. A test hole drilled to ascertain the existence of a supply of water is subject to the same provisions of the Code and regulations as the well itself.

All amounts expended in the drilling of test holes are in the first instance capital expenditures and are not deductible from gross income.

When a sufficient supply of water for business purposes is found and a water well is drilled, abandonment of the test hole or holes

does not give rise to a deduction from gross income. If the drilling of the test hole or holes is an integral part of the development of a water well in a particular area, the cost thereof becomes a part of the cost of the well. For example, in the search for water within a given area, five test holes were drilled. Upon the drilling of the fifth test hole a sufficient supply of water was found. Even though the first four test holes proved nonproductive, the cost of drilling all five test holes is added to and becomes a part of the cost of the water well.

However, when sufficient water for business purposes is not found after the drilling of the test hole or holes and they are abandoned as indicated in Revenue Ruling 56–599, a loss is sustained, deductible under section 165(a) of the Code, subject to the conditions prescribed in section 1.167(a)–8 of the regulations. If, in a situation of this nature, five test holes are drilled in the search for water and none is found, the costs of drilling the test holes are aggregated, and the entire cost is deductible as a loss when the project is abandoned. This principle is applicable even when, in connection with a particular project, test holes may have been drilled in different taxable years.

SECTION 265.—EXPENSES AND INTEREST RELATING TO TAX-EXEMPT INCOME

26 CFR 1.265–2: Interest relating to tax-exempt income. Rev. Rul. 61–222 [1]

The provisions of section 265(2) of the Internal Revenue Code of 1954 have no application to interest paid on indebtedness represented by deposits in banks engaged in the general banking business since such indebtedness is not considered to be "indebtedness incurred or continued to purchase or carry obligations * * *" within the meaning of section 265. Section 265(2) of the Code provides for the nondeductibility of interest on indebtedness incurred to purchase or carry certain obligations on which the interest is exempt from Federal income tax.

SECTION 267.—LOSSES, EXPENSES, AND INTEREST WITH RESPECT TO TRANSACTIONS BETWEEN RELATED TAXPAYERS

26 CFR 1.267(a)–1: Deductions disallowed. Rev. Rul. 61–163

> A loss sustained by a corporation on the transfer of certain securities to its qualified employees' pension trust fund and a loss sustained by a subsidiary of such corporation on the sale of land to the same pension fund, which also covers its employees, are not allowable deductions inasmuch as such losses are from sales or exchanges of property between a grantor and a fiduciary of the same trust.

Advice has been requested whether a loss sustained by a corporation on the transfer of certain securities to its qualified employees' pension trust and a loss sustained by a subsidiary of such corporation on the

[1] Based on Technical Information Release 348, dated December 1, 1961.

sale of land to the same pension trust, which also covers its employees, are losses from transactions between a grantor and a fiduciary of the same trust and, therefore, not allowable for Federal income tax purposes.

A parent corporation established a trusteed pension plan for its employees and those of its affiliated corporations. Under the terms of the trust agreement, contributions by the corporations are made to the trustees, who have the power to invest the trust funds in such amount and such manner as may seem advisable. The plan and the trust qualify under section 401(a) of the Internal Revenue Code of 1954 for exemption from tax under section 501(a) of the Code.

The parent corporation made a contribution to the pension trust fund in the form of securities of other companies. The fair market value of the securities, at the date of contribution, was less than the cost basis in the hands of the corporation. Hence, the transfer resulted in a loss to the corporation.

In exercising their power to invest the trust funds, the trustees purchased land from one of the parent's wholly owned subsidiary corporations. This subsidiary contributes to the pension trust and its employees are included in the plan and have the same status as all other employees under the plan. Since the agreed sales price was less than the cost basis of the property, the transaction resulted in a loss to the subsidiary.

Section 267 of the Code provides, in part, as follows:

> (a) DEDUCTIONS DISALLOWED.—No deduction shall be allowed—
>
> (1) LOSSES.—In respect of losses from sales or exchanges of property (other than losses in case of distributions in corporate liquidations), directly or indirectly, between persons specified within any one of the paragraphs of subsection (b).
>
> * * * * * * *
>
> (b) RELATIONSHIPS.—The persons referred to in subsection (a) are:
>
> * * * * * * *
>
> (4) A grantor and a fiduciary of any trust.

Section 1.401–1(d) of the Income Tax Regulations states that a trust forming part of a plan of several employers for their employees will be qualified if all the requirements are otherwise satisfied.

Thus, in order for a subsidiary to be entitled to a deduction for contributions to a pension trust, it must establish that the trust meets the requirements of section 401. The subsidiary in the present case has contributed to the pension trust; its employees are covered by the pension trust; and it has claimed the deductions for such contributions to the pension trust on its Federal income tax returns. The subsidiary is a member of the affiliated group constituting a single economic unit.

By reason of the fact that, under section 1.401–1(d) of the regulations, several employers may operate through a single trust, each corporation that contributes to the pension trust and whose employees are covered by the plan is, in effect, the grantor of the pension trust.

Hence, the sale of land by the subsidiary to the trustee is, like the contribution of securities to the trust by the parent corporation, a transaction between a grantor and a fiduciary of the same trust.

Accordingly, it is held that the loss sustained by the parent corporation on the transfer of the securities to its qualified employees' pension fund and the loss sustained by the subsidiary of such corpo-

ration on the sale of land to the same pension fund, which also covers its employees, are not allowable deductions inasmuch as such losses are from sales or exchanges of property between a grantor and a fiduciary of the same trust.

SUBCHAPTER C.—CORPORATE DISTRIBUTIONS AND ADJUSTMENTS

PART I.—DISTRIBUTIONS BY CORPORATIONS

Subpart C.—Definitions; Constructive Ownership or Stock

SECTION 316.—DIVIDEND DEFINED

26 CFR 1.316–1: Dividends.

Proceeds of insurance on the life of an officer of a closely held corporation paid directly to shareholders of the corporation. See Rev. Rul. 61–134, page 250.

PART II.—CORPORATE LIQUIDATIONS

Subpart A.—Effects on Recipients

SECTION 331.—GAIN OR LOSS TO SHAREHOLDERS IN CORPORATE LIQUIDATIONS

26 CFR 1.331–1: Corporate liquidations.

A sale by one corporation of its assets to a new corporation followed by liquidation. See Rev. Rul. 61–156, page 62.

Subpart B.—Effects on Corporations

SECTION 337.—GAIN OR LOSS ON SALES OR EXCHANGES IN CONNECTION WITH CERTAIN LIQUIDATIONS

26 CFR 1.337–1: General. (Also Section 61; 1.61–1.) Rev. Rul. 61–214

In connection with a plan of complete liquidation, where a corporation sold to a single buyer all of its assets, including certain items from which the taxpayer derived full tax benefits through deductions in prior taxable years, that portion of the proceeds representing a recovery of the amounts of such previously deducted items is treated as ordinary income to the corporation under section 61 of the Internal Revenue Code of 1954 and not as nonrecognized gain under section 337(a) of the Code.

Advice has been requested whether, in connection with a sale of corporate assets, certain recoveries of items which previously had been deducted for Federal income tax purposes are to be treated as

proceeds of a nontaxable sale under the provisions of section 337(a) of the Internal Revenue Code of 1954.

An office building corporation, availing itself of the benefits of section 337 of the Code, adopted a plan of complete liquidation and within the 12-month period sold its entire assets to a single buyer. Included in the sale were a stock-pile of coal, plumbing supplies, and small tools. The costs of such items had been deducted in full in taxable years prior to the year of sale.

Section 337(a) of the Code, pertaining to gain or loss on sales or exchanges in connection with certain liquidations, sets forth the general rule that, if a corporation adopts a plan of complete liquidation on or after June 22, 1954, and, within the 12-month period beginning on the date of the adoption of such plan, all of the assets of the corporation are distributed in complete liquidation, less assets retained to meet claims, then no gain or loss shall be recognized to such corporation from the sale or exchange by it of property within such 12-month period.

The provisions of section 337(a) apply only to gain or loss from the "sale or exchange" of property. In the instant case, part of the proceeds from the sale is, in reality, a recovery of amounts previously deducted for Federal income tax purposes. Thus, that part is not to be treated as gain from the sale of assets, but, rather, is subject to the rule that a recovery of an amount previously deducted constitutes ordinary income to the extent of a prior tax benefit. See Rev. Rul. 60–49, C.B. 1960–1, 148; *Central Building and Loan Association* v. *Commissioner*, 34 T.C. 447 (1960); *First State Bank of Stratford* v. *Commissioner*, 168 Fed. (2d) 1004 (1948), certiorari denied, 335 U.S. 867 (1948).

In view of the foregoing, it is held that in the instant case the portion of the proceeds representing a recovery of the amounts of such items which previously had been deducted for Federal income tax purposes is to be treated as ordinary income to the corporation under section 61 of the Code and not as nonrecognized gain under the provisions of section 337(a) of the Code.

A sale by a corporation of its assets to a new corporation formed by the management of the selling corporation with the 12-month period following the adoption of a plan of complete liquidation. See Rev. Rul. 61–156, page 62.

PART III.—CORPORATE ORGANIZATIONS AND REORGANIZATIONS

Subpart B.—Effects on Shareholders and Security Holders

SECTION 355.—DISTRIBUTION OF STOCK AND SECURITIES OF A CONTROLLED CORPORATION

26 CFR 1.355–1: Distribution of stock and securities of controlled corporation. Rev. Rul. 61–198[1]

The Internal Revenue Service will not follow the decision of the United States Court of Appeals for the Sixth Circuit in *Commis-*

[1] Based on Technical Information Release 339, dated October 3, 1961.

sioner v. *Edmund P. and Virginia Coady*, 289 Fed. (2d) 490 (1961), affirming 33 T.C. 771 (1960), Nonacq. C.B. 1960–2, 8.

In the *Coady* case, "C" corporation, one functionally integrated business, transferred half of its business assets to Coady Company, a newly formed corporation, taking back all of the latter's stock, which it distributed to taxpayer (who owned fifty per cent of the outstanding stock of "C") in exchange for all of his stock in "C" corporation. The Tax Court of the United States, with six dissents, held that section 355 of the Internal Revenue Code of 1954 was applicable and that the distribution to the taxpayer of the Coady Company's stock accordingly qualified for nonrecognition of taxable gain. The reviewing court affirmed.

The decision, one of first impression, holds invalid the provision of the applicable Treasury regulations (section 1.355–1(a) of the Income Tax Regulations, promulgated December 2, 1955) which permits, without recognition of taxable gain to the shareholders or security holders, the separation of a corporation or corporations actively conducting two or more existing businesses but expressly provides that section 355 of the Code does not apply to the division of a single business.

Although there was no basis for request of certiorari to the Supreme Court of the United States in this case and certiorari was not applied for, the decision will not be followed as a precedent in the disposition of similar cases, and the Internal Revenue Service's position will be maintained pending further judicial test of the Treasury regulations.

Subpart D.—Special Rule; Definitions

SECTION 368.—DEFINITIONS RELATING TO CORPORATE REORGANIZATIONS

26 CFR 1.368–1: Purpose and scope of exception of reorganization exchanges. Rev. Rul. 61–156

(Also Sections 331, 337; 1.331–1, 1.337–1.)

A transaction cast in the form of a sale by one corporation of its assets to a newly organized corporation (in which the shareholders of the "selling" corporation will own 45 percent of the outstanding stock) and a subsequent liquidation of the "selling" corporation may be considered, in substance, as a reorganization under section 368 of the Internal Revenue Code of 1954, rather than a transaction governed by the provisions of sections 337 and 331 of the Code. Revenue Ruling 56–541, C.B. 1956–2, 189, revoked.

Advice has been requested whether the transaction described below should be treated, for Federal income tax purposes, as a sale of corporate assets to a newly organized corporation followed by the liquidation of the "selling" corporation under sections 337 and 331 of the Internal Revenue Code of 1954, or whether the transaction should be treated as a reorganization within the meaning of section 368 of the Code.

Within a 12-month period following the adoption of a plan of complete liquidation, a corporation sold substantially all of its assets to a new corporation formed by the management of the selling cor-

poration. The "purchasing" corporation paid 18,000x dollars for the assets as follows:

(a) 2,025x dollars in shares of its stock equal to 45 percent of all the shares to be issued,

(b) 4,975x dollars in long-term notes, and

(c) 11,000x dollars in cash obtained through a first mortgage borrowing on the assets acquired.

Immediately thereafter, the new corporation sold shares of its stock, equal to 55 percent of all the shares to be issued, to the public through underwriters.

The "selling" corporation was then completely liquidated, paying off its funded and unfunded liabilities and distributing the balance of its assets, including the 45 percent stock interest in the purchasing corporation, the long-term notes, and cash to its shareholders. As a result of the transaction, the business enterprise continued without interruption in the corporate form with a substantial continuing stock interest on the part of those persons who were shareholders in the selling corporation.

Section 1.331–1(c) of the Income Tax Regulations provides as follows:

> A liquidation which is followed by a transfer to another corporation of all or part of the assets of the liquidating corporation or which is preceded by such a transfer may, however, have the effect of the distribution of a dividend or of a transaction in which no loss is recognized and gain is recognized only to the extent of "other property." See sections 301 and 356.

In this case, if the issuance of stock to the new investors is disregarded, there is clearly a mere recapitalization and reincorporation coupled with a withdrawal of funds. The withdrawal would be treated either under section 356(a) of the Code as "money or other property" received in connection with a reorganization exchange of stock for stock, or under section 301 of the Code as an unrelated distribution to the shareholders.

The issuance of stock to new investors can be disregarded as being a separate transaction, since even without it the dominant purpose—to withdraw corporate earnings while continuing the equity interest in substantial part in a business enterprise conducted in corporate form—was fully achieved. The issuance of stock to new investors was not needed to implement the dominant purpose and, therefore, the rest of the transaction was not fruitless without it and so dependent on it.

The transaction was shaped so as to make it essentially "a device whereby it has been attempted to withdraw corporate earnings at capital gains rates by distributing all the assets of a corporation in complete liquidation and promptly reincorporating" them. See Conference Report No. 2543, 83d Cong., to accompany H.R. 8300 (Internal Revenue Code of 1954), page 41.

It was not intended by Congress that such a device should obtain the benefits of section 337 and avoid dividend taxation. In substance there was no reality to the "sale" of corporate assets or to the "liquidation" of the selling corporation, since each was only a formal step in a reorganization of the existing corporation. The entire transaction was consummated pursuant to a plan of reorganization which read-

justed interests in property continuing in a modified corporate form. Sections 1.368–1(b) and 1.368–2(g) of the regulations.

The newly formed "purchasing" corporation was utilized to effect, in substance, a recapitalization and a change in identity, form, or place of organization of the "selling" corporation and, at the same time, to withdraw accumulated earnings from the corporate enterprise for the benefit of the shareholders, while they nevertheless continued a substantial equity interest in the enterprise.

The fact that the shareholders of the "selling" corporation own only 45 percent of the stock of the "purchasing" corporation because of the public stock offering does not dispose of the reorganization question. A surrender of voting control, or ownership of less than 50 percent of the stock of a newly-formed corporation, does not in itself mark a discontinuity of interest. In *John A. Nelson Co.* v. *Helvering*, 296 U.S. 374, Ct.D. 1062, C.B. XV–1, 274 (1936), the Supreme Court of the United States held that there was a "reorganization" even though the shareholders of the acquired corporation received less than half of the stock of the acquiring corporation and received only nonvoting preferred stock therein. It is necessary only that the shareholders continue to have a definite and substantial equity interest in the assets of the acquiring corporation.

In view of the foregoing, it is held that the transaction here described constitutes a reorganization within the meaning of sections 368(a)(1) (E) and (F) of the Code. No gain or loss is recognized to the "selling" corporation on the exchange of property, as provided by section 361 of the Code. The basis of the assets in the hands of the "purchasing" corporation will be the same as in the hands of the "selling" corporation, as provided in section 362(b) of the Code. No gain or loss is recognized under section 354 of the Code on the exchange of the stock of the "selling" corporation for stock of the "purchasing" corporation pursuant to the plan of reorganization.

With regard to the stockholders' withdrawal of money and other property from the corporate solution, it is necessary to determine whether such withdrawal is to be treated as "boot" received as part of the consideration for their stock in the "selling" corporation in accordance with section 356(a) of the Code or as a separate dividend distribution taxable in accordance with the provisions of section 301 of the Code. See sections 1.301–1(1) and 1.331–1(c) of the regulations and *J. Robert Bazley* v. *Commissioner*, 331 U.S. 737, Ct.D. 1687, C.B. 1947–2, 79, rehearing denied and amended, 332 U.S. 752 (1947).

Under section 356(a)(1) of the Code, gain would be recognized to the shareholders of the "selling" corporation upon the surrender of their shares of stock in exchange for stock of the "purchasing" corporation, its long-term notes, cash, and other assets, but in an amount not in excess of the sum of cash and the fair market value of the long-term notes and other assets received. Under section 356(a)(2) of the Code, such gain would be taxable as a dividend to each shareholder to the extent of his ratable share of the undistributed earnings and profits of the corporation accumulated after February 28, 1913; the remainder, if any, would be treated as gain from the exchange of property. Under section 301 the distribution would be taxable as a dividend to the same extent as a dividend formally declared in the same amount.

In this case, viewing the issuance of stock of the "purchasing" corporation to new investors as a transaction separate from the reorganization, it is concluded that the distribution to stockholders of the "selling" corporation of the cash, long-term notes, and other assets should be treated as a distribution under section 301 of the Code.

In view of the conclusions reached herein, reconsideration has been given to Revenue Ruling 56–541, C.B. 1956–2, 189, which holds under similar circumstances that a nontaxable corporate sale of assets was effected under section 337 of the Code and that distributions to the shareholders were to be treated as in full payment in exchange for their stock under a plan of complete liquidation of the old corporation. The conclusions reached in the instant case are equally applicable to the question involved in Revenue Ruling 56–541. Accordingly, Revenue Ruling 56–541, C.B. 1956–2, 189, is revoked.

Under authority of section 7805(b) of the Code, this Revenue Ruling will not be applied retroactively in any case in which transactions were consummated prior to August 21, 1961, in reliance on the Service's position as published in Revenue Ruling 56–541 and a retroactive application would be to the taxpayer's detriment.

SUBCHAPTER D.—DEFERRED COMPENSATION, ETC.

PART I.—PENSION, PROFIT-SHARING, STOCK BONUS PLANS, ETC.

SECTION 401.—QUALIFIED PENSION, PROFIT-SHARING, AND STOCK BONUS PLANS

26 CFR 1.401–1: Qualified pension, profit-sharing and stock bonus plans. Rev. Rul. 61–121

> The death benefit payable under the provisions of a qualified employees' pension plan to a widow of an employee who died prior to normal retirement age may be regarded in this case as "incidental" within the meaning of section 1.401–1(b)(1)(i) of the Income Tax Regulations, where the value of such benefit does not exceed the death benefit that would have been payable had the benefit been funded under a typical retirement income contract.

Advice has been requested whether death benefits for widows and children under the provisions of an employees' pension plan intended to qualify under section 401(a) of the Internal Revenue Code of 1954 may be regarded as "incidental" within the meaning of the regulations under that section.

An employees' pension plan covers employees who have completed five years of service, provided they have not then attained normal retirement age 65. The normal annual retirement benefits, for those retiring on or after January 1, 1959, are as follows: for past service, one percent of 1958 compensation multiplied by the number of years of service prior to January 1, 1959, and after the fifth anniversary of service; for future service, one and one-half percent of annual compensation for each year of participation after December 31, 1958. The minimum normal retirement benefit is $20 per month. Employees contribute three percent of compensation.

Early retirement is permitted in the case of an employee who terminates employment after age 55 with at least ten years of credited service, and the employee is entitled to a deferred annuity beginning at age 65 based on service to the date of the termination of his employment, or, with the consent of the retirement committee, an actuarially equivalent annuity beginning at an earlier age. There is no vesting except in the case of normal or early retirement, and a terminated employee is entitled only to a return of his own contributions accumulated with interest.

Pensions are paid to a widow and minor children of an employee where he dies while in the service of the employer and between the ages of 60 and 64, inclusive, having completed 20 or more years of service of which at least 15 were credited under the plan. The widow's benefit is paid until death or remarriage, and each surviving child not over age 18 is paid a benefit until his 19th birthday. Such benefits are based on the participant's "anticipated retirement income," which is the pension that would have been payable to the participant at normal retirement date if he had continued in service to that date earning the compensation in effect at the time of death. The widow's benefit is 50 percent of "anticipated retirement income," with ten percent of such income to each child if there is a widow surviving, or 20 percent of such income to each child otherwise. There is an aggregate maximum of 50 percent of "anticipated retirement income" to all children combined if a widow survives, or 100 percent otherwise. The widow's benefit is reduced actuarially if she was more than ten years younger than her husband.

Section 1.401–1(b)(1)(i) of the Income Tax Regulations permits death benefits in qualified pension plans if those benefits are "incidental." This provision of the regulations recognizes that in many cases benefits under pension plans are funded by means of typical retirement income contracts, under which the death benefits prior to retirement are equal to 100 times the anticipated monthly lifetime pension, or the accumulated reserve if greater.

Actuarial computations show that the value of a widow's benefit under the plan generally would not exceed the reserve accumulated for the employee's retirement benefits under a level premium method of funding similar to that used in typical retirement income contracts. In the few possible situations where the value of the widow's benefits could exceed the reserve, the amount of the excess would be inconsequential. Also, in view of the circumstances under which the children's benefits are paid in this case, they may be ignored for the purpose of determining whether the death benefits are incidental.

Accordingly, it is held that the death benefits in this case generally would not exceed those that would have been payable had the benefits been funded under typical retirement income contracts and, therefore, may be regarded as "incidental" within the meaning of section 1.401–1(b)(1)(i) of the regulations.

Rev. Rul. 61-157

Revised compilation of guides applicable to the qualification of pension, annuity, profit-sharing, and stock bonus plans under section 401(a) of the Internal Revenue Code of 1954, as of August 28, 1961.

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PART 1.—INTRODUCTION

(a) BACKGROUND.—A trust created or organized in the United States and forming part of a stock bonus, pension, or profit-sharing plan of an employer for the exclusive benefit of his employees or their beneficiaries constitutes a qualified trust under section 401(a) of the Internal Revenue Code of 1954 if it meets the further requirements set forth in such section as to contributions, nondiversion, coverage, and nondiscrimination in contributions or benefits. A qualified trust is exempt from tax under section 501(a) unless exemption is denied under section 502 because it is operated as a feeder organization, or under section 503 for having engaged in a prohibited transaction. An exempt trust, however, is subject to tax under section 511 on its un-

related business taxable income. Various tax benefits to employers, employees and their beneficiaries stem from an exempt trust. A trust, however, is not a prerequisite for such benefits. For example, deferment of tax and the long-term capital gain treatment are also provided for employees and their beneficiaries under section 403(a), and deductions for employer contributions are allowable under section 404(a)(2), in the case of nontrusteed annuity plans which meet the requirements of such sections, inclusive of the provisions under paragraphs (3) through (6) of section 401(a), relating to nondiscrimination.

(b) PURPOSE.—It is the purpose of this Revenue Ruling to bring up-to-date the guides which have been developed as a result of the determination of various issues relative to the qualification of plans and trusts, to correlate the rules which have been evolved with the applicable provisions of the Internal Revenue Code of 1954 and the corresponding Income Tax Regulations, and to codify various individual releases, except in cases where to do so would merely be repetitious or cumulative, and, in such cases, reference is made to the specific release in point. The issues presented are not all-inclusive but have been found to be present in many plans. It is contemplated that as new issues of general import arise additional releases will be issued. As to the effect of a new position on a case in which a ruling or determination letter had been issued see Revenue Ruling 54–172, C.B. 1954–1, 394, and P.S. No. 35 Revised, November 16, 1944.

(c) RULES PREVIOUSLY PROMULGATED.—Revenue Ruling 33, C.B. 1953–1, 267, sets forth rules which had been developed with respect to the qualification of plans under section 165(a) of the Internal Revenue Code of 1939, and Revenue Ruling 57–163 C.B. 1957–1, 128, contains guides for qualification of plans under section 401(a) of the Internal Revenue Code of 1954 as such guides were in effect on April 22, 1957, the date of publication of Internal Revenue Bulletin 1957–16 through which the Revenue Ruling was released. Certain parts of such rules had previously been modified by individual releases but, to the extent that inconsistencies still exist with the views here expressed, they are accordingly further modified.

(d) REFERENCES.—Certain issues are common to all types of plans while others are present only in particular categories, such as pension and annuity plans or profit-sharing and stock bonus plans. The various issues are discussed in their relationship to the applicable provisions of the Internal Revenue Code of 1954 and the corresponding regulations. Rulings listed in the appendix are incorporated by reference and made a part hereof, with appropriate modifications where necessary to conform with the Internal Revenue Code of 1954 and with this release. The omission of any rulings from the appendix is not to be construed as a revocation or modification of such rulings. Reference is made only to those rulings which are within the context of the particular guides considered. Rulings published in the Internal Revenue Bulletin are cited by specific reference. P.S. releases have also been made public although not published in the Bulletin. Copies are available in the Offices of District Directors of Internal Revenue and in the National Office in Washington. The present status of the respective releases is shown in the appendix.

PART 2.—QUALIFIED PENSION, ANNUITY, PROFIT-SHARING, AND STOCK BONUS PLANS

SECTION 401(A) OF THE INTERNAL REVENUE CODE OF 1954—REGULATIONS SECTION 1.401–1

(a) APPLICABLE PLANS.—The provisions of section 401(a) are applicable only to trusteed pension, profit-sharing, and stock bonus plans, and only the requirements of paragraphs (3) through (6) of such section also apply to nontrusteed annuity plans. For definitions of plans of these types, see the Income Tax Regulations: section 1.401–1(b)(1)(i) for pension plans, section 1.401–1(b)(1)(ii) for profit-sharing plans, section 1.401–1(b)(1)(iii) for stock bonus plans, and section 1.404(a)–3(a) for annuity plans.

(b) DOMESTIC TRUST.—A qualified employees' trust must be organized or created in the United States and maintained at all times as a domestic trust. If, however, a foreign situs trust meets the requirements of section 401(a) in all other respects, employers making contributions thereunder are allowed deductions within the applicable limits, as provided for in section 404(a)(4), and beneficiaries of such trust are granted the same tax treatment, in accordance with section 402(c), as is applicable to beneficiaries of a domestic trust. It should be noted however that unless the nonresident alien individual is engaged in a trade or business in the United States or provision is otherwise made by treaty, the long-term capital gain treatment does not apply to distributions to such an individual and withholding of tax applies to the distributions under either a domestic or foreign situs trust. See sections 871 and 1441 of the Code and regulations thereunder.

(c) PLAN AND TRUST OF MULTIPLE EMPLOYERS.—A single plan and trust may be maintained by two or more employers, regardless of their affiliation, but each must meet all applicable requirements. See section 1.401–(d) of the regulations and P.S. No. 14, dated August 24, 1944. Where, under specified conditions, separate qualified and exempt trusts pool their funds in a group trust created to provide diversification of investments, the group trust may also be exempt and the status for exemption of the separate trusts will not be adversely affected. See Rev. Rul. 56–267, C.B. 1956–1, 206.

(d) LIFE INSURANCE BENEFITS.—A qualified plan may not provide only such benefits as are furnished through the purchase of ordinary life insurance contracts which may be converted to life annuities at the normal retirement date. See Rev. Rul. 54–67, C.B. 1954–1, 149. Life insurance protection may, however, be provided under a qualified plan provided that such protection is merely an incidental feature of the plan. In the case of a pension or annuity plan, the life insurance benefit is deemed to be incidental where the insurance protection is not greater than 100 times the monthly annuity, e.g., $1,000 of life insurance for each $10 of monthly annuity. See Rev. Rul. 60–83, C.B. 1960–1, 157. In the case of a profit-sharing plan which provides for the use of trust funds to purchase and pay premiums on ordinary life insurance contracts, the insurance feature is deemed to be incidental if: (1) the aggregate premiums for life insurance in the case of each participant is less than one-half of the aggregate of the contributions allocated to him at any particular time, and (2) the

plan requires the trustee to convert the entire value of the life insurance contract at or before retirement into cash, or to provide periodic income so that no portion of such value may be used to continue life insurance protection beyond retirement, or to distribute the contract to the participant. See Rev. Rul. 54–51, C.B. 1954–1, 147, as amplified both by Rev. Rul. 57–213, C.B. 1957–1, 157, and Rev. Rul. 60–84, C.B. 1960–1, 159. Where life insurance benefits are applied to reduce employer contributions under a pension plan, amounts contributed by the employer for such insurance constitute advance funding and are not currently deductible. See Rev. Rul. 55–748, C.B. 1955–2, 234.

(e) EMPLOYEE PARTICIPANTS.—A qualified plan must benefit employees or their beneficiaries exclusively. Such a plan cannot be maintained where there are no employees, active or retired, who are covered thereunder. See Rev. Rul. 55–629, C.B. 1955–2, 588. An arrangement does not qualify as a plan under section 401(a) if the benefits which it provides are not payable to an employee but only to his beneficiary upon his death. See Rev. Rul. 56–656, C.B. 1956–2, 280.

(1) *Partners.*—Partners are not employees and therefore are not eligible to participate in a qualified plan. See I.T. 3350, C.B. 1940–1, 64, and P.S. No. 23, dated September 2, 1944. Neither are they to be credited for services as partners prior to becoming employees in a successor corporation, either for prior service benefits or for meeting the eligibility requirements. See also Section 1361(d) of the Code which provides that a partner or proprietor of an unincorporated business enterprise electing to be taxed as a corporation shall not be considered an employee for the purpose of participating in a qualified plan.

(2) *Associates.*—Where an organization is classified as an association taxable as a corporation, and an employer-employee relationship exists between the association and the persons who are associates therein, such associates, if otherwise eligible, may be included in a plan which is intended to qualify under section 401(a) of the Code. The fact that an organization establishes a plan under section 401(a) is not determinative of whether such organization will be classified as a partnership or as an association taxable as a corporation. See Revenue Ruling 57–546, C.B. 1957–2, 886, modifying Revenue Ruling 56–23, C.B. 1956–1, 598. Rules for determining whether an organization is a trust, a partnership, or an association taxable as a corporation are set forth in the Regulations on Procedure and Administration pertaining to section 7701 of the Code. See T.D. 6503, C.B. 1960–2, 409. The pertinent provisions of these regulations relate generally to taxable years beginning after December 31, 1960.

(3) *Stockholder participants.*—Stockholders who are bona fide employees of a corporation may participate in the corporation's plan to the same extent as other employees. If, however, the plan is designed as a subterfuge for the distribution of profits to stockholders, it will not qualify as a plan for the exclusive benefit of employees. The plan must not be weighted in favor of stockholder-employees with respect to eligibility requirements or with respect to contributions or benefits. See section 1.401–1(b)(3) of the Income Tax Regulations and I.T. 4020, C.B. 1950–2, 61.

(4) *Attorneys and other practitioners.*—An attorney, or other professional person, may be a bona fide employee, and, as such, eligible to participate in a qualified plan. The mere fact that a professional person has an independent income from the practice of his profession will not necessarily preclude him from participating in such a plan. He must, however, be an employee for all purposes, including coverage as an employee for social security or a similar public program, if applicable to other employees, and for income tax withholding purposes. Thus, if his actual employment for such purposes commences as of a certain date, he is not to be credited for services prior thereto, such as, for example, for the purposes of meeting the years of service requirements to be eligible to participate in the plan or to obtain benefits based on past services.

(5) *Insurance agents.*—Section 7701(a)(20) of the Code provides that for the purpose of contributions to, and distributions from, a stock bonus, pension, or profit-sharing plan or trust, or under an annuity plan, the term "employee" shall include a full-time life insurance salesman who is considered an employee for the purpose of the Federal Insurance Contributions Act, or in the case of services performed before January 1, 1951, who would be considered an employee if his services were performed during 1951. Thus, the same rules apply with respect to treating full-time life insurance salesmen as employees for inclusion in a qualified plan as are applicable to the tax treatment for old-age, survivors, and disability insurance purposes. This inclusion does not, however, extend to insurance brokers and others who are not full-time life insurance agents within the purview of section 3121(d)(3)(B) of the Code.

(f) FUNDED PLAN.—A qualified plan must be a funded plan. Contributions are made either to a trust or paid as premiums under insurance contracts. In pursuance with an established funding method, however, employer contributions may be deferred. Thus, a qualified pension plan may provide that current contributions be made by employees only, but that the employer is obligated to pay the full amount of the stipulated retirement benefits to each retired employee-participant after the funds in the trust forming a part of such plan have been fully exhausted. See Rev. Rul. 54–152, C.B. 1954–1, 149. However, see part 5(f).

(g) UNRELATED BENEFITS.—A qualified pension plan does not provide for the payment of benefits not customarily included in that type of plan, such as layoff benefits or benefits for sickness, accident, hospitalization, or medical expenses. See the last sentence of section 1.401–1(b)(1)(i) of the regulations. The annuity portion of a contract with an insurance company by means of which an employees' nontrusteed annuity plan is funded may, however, if otherwise satisfactory, meet the applicable requirements for qualification even though the contract also provides separate group term life insurance and accident and health insurance. See Rev. Rul. 56–633, C.B. 1956–2, 279.

(h) PLAN OF DEFERRED COMPENSATION.—A qualified plan is a plan of deferred compensation. A pension plan provides systematically for the payment of definitely determinable benefits to employees over a period of years, usually for life, after retirement. A profit-sharing

plan must provide a definite predetermined formula for allocating contributions among participants and for distributing the accumulated funds after a fixed number of years, the attainment of a stated age, or upon the prior occurence of some event such as layoff, illness, disability, retirement, death, or severance of employment. The term "fixed number of years" is considered to mean at least two years. See Rev. Rul. 54–231, C.B. 1954–1, 150. A stock bonus plan is similar to a profit-sharing plan except that the contributions by the employer are not necessarily dependent upon profits and the benefits are distributable in stock of the employer company. See section 1.401–1(b)(1)(iii) of the regulations.

(i) EMPLOYEE WITHDRAWALS UNDER A PENSION PLAN.—A qualified pension plan may provide for the payment of benefits, such as disability and death benefits, prior to normal retirement if such benefits are only incidental to the main purpose of the plan. Restrictions and limitations, however, apply to the withdrawal of funds by employees in times of financial need or otherwise.

(1) *Funds consisting of employer contributions or increments.*—A pension plan must not permit participants, prior to any severance of employment or the termination of the plan, to withdraw all or a part of the funds accumulated on their behalf consisting of employer contributions or increments. A similar provision in a profit-sharing plan, however, may, under appropriate circumstances be acceptable. See Rev. Rul. 56–693, C.B. 1956–2, 282, modified by Rev. Rul. 60–323, C.B. 1960–2, 148.

(2) *Discontinuance of participation.*—Upon discontinuance of his participation under a pension plan an employee may be permitted to withdraw his own contributions together with an amount which represents the increments actually earned thereon, but not an amount in excess of such earnings. See Rev. Rul. 60–281, C.B. 1960–2, 146.

(3) *Employee voluntary contributions.*—A pension plan may provide for the withdrawals by participants of their voluntary contributions which are made in addition to compulsory contributions, where such withdrawals do not affect a member's participation in the plan, the employer's past or future contributions on his behalf, the basic benefits provided by both the participant's and employer's nonwithdrawable contributions, and no interest is allowed on contributions withdrawn either at the time of withdrawal or in computing benefits on retirement. See Rev. Rul. 60–323, C.B. 1960–2, 148.

(4) *Conversion of contributory to noncontributory plan.*—Where a contributory pension plan is amended to provide for employer contributions only, provision may be made for a refund of employee contributions if discrimination does not result in favor of employees who are officers, shareholders, supervisors, or highly compensated. See Rev. Rul. 61–79, C.B. 1961–1, 138.

(j) WRITTEN PROGRAM.—A qualified plan must be a definite written program setting forth all provisions essential for qualification. See section 1.401–1(a)(2) of the regulations. In the case of a trusteed plan, there must be a valid existing trust, complete in all respects and recognized as such under the applicable local law, pursuant to a plan in effect, except that in the case of a trust of an employer on the accrual

basis, if only the trust corpus is lacking at the close of the first taxable year, it may be furnished no later than the due date of the employer's return, plus extensions of time in which to file. See Mim. 5985, C.B. 1946–1, 72, as modified by Rev. Rul. 57–419, C.B. 1957–2, 264. The trust must be evidenced by an executed written document setting forth the terms thereof. See Mim. 6394, C.B. 1949–1, 118, and Rev. Rul. 56–673, C.B. 1956–2, 281. In the case of a nontrusteed annuity plan which is evidenced only by contracts with an insurance company, the plan is not in effect until such contracts are executed and issued. Where, however, the plan is separate and apart from a group annuity contract, or annuity contracts, the plan may be in effect before the close of the first taxable year where appropriate steps are taken to establish the plan, and the insurance contracts have been applied for, the application has been accepted by the insurance company, the contracts or abstracts have been prepared in sufficient detail defining all terms, at least a part payment of the premiums due has been irrevocably made, and the plan has been communicated to employees. See Rev. Rul. 59–402, C.B. 1959–2, 122, modifying Mim. 6020, C.B. 1946–1, 74.

(k) COMMUNICATION TO EMPLOYEES.—Employees are to be apprised of the establishment of a qualified plan and the salient provisions thereof. The most effective way of doing so is to furnish each employee with a copy of the plan. Where this is not feasible, however, various substitutes may be used. It will be sufficient that a booklet summarizing the plan in all its essential features be furnished the employees, or that a notice be posted on the company's bulletin board, which must be in conspicuous view, stating that a plan has been established, setting forth the type thereof, specifying the eligibility requirements, containing a synopsis of all benefits provided thereunder, indicating whether employees are to contribute and, if so, the amount or rate of contributions, and defining the vesting provisions, and, in the case of a profit-sharing or stock bonus plan, setting forth the employer contribution commitment, if any. In all cases of substitutes for furnishing employees with copies of the plan, the medium used must apprise the employees that a copy of the complete plan may be inspected at a designated place on the company's premises during stated times.

(l) PROFIT-SHARING AND STOCK BONUS PLANS OF AFFILIATED COMPANIES.—In the case of a profit-sharing plan, or a stock bonus plan in which contributions are determined with reference to profits, of an affiliated group of corporations within the purview of section 1504 of the Code, contributions may be made by other members of the group for the benefit of employees of a corporation which is prevented from making a contribution because it lacks, or has insufficient, current or accumulated earnings or profits, to the extent and in the manner provided in section 404(a)(3)(B) of the Code and section 1.404(a)–10 of the regulations.

(m) FEEDER PLAN.—A stock bonus or profit-sharing plan which provides that the funds therein may be used to meet the costs of a pension or annuity plan operated concurrently and covering the same employees, if and when the employer suspends contributions to the latter plan, is generally called a "feeder" plan and, as such, does not qualify because it relieves the employer from contributing to the pension or annuity plan and is, therefore, not for the exclusive benefit

of the employees or their beneficiaries. See section 1.401–1(b)(3) of the regulations. An employee who has a vested right under a stock bonus or profit-sharing plan may, however, if the plan so provides, authorize a transfer of all or a part of his vested interest in order to make up a deficiency in the employer's contribution under a pension or annuity plan. In such case, the amount transferred is includible in the employee's gross income as though a distribution of such interest had been made. See P.S. No. 37, dated October 7, 1944. It should also be observed that a feeder plan is different from a feeder organization. As to the latter, see paragraph (r)(4) hereof and section 502 of the Code which denies exemption under section 501 to an organization which is operated for the primary purpose of carrying on a trade or business for profit even though all of its profits are payable to one or more organizations exempt under section 501.

(n) DEFINITELY DETERMINABLE BENEFITS.—Benefits under a qualified pension plan must be definitely determinable. See section 1.401–1(b)(1)(i) of the regulations. Benefits are not definitely determinable if they may be suspended after retirement without cause. The plan may provide, however, that benefits shall be suspended for any period of time during which primary insurance benefits under the Federal Social Security Act are discontinued because of employment after retirement date. See Rev. Rul. 82, C.B. 1953–1, 288. Benefits which vary with the increase or decrease in the market value of the assets from which such benefits are payable, or which vary with the fluctuation of a specified and generally recognized cost-of-living index, are consistent with a plan providing for definitely determinable benefits. See Rev. Rul. 185, C.B. 1953–2, 202.

(o) CONTINGENCY OR SURPLUS RESERVE.—The practice of contributing the full amount of annual premiums under an insured pension plan, without reduction for accumulated dividends and regardless of the amount of the allowable deduction limitation, would result in the creation of a contingency or surplus reserve. If a significant part of a trust fund consists of such a contingency or surplus reserve, the plan's qualification could be adversely affected. If the advance funding, however, is minor in relation to the actuarial liability under the plan, if there is no possibility of the reversion of a substantial amount to the employer on termination of the plan, and if the advance funding is exclusively for the benefit of the employees or their beneficiaries, such advance funding would not adversely affect the qualification of the plan. Advance funding does not constitute a current deduction. Accordingly, the deduction otherwise allowable to the employer for any taxable year, under section 404(a) of the Code, must be reduced by the amount of dividends earned, and interest credited on accumulations thereof, in the current or next preceding taxable year. See Rev. Rul. 60–33, C.B. 1960–1, 152.

(p) PERMANENCY.—A qualified plan is a permanent and continuing program. A plan which is set up during years of high tax rates and is abandoned within a few years without a valid business reason when profits fall off does not satisfy this requirement. Also, especially in the case of a pension plan under which benefits are funded at a higher rate for employees in whose favor discrimination is prohibited than for other employees, if the plan is discontinued before ample provision is made for comparable benefits for such other employees,

it will be deemed not to have been a bona fide program for the exclusive benefit of employees in general from its inception. In the case of a profit-sharing plan, merely making a single or occasional contribution out of profits for employees does not satisfy the requirement for permanency. There must be recurring and substantial contributions. See section 1.401–1(b)(2) of the regulations. For a more detailed discussion of the applicable principles and illustrative cases, see Mim. No. 6136, C.B. 1947–1, 58, as modified by Rev. Rul. 55–60, C.B. 1955–1, 37. See also Exhibit "A" of Rev. Proc. 56–12, C.B. 1956–1, 1029, for information to be filed for a determination as to the effect of a curtailment or termination of a plan on its prior qualification; P.S. No. 56, dated June 27, 1946, as to notice by the trustee on termination of a plan; P.S. No. 57, dated August 5, 1946, as modified by Rev. Rul. 56–596, C.B. 1956–2, 288, as to the effect of a suspension of contributions; and P.S. Nos. 64 and 67, dated November 9, 1950, and April 26, 1951, respectively, and Rev. Rul. 55–681, C.B. 1955–2, 585, as to union negotiated plans. A qualified profit-sharing plan may, under appropriate circumstances, provide that an employee may elect each year to participate in the trust forming a part of such plan or to accept his share in cash. See, however, parts 4(d) and 5(a) hereof as to meeting the requirements for coverage and nondiscrimination in contributions or benefits. A profit-sharing plan which does not contain a definite contribution formula may qualify if all other applicable requirements are met. See section 1.401–1(b)(1)(ii) of the regulations and Rev. Proc. 56–22, C.B. 1956–2, 1380.

(q) DESIGNATION OF BENEFICIARIES.—Beneficiaries of employees under a qualified plan may be designated by the respective participants without restriction, or they may be restricted under the plan to specified persons, or to a group of persons, who are the natural objects of the employee's bounty, his estate, or his dependents. See Rev. Rul. 54–398, C.B. 1954–2, 239.

(r) INVESTMENT OF TRUST FUNDS.—Investments of an exempt employees' trust are subject to the following: (1) As a function of a trust which under section 401(a) of the Code, is part of a plan of an employer for the exclusive benefit of his employees or their beneficiaries, the investments must be consistent with such purpose. (2) They must not constitute prohibited transactions, as defined under section 503. (3) Investments which result in unrelated business taxable income subject the trust to tax under section 511 on such income. (4) They must not be used to operate a feeder organization.

(1) *Exclusive benefit requirement.*—The primary purpose of benefiting employees or their beneficiaries must be maintained with respect to investments of trust funds as well as in other activities of the trust. This requirement, however, does not prevent others from also deriving some benefit from a transaction with the trust. For example, a sale of securities to the trust at a profit benefits the vendor, but if the purchase price is not in excess of the fair market value of the securities and the applicable investment requisites have been met, the transaction is consisting with the requirement of benefiting employees or their beneficiaries. These requisites are: (1) the cost must not exceed fair market value at the time of purchase, (2) a fair return commensurate with the prevailing rate must be provided, (3) suffi-

cient liquidity is to be maintained so as to permit distributions in accordance with the terms of the plan, and (4) the safeguards and diversity that a prudent investor would look to are to exist. Upon compliance with these requisites, if the trust instrument and local law permit investments in the stock or securities of the employer, such investments would be deemed consistent with the purposes of section 401(a). The District Director, however, is to be notified if stock or securities of the employer is acquired by the trust so that a determination may be made whether the trust serves any purpose other than constituting part of a plan for the exclusive benefit of employees. See section 1.401–1(b)(5)(ii) of the regulations. Such notification is to be made as part of the annual information return, Form 990–P, unless an advance determination letter is requested and, if so, at the time of making a request to the appropriate District Director of Internal Revenue for such letter. The notification is to include the information called for in Exhibit "B", or Exhibit "B–1", in the alternative, of Revenue Procedure 56–12, C.B. 1956–1, 1029, and certified to by the accounting or other responsible officer.

(2) *Prohibited transactions.*—Exemption will be denied to an employees' trust which engages in a prohibited transaction within the purview of section 503 of the Code. Transactions with the employer-grantor of the trust, or related or affiliated interests, which are prohibited are set forth in section 503(c). Special rules, however, apply to the requirement for adequate security in the case of obligations which are acquired by the trust under the conditions of section 503(h), and in the case of loans to employers in the unincorporated stock brokerage business in compliance with the requirements of section 503(i).

(3) *Unrelated business income.*—An exempt employees' trust is taxable under section 511 of the Code on its unrelated business taxable income, as defined in section 512, which is derived from any unrelated trade or business, as defined in section 513. Special rules are set forth in section 514 with respect to business leases. If business lease indebtedness is incurred, rental income is includible in gross income in the ratio that the business lease indebtedness, at the close of the taxable year, bears to the adjusted basis of the property at such time.

(4) *Feeder organizations.*—An employees' trust which is operated for the primary purpose of carrying on a trade or business for profit is denied exemption under section 502 of the Code, even though all of its profits are payable to one or more exempt organizations.

(s) VALUATION OF SECURITIES ON INVENTORY DATE.—Any type of qualified plan which provides for distributions in accordance with amounts stated or ascertainable, credited to participants, as in the case of profit-sharing, stock bonus, and trusteed pension plans of the money-purchase type, must provide for a valuation of securities held by the trust, at least once a year, on a specified inventory date, in accordance with a method consistently followed and uniformly applied. The fair market value on the inventory date is to be used for this purpose. The respective accounts of participants are to be adjusted in accordance with the valuation. For example, if as a

result of a valuation on the inventory date, John Doe's account, which previously showed a balance of $1,000, is to be increased by one-tenth of one percent of the increase in the value of the trust assets, and such increase is $50,000, his interest is to be increased by $50.

(t) ALLOCATION OF STOCK BONUS AND PROFIT-SHARING FUNDS.—All funds in an exempt stock bonus or profit-sharing trust must be allocated to participants in accordance with a definite formula. Thus, no reserves are to be provided by withholding allocations from participants. If suspense accounts are maintained, provision is to be made for ascertaining the respective shares of participants in such accounts and such shares are to be included in the distribution.

PART 3.—IMPOSSIBILITY OF DIVERSION UNDER THE TRUST INSTRUMENT

SECTION 401(a)(2) OF THE INTERNAL REVENUE CODE OF 1954—REGULATIONS SECTION 1.401–2

(a) TRUST INSTRUMENT MUST MAKE PROHIBITED DIVERSION IMPOSSIBLE.—Section 401(a)(2) of the Code requires that under the trust instrument it must be impossible " * * * at any time prior to the satisfaction of all liabilities with respect to employees and their beneficiaries under the trust, for any part of the corpus or income to be (within the taxable year or thereafter) used for, or diverted to, purposes other than for the exclusive benefit of * * * employees or their beneficiaries * * *." The term "trust instrument" means a written document. Although an oral trust may be recognized under the applicable local law, section 401(a)(2) requires the trust instrument to make the prohibited diversion impossible. The trust instrument must definitely and affirmatively make it impossible for the nonexempt use or diversion to occur. See section 1.401–2(a)(2) of the regulations. The trust must also constitute a valid trust under the law in the jurisdiction to which it is subject. See Mim. 6394, C.B. 1949–1, 118; also Mim. 5985, C.B. 1946–1, 72, as modified by Rev. Rul. 57–419, C.B. 1957–2, 264.

(b) PAYMENT OF EMPLOYER'S CLAIMS.—A qualified trust may contain a spendthrift clause precluding the use of trust funds for the payment of debts or other obligations of participants and preventing a sale, transfer, or assignment of a participant's interest. It may, however, limit such prohibition so as not to be applicable to indebtedness due the employer. The repayment of a loan owing by an employee is for the economic benefit of the employee since it relieves him of a liability. If a trust did not contain a spendthrift clause so that an employee's creditors could reach his interest, the fund would still be for the exclusive benefit of the employees. Accordingly, the mere fact that the employer is the only one who has that right does not change the result. See Rev. Rul. 56–432, C.B. 1956–2, 284.

(c) CONDITIONAL PAYMENTS.—A provision in a newly established plan for the return of employer contributions only in the event that the Commissioner of Internal Revenue rules that the plan is not qualified does not, of itself, prevent qualification of the plan and exemption of the trust. The plan must be in full force and effect, and the nonreversionary provisions must otherwise prevent the nonexempt use

of the funds. It is only by the Commissioner's determination that the plan does not qualify that a recovery of employer contributions made prior to such determination is possible. Under such circumstances, the conditional payment, and the provision therefor, are held not to prevent qualification of the plan and exemption of the trust. See Rev. Rul. 60-276, C.B. 1960-2, 150.

(d) ERRONEOUS ACTUARIAL COMPUTATION.—Trust funds must not be used for purposes other than for the exclusive benefit of employees or their beneficiaries prior to the termination of the trust and the satisfaction of all liabilities with respect to employees and their beneficiaries under the trust, and, only then, may recovery be had in the case of a pension trust to the extent of any surplus existing because of an actuarial error. In determining whether any surplus exists on termination of a trust, and the amount thereof, all liabilities, contingent as well as fixed, with respect to employees and their beneficiaries under the trust must be taken into account. Fixed liabilities are the amounts required to provide the benefits payable to those who have become entitled to them. Contingent liabilities are the benefit credits accrued up to the time of termination of the trust for employees (and their beneficiaries) who might have become entitled to benefits if the trust had been continued indefinitely. If such liabilities are to be discharged by commuting the payments (other than through the purchase of insurance company contracts), the value thereof at the time of termination of the trust must be determined for this purpose by use of assumptions no less conservative in any respect than were used in determining costs during the previous life of the trust, and no discount for severances other than death may be assumed.

(e) NO REVERSION IN PROFIT-SHARING OR STOCK BONUS PLANS.—Allocations under profit-sharing and stock bonus plans are not predicated upon amounts actuarially necessary to provide stipulated retirement benefits. See I.T. 3660, C.B. 1944, 136. See also section 1.401-1(b)(1)(i) of the regulations to the effect that a plan designed to provide benefits for employees or their beneficiaries to be paid upon retirement or over a period of years after retirement will, for the purposes of section 401(a) of the Code, be considered a pension plan if the employer contributions under the plan can be determined actuarily on the basis of definitely determinable benefits, or, as in the case of money purchase pension plans, such contributions are fixed without being geared to profits. Consequently, in profit-sharing and stock bonus plans there can be no reversion of any kind since such plans do not provide benefits which are predicated on actuarial assumptions or computations.

(f) APPLICATION OF DIVIDENDS AND OTHER CREDITS UNDER GROUP ANNUITY CONTRACTS.—Provisions analogous to that set forth in section 401(a)(2) of the Code, prohibiting diversion of funds from exempt trusts, are contained in section 404(a)(2), relating to deductions of contributions under nontrusteed annuity plans, and in section 403(a)(2)(A)(ii), relating to the capital gains treatment for certain distributions under nontrusteed annuity plans. Section 404(a)(2), for example, requires that, where retirement annuities are purchased, refunds of premiums, if any, must be applied within the current taxable year or next succeeding taxable year towards the purchase of such

retirement annuities. To satisfy this requirement, there must be a definite written arrangement between the employer and the insurer, either as part of the annuity contract or by separate written direction from the employer to the insurer, or partly in one form and partly in the other, providing that:

(1) *Restriction on payment of credits or returns to employer.*—No credits or returns, other than those arising from corrections of errors in records or computations, such as misstated ages or similar corrections, may be paid to the employer prior to permanent discontinuance of contributions.

(2) *Application of dividends or other returns or credits.*—All dividends, experience rating credits, or employer surrender or cancellation credits ascertained prior to permanent discontinuance or contributions are to be applied regularly as they are determined toward the premiums next due for purchase of annuities under the plan before any further employer contributions are so applied.

(3) *Surrender or cancellation credits after discontinuance of plan.*—If surrender or cancellation credits may be made after discontinuance of the plan but before all retirement annuities with respect to service prior to discontinuance of the plan have been purchased, such credits will be applied regularly as they are determined to purchase such retirement annuities by a procedure which does not contravene the conditions of section 401(a)(4).

(4) *Dividends or experience credits after discontinuance of contributions.*—Any dividends or experience credits similar to dividends made after permanent discontinuance of contributions, or any surrender or cancellation credits made after permanent discontinuance of contributions and after all retirement annuities with respect to service prior to discontinuance of the plan have been purchased, may be paid to the employer provided they are paid as nearly as practicable as they are determined so that no substantial accumulation results. (It may be noted that this possibility of return to the employer after discontinuance is analogous to the provision permitting return to the employer, on termination of an exempt pension trust of any surplus arising from erroneous actuarial computations.)

PART 4.—REQUIREMENTS AS TO COVERAGE

SECTION 401(A)(3)(A) AND (B), (5), AND (6) OF THE INTERNAL REVENUE CODE OF 1954—REGULATIONS SECTION 1.401-3

(a) PLAN MUST BENEFIT EMPLOYEES IN GENERAL.—Section 401(a)(3) of the Code permits an employer to designate several pension, stock bonus, profit-sharing, and annuity plans as constituting parts of a plan which he intends to qualify under such section. If all of the plans so designated cover a sufficient portion of all employees, there is no requirement that a definite proportion of the employees be included in any one plan. The plan, or plans, must benefit employees in general and, towards this end, must cover either a number which is at least equal to that determined under the percentage provisions of section 401(a)(3)(A), or such employees as qualify under a nondiscriminatory classification within the purview of section 401(a)(3)(B). A plan will not necessarily fail of qualification merely because

it covers only the employer's one employee, provided, however, that it is not designed, or operated, as a means of siphoning profits to a shareholder-employee or otherwise limiting participation to an employee of a class in whose favor discrimination is prohibited under section 401(a)(3)(B) and (4). See Rev. Rul. 55–81, C. B. 1955–1, 392.

(b) PERCENTAGE COVERAGE REQUIREMENTS.—The percentage coverage requirements of section 401(a)(3)(A) of the Code may be met by including in the plan a number of employees at least equal to that determined by applying either of the alternative percentage provisions. The percentages are applied after excluding certain short service, seasonal, and part-time employees. For example, if out of a total of 1,200 employees, 100 have less than three years of service (the minimum period prescribed by the plan), 25 do not customarily work for more than 20 hours in any one week, and 75 are employees whose customary employment is for not more than five months in any calendar year, the percentages are applied to the balance of 1,000. The alternative percentage provisions are:

1. Seventy percent or more of all employees (70% of 1,000 in the above example) must be covered under the plan.

2. Seventy percent or more of all employees (70% of 1,000 in the above example) must be eligible to benefit under the plan, and, if so, at least 80 percent of all eligible employees must actually be covered.

Under the first alternative, on the basis of the figures used, if at least 700 employees are covered, the requirements of section 401(a)(3)(A) are satisfied. Under the second alternative, on the same basis, 700 or more employees must be eligible to participate and at least 80 percent of those eligible must actually participate. For example, if employees are also required to contribute five percent of compensation in order to participate, and, say, 750 of them are eligible to do so, then if at least 600 actually do contribute and are covered under the plan, the requirements of section 401(a)(3)(A) are also met.

(c) CLASSIFICATION OF EMPLOYEES.—In lieu of meeting the percentage requirements of section 401(a)(3)(A) of the Code, an employer may set up a classification of employees which, if found by the Commissioner of Internal Revenue not to discriminate in favor of officers, shareholders, supervisors, or highly compensated employees, will satisfy the requirements of section 401(a)(3)(B). Under such section, plans may qualify which are limited to employees who are within a prescribed age group, have been employed for a stated number of years, have been employed in certain designated departments, or are in other classifications, provided that the effect of covering only such employees does not discriminate in favor of employees within the enumerations with respect to which discrimination is prohibited. See section 1.401–3(d) of the regulations.

(d) IMMEDIATE AND DEFERRED PROFIT-SHARING PLANS.—A profit-sharing plan which is qualified under section 401(a) of the Code is a plan of deferred compensation and, as such, provides for distributing the funds accumulated thereunder after a fixed number of years, the attainment of a stated age, or upon the prior occurrence of some event such as illness, disability, retirement, death, layoff, or severance of employment. Thus, employees who receive the amounts allocated

to their accounts before the expiration of such period of time or the occurrence of such contingency are not considered covered under the plan for the purposes of section 401(a)(3)(A) and (B). See section 1.401–3(c) of the regulations. If the employee has a right of election to receive his share of the profits in cash or to have it deferred through payment into a trust for his benefit, qualification of the plan is made by reference only to those employees who participate in the trust. See Rev. Rul. 56–497, C.B. 1956–2, 284.

(e) DIFFERENT ELIGIBILITY REQUIREMENTS FOR PRESENT AND FUTURE EMPLOYEES.—A provision for different eligibility requirements for present and future employees is not necessarily discriminatory within the purview of section 401(a)(3)(B) of the Code. If present employees who are officers, shareholders, supervisors, or highly compensated can meet the requirements for new employees there is no objection to the dual requirements. For example, if all present employees regardless of age are eligible and only those new employees who are at least 30 years old may participate, but all present employees who fall within one or more of the categories enumerated in section 401(a)(3)(B) are at least 30 years of age, the eligibility provision is not objectionable, even though there are other present employees who are under 30 years of age. Similarly, if all present employees are eligible regardless of years of service but only those future employees who will complete five years of service will be eligible, but all present employees who are officers, shareholders, supervisors, or highly compensated have at least five years of service, although there are other present employees who have less than five years, the eligibility provision is acceptable. If however, in the above illustrations, there are employees within the enumerated categories who are under 30 years of age or have less than five years of service, the prohibited discrimination is likely to arise in operation when new employees are added, and, therefore, in such a case such a provision would not be acceptable as a basis for a favorable advance ruling.

(f) CONTINUING PARTICIPATION IN THE EVENT OF LEAVE OF ABSENCE.—Plans may provide for continued participation in the event of leave of absence for a specified purpose, such as service in the Armed Forces, sickness, or disability. All participants under similar circumstances, however, must be treated alike.

(g) BURDENSOME CONTRIBUTIONS.—Section 1.401–3(d) of the regulations provides in part: "* * * if a contributory plan is offered to all of the employees, but the contributions required of the employee participants are so burdensome as to make the plan acceptable only to the highly paid employees, the classification will be considered discriminatory in favor of such highly paid employees." For example, if the plan requires employee contributions of ten percent of compensation, it will be necessary to determine whether lower paid employees are kept out of the plan because of such requirement. If it is found that lower paid employees are not participating because of the contribution requirement, the classification may be held to discriminate in favor of a group enumerated in section 401(a)(3)(B) and (4) of the Code. As a general rule, however, employee contributions of six percent or less are not deemed to be burdensome. In cases where the plan provides for optional rates of contribution by employees, and employer contributions or the benefits are geared

to the employee contributions in such a way that a higher rate of employee contributions will result in larger benefits from employer contributions, the employee contributions may similarly be found to be burdensome and result in discrimination in contributions or benefits in contravention of section 401(a)(4), but generally only if the highest rate of employee contribution permitted is in excess of six percent of compensation. The test is whether the contribution provisions operate to deprive lower paid employees of benefits at least as high in proportion to compensation as are provided for higher paid employees, after taking into account differentials permitted under the requirements for integration with social security benefits. See subparagraph (j) below.

(h) VOLUNTARY CONTRIBUTIONS.—Where employees are permitted to make voluntary contributions to which employer contributions are not geared, a potential disproportionate allocation of employer contributions is not present. Such voluntary contributions, however, must be kept within reasonable bounds. Accordingly, provision may be made for voluntary employee contributions of amounts up to 10 percent of compensation, provided that employer contributions, or the benefits derived therefrom, are not geared to employee contributions which must be used to provide additional benefits only for the individual contributing employees. See Rev. Rul. 59–185, C.B. 1959–1, 86.

(i) CLASSIFICATION WITHIN PURVIEW OF STATUTE BUT DISCRIMINATORY IN OPERATION.—A classification may appear to be satisfactory on paper but if in actual operation of the plan it discriminates in favor of employees who are highly compensated, etc., the plan will fail of qualification. For example, a plan ostensibly covers all employees regardless of service but nonforfeitable rights are provided only for those who have at least 15 years of service and stay on until normal retirement age 65. Except for a handful of executives who are shareholders and officers, employees are migratory workers who stay on a job for a relatively short time and then move elsewhere. Although the coverage provisions on paper seem satisfactory, in actual operation only the executive employees will benefit. Accordingly, both paragraphs (3)(B) and (4) of section 401(a) of the Code are considered together in determining whether the requirements of each is met. It is possible in the illustration used that the plan may qualify if satisfactory provisions for vesting are incorporated therein. See part 5(c) hereof. In the case of a profit-sharing plan under which employees may elect to receive their shares in cash or to participate in a trust, the trust must include enough lower paid employees to demonstrate that in the operation of the plan there is no discrimination in favor of higher paid employees. See Rev. Rul. 56–497.

(j) INTEGRATION.—Plans which exclude employees who earn less than a specified amount or provide proportionately lesser benefits for such employees may qualify if the benefits under the plan integrate with those provided under the social security or similar (e.g., Railroad Retirement Act) program. The total benefits, inclusive of those under the social security or similar program, are used for comparative purposes. If a plan is properly integrated, a classification which excludes all employees who are compensated below the compensation

level used for integration purposes will not be considered discriminatory solely because the contributions or benefits based on that part of excluded remuneration differ from contributions or benefits based on that part of remuneration which is not so excluded.

(1) *Integration rules.*—The rules for integrating benefits under a plan with those provided under the Social Security Act, prior to the 1950 amendments, are set forth in Commissioner's Mimeograph 5539, C.B. 1943, 499. Supporting rulings under that mimeograph are contained in I.T.'s 3613, 3614, and 3615, C.B. 1943, 475, 476 and 477, respectively, and in P.S. Nos. 5, 13, and 30, dated July 29, 1944, August 24, 1944, and September 16, 1944, respectively. Rules as to integration of deferred benefit plans of employers with the old-age and survivors insurance benefits provided by the Social Security Act Amendment of 1950 are contained in Mimeograph 6641, C.B. 1951–1, 41, and the modification effected as a result of amendments to the Social Security Act by Public Law 590, 82d Congress, 2d Session approved July 18, 1952, are set forth in Revenue Ruling 13, C.B. 1953–1, 294. P.S. No. 34, dated September 23, 1944, sets forth the rules applicable to integrating benefits under a plan with those under the Railroad Retirement Act, as in effect as of September 23, 1944, and Revenue Ruling 12, C.B. 1953–1, 290, prescribed the applicable integration rules as effected by amendments to the Railroad Retirement Act through October 1951. Section 1.401–3(e) of the regulations prior to amendment by T.D. 6447, C.B. 1960–1, 163, established the general basis for integrating pension, annuity, profit-sharing, and stock bonus plans which limit coverage to employees earning in excess of $4,200 a year, or which base contributions or benefits only on compensation in excess of that amount, with the benefits provided by the Social Security Act as amended through 1956. Revenue Ruling 56–692, C.B. 1956–2, 287, extends the provisions of Mimeograph 6641, except paragraphs 11 and 15 thereof, to plans which are integrated at $4,200 a year and gives effect to the more liberal definition of "average annual compensation," as provided by section 1.401–3(e)(2)(i) of the regulations, prior to amendment by T.D. 6447. Such Treasury Decision, however, sets forth the general basis for integration of pension, annuity, profit-sharing, and stock bonus plans which limit coverage to employees earning in excess of $4,800 a year, or which base contributions or benefits only on compensation in excess of that amount, with benefits provided by the Social Security Act, as amended through 1958. Revenue Ruling 61–75, C.B. 1961–1, 140, contains guides for determining whether a plan is integrated with benefits under the Social Security Act as so amended, and modifies Mimeograph 6641 and Revenue Ruling 13.

(2) *Death benefits under prior integration rules.*—For the rules applicable to plans providing death benefits and integrated under Mimeograph 5539, see Revenue Ruling 57–163, Part 4(i)(2), C.B. 1957–1, 128, at 143.

(k) LIMITATION ON EXCESS TRUST EARNINGS CREDITS UNDER INTEGRATED PLANS.—A trusteed pension plan which covers only employees earning in excess of a specified amount, or under which benefits are

offset by all or part of the primary social security benefit, will not meet the integration requirements if it contains no limitation on the amount of excess earnings of the trust which may be credited to a participant's account. Where a plan provides that actual trust earnings are to be credited proportionately to the individual accounts of participants, regardless of whether such earnings are greater or less than the assumed rate, the result may be that employees will benefit to an extent in excess of the permissible limit for integration purposes. Hence, such a provision is not acceptable. The plan may meet the integration requirements, however, if it is amended to include limits insuring that the crediting of the excess earnings will not cause the actual benefits to exceed the integration limits. Any excess earnings which, in any year, cannot be credited to a participant's account because of such limitation, is to be used to reduce the employer's contribution for that year. As an alternative, however, the plan may provide that excess earnings will be allocated on a basis which does not involve integration, e.g., allocating excess earnings in proportion to compensation, or total compensation since becoming a participant. See Rev. Rul. 60–337, C.B. 1960–2, 151.

(l) Coverage Limited to Employees Exempt from Overtime Pay Provisions of the Fair Labor Standards Act.—A classification which consists only of such employees who are exempt from the overtime provisions of the Fair Labor Standards Act is not automatically nondiscriminatory. Such a classification may, however, be acceptable in a particular case if it either includes enough employees to satisfy the percentage coverage requirements or if it in fact does not discriminate in favor of employees within the enumerations with respect to which discrimination is prohibited. Section 13(a)(1) of the Fair Labor Standards Act provides that the overtime pay provisions shall not apply to any employee who is employed in a bona fide executive, administrative, professional, or local retailing capacity, or in the capacity of outside salesman, as such terms are defined and delineated by regulations of the Wage and Hour Division of the Department of Labor. These regulations prescribe minimum compensation levels for employees within the prescribed categories. Hence, a plan covering only such employees which has the effect of covering substantially only salaried and clerical employees earning above a certain minimum compensation level must satisfy the integration requirements in order to qualify. See subpart (j) hereof. Furthermore, the classification may be found to be discriminatory if it consists primarily of employees who are officers, shareholders, supervisors, or highly compensated, or if there are relatively many salaried or clerical employees earning in excess of the specified compensation levels who are not exempt from the overtime provisions of the Fair Labor Standards Act and are therefore excluded from the plan. See Rev. Rul. 59–14, C.B. 1959–1, 84.

(m) Coverage Requirements Must Be Met on at Least One Day in Each Quarter.—The coverage requirements of section 401(a)(3) of the Code, either on the percentage basis under subparagraph (A) or on the basis of a nondiscriminatory classification under subparagraph (B), may be satisfied for an entire taxable year if such requirements are met on at least one day in each quarter of the taxable year. For example. assuming that the taxable year coincides with the calen-

dar year, if the percentage basis is applicable and on the first day of the taxable year 1,000 employees have at least the minimum service requirements prescribed by subparagraph (A), it is sufficient if not less than 700 employees are eligible to participate and not less than 80 percent of those eligible are actually participating on that day even though employee turnover changes the percentages to less than 70 and 80 on all other days prior to April 1 of the same year. The percentage requirements will again have to be met on at least one day during the quarter commencing with April 1, and so on for the other quarters during the year.

(n) DENIAL OF PARTICIPATION FOR FAILURE TO ENTER PLAN UPON BECOMING ELIGIBLE.—Plans may provide for denial of participation for failure to enter plan upon becoming eligible provided that participation requires something substantially more than mere consent on the part of the employee. For example, under an employee contributory plan, if an employee refuses to sign a prescribed form for participation authorizing salary deductions in accordance with the plan, the plan may provide for the denial of participation at any other time or for a limited time. Similarly, under an insured plan which requires a physical examination and information as to condition of health, the plan may provide that refusal to take the examination or furnish the information will bar the employee from participation. Adequate notice, however, must be given the employee and the consequences of his failure to comply must be clearly presented to him after which, if he refuses to join, the exclusion provisions of the plan become operative as to such employee. Such provisions must be uniformly applied so as not to result in the prohibited discrimination.

(o) REENTRY INTO PLAN AFTER DISCONTINUANCE OF PARTICIPATION.—Plans may provide for reentry after discontinuance of original participation upon severance of employment or for other reasons, such as failure to continue contributions on the part of the employee. Such provisions, however, must be uniformly applied and in no event should they permit a duplication of benefits.

(p) DELAY IN PURCHASING INSURANCE CONTRACTS.—Generally, a statement in a plan exonerating the trustee from liability in the event of a reasonable delay in the purchase of insurance contracts for participants will not adversely affect the qualification of the plan, provided, however, that the benefits are calculated from the effective date of participation.

(q) EMPLOYEES OF MORE THAN ONE EMPLOYER.—In the case of a pension plan maintained by more than one employer, where employees covered by the plan may receive compensation from more than one of the participating employers, the aggregate compensation may be used in determining the employee's eligibility for benefits in the plan. See Rev. Rul. 55-276, C.B. 1955-1, 401.

PART 5.—DISCRIMINATION IN CONTRIBUTIONS OR BENEFITS

SECTION 401(a)(4) OF THE INTERNAL REVENUE CODE OF 1954—REGULATIONS SECTION 1.401-4

(a) NONDISCRIMINATORY CONTRIBUTIONS OR BENEFITS.—One of the requirements for qualification of a plan is that there must be no discrimination in contributions or benefits in favor of employees who

are officers, shareholders, supervisors, or highly compensated, as against other employees whether within or without the plan. See section 1.401–4(a)(1)(i) of the regulations. Thus, for example, a profit-sharing plan which provides for allocations of employer contributions among participants to the extent of 20 percent of compensation for highly compensated employees, and but 10 percent for all others, is discriminatory within the purview of section 401(a)(4) of the Code. See I.T. 3678, C.B. 1944, 321. Similar considerations apply to pension and annuity plans, but differences in favor of higher paid employees may be acceptable if the plan is satisfactorily integrated. See part 4(j) hereof. Also, as provided in section 1.401–4(a)(1)(ii) of the regulations, any amount allocated to an employee which is withdrawn before the expiration of the time or the occurrence of an event specified in section 1.401–1(b)(1)(ii) of the regulations is not considered in determining whether the contributions under the plan discriminate in favor of employees who are officers, etc. See Rev. Rul. 56–497, C.B. 1956–2, 284.

(b) VARIATIONS IN CONTRIBUTIONS OR BENEFITS.—Variations in contributions or benefits may be provided so long as the plan, viewed as a whole for the benefit of employees in general, with all its attendant circumstances, does not discriminate in favor of employees who are officers, etc. In some cases, benefits under a profit-sharing plan may vary by reason of a distribution formula which takes into consideration years of service. See I.T.'s 3685 and 3686, C.B. 1944, 324 and 326, respectively, and P.S. No. 28, dated September 2, 1944. While the situation described in I.T. 3685 illustrates the result in that case under which the addition of units of compensation and units of service did not result in the prohibited discrimination, and I.T. 3686 illustrates a case in which the multiplication of units of compensation by units of serve resulted in such discrimination, it was not intended to imply by those rulings that any formula using the addition approach is automatically acceptable and that any formula using the multiplication method is basically discriminatory. The result of the operation of the formula is controlling in each case. If the application of any type of formula results in the prohibited discrimination, as measured by the ratio of benefits to compensation, the formula is not acceptable. See also Rev. Rul. 57–77, C.B. 1957–1, 158.

(c) VESTED RIGHTS.—Various provisions for vesting are in use, ranging from complete and immediate vesting through different forms of graduated vesting, upon completion of stated service or participation requirements, and, or, reaching a specified age, to no vesting until attainment of normal or stated retirement age. A determination as to satisfactory vesting provisions will of necessity depend on the facts in a particular case. For example, where a company with a large employee turnover experience establishes a plan covering all employees, but provides no vested rights prior to normal retirement, the discriminatory situation described in part 4(i) hereof may result. Accordingly, an advance favorable determination with respect to the qualification of such plan is not warranted. The situation may be remedied, however, by a provision for fully vested rights after a reasonable waiting period. See P.S. No. 22, dated September 2, 1944.

(1) *Requirement for ultimate vesting.*—A plan will not be held to qualify unless an employee who has reached the normal retire-

ment age (in the case of a pension or annuity plan) or the stated age (or other specified event has transpired in the case of a profit-sharing or stock bonus plan), and has satisfied any reasonable and uniformly applicable requirements as to length of service or participation, is vested in the contributions made or benefits payable under the plan. Provision may, however, be made for discontinuance of benefits to a retired employee for cause, which must be distinctly specified, such as, for example, taking a position with a competitor of the employer, in divulging the employer's trade secrets to competitors. Similarly, provision may be made for the granting of less liberal rights under such circumstances. Whatever provisions are made, however, must not discriminate in favor of employees who are officers, shareholders, supervisors, or highly compensated.

(2) *Vesting on termination of plan.*—Qualified plans are to provide for fully vested rights in all participants, and for distribution of the funds, upon the termination of the plan. Any provision for distribution is acceptable if it specifies the method to be used and: (1) is not in conflict with the restrictions set forth in Mimeograph 5717, C.B. 1944, 321 (see subpart (e) hereof), and (2) cannot otherwise discriminate in favor of employees who are officers, etc. See section 1.401–4(c) of the regulations. The distribution of unallocated funds may be in cash or in the form of other benefits provided under the plan. The distribution among employees, other than those whose benefits have been restricted in accordance with the provisions of Mimeograph 5717 need not necessarily benefit all such other employees. For example, a distribution may be satisfactory if priority is given to benefits for employees over the age of 50 at the time of termination of the plan, or those who then have at least 10 years of service, or those who meet both such age and service requirements, provided, however, that there is no possibility of discrimination in favor of employees who are highly compensated, etc. Here, too, if there is no possibility that the prohibited discrimination will result, upon termination of the plan the funds may be used, for example, first to continue benefits to retired employees, then for employees who have met the requirements for retirement but have not yet retired, then for employees over age 60, and so on until the funds are fully exhausted.

(3) *Vesting upon suspension of contributions under a profit-sharing plan.*—If, under the terms of a profit-sharing plan, authority is specifically reserved to discontinue contributions without terminating the trust, the plan must also contain an appropriate provision granting fully vested rights to participants upon discontinuance of contributions by the employer. The situation is similar to a case in which actual termination of the trust occurs. See Rev. Rul. 56–596, C.B. 1956–2, 288.

(d) Application of Forfeitures.—Funds under a qualified plan, arising from forfeitures or other reason, must not be allocated to the remaining participants in such a manner as to effect the prohibited discrimination. This requirement is met in the case of a pension plan by complying with the rule enunciated in section 1.401–1(b)(1)(i) of the regulations, regarding definitely determinable benefits,

that: "Benefits are not definitely determinable if funds arising from forfeitures on termination of service, or other reason, may be used to provide increased benefits for the remaining participants instead of being used to reduce the amount of contributions by the employer." This provision is equally applicable to pension plans of the money-purchase type. See Rev. Rul. 109, C. B. 1953–1, 288, and Rev. Rul. 60–73, C.B. 1960–1, 155. Similarly, in a stock bonus or profit-sharing plan, provision may be made that forfeitures be used to reduce the employer contributions which would otherwise be required under the contribution formula, but such application of forfeitures is not mandatory in plans of these types. It should be observed, however, that whatever provision is made for absorbing forfeitures, discrimination in favor of employees who are officers, etc., must not result.

(e) TERMINATION RULE.—If benefits for employees who are officers, etc., are funded, or substantially so, because of their nearness to retirement, and benefits for other employees are not similarly funded prior to termination of the plan, the prohibited discrimination will result. Consequently, under the applicable circumstances, an advance favorable determination letter as to the qualification of a pension or annuity plan will not be issued unless the plan contains satisfactory provisions limiting the benefits for officers, etc., in the event of early termination of the plan. The rules for this purpose are set forth in Mimeograph 5717, C.B. 1944, 321, modified by Revenue Ruling 61–10, C.B. 1961–1, 143. Explanatory releases consist of P.S. Nos. 8, 25, 29, 31, 38, 42, 50, and 52 as modified by Revenue Ruling 55–60, C.B. 1955–1, 37. Similar rules are not applicable to stock bonus and profit-sharing plans since acceptable allocation formulae under such plans are designed to preclude the prohibited discrimination under comparable circumstances. The requirements pertaining to permanency, however, are applicable to all types of plans. See part 2(p) hereof.

(f) DISCONTINUANCE OR SUSPENSION OF CONTRIBUTIONS AND CURTAILMENTS.—A discontinuance of contributions is in effect a termination of the plan except that the formal steps to accomplish such result are not taken. Employees who become eligible to enter the plan subsequent to the discontinuance receive no benefits and no additional benefits, attributable to employer contributions, accrue to any of the participants unless contributions are resumed. The same requisites which apply to a termination of a plan are, therefore, equally applicable to a discontinuance. In such case, vesting of employees' rights is required. See paragraph (c)(2) of this part and Rev. Rul. 55–186, C.B. 1955–1, 39, as modified by Rev. Rul. 56–596, C.B. 1956–2, 288.

(1) *Suspensions.*—A suspension is a temporary cessation of contributions which may ripen into a discontinuance. In the case of a pension or annuity plan, however, a suspension of contributions will not necessarily require vesting of employees' rights merely because of the existence of such situation, and the applicability of a prior ruling as to the qualification of the plan under section 401(a) of the Code will not be affected thereby if the following conditions are met, namely: (1) The benefits to be paid or made available under the plan are not affected at any time by the suspension, and (2) the unfunded past service cost

at any time (which includes any unfunded prior normal cost and unfunded interest on any unfunded cost) does not exceed the unfunded past service cost as of the date of establishment of the plan (plus any additional past service or supplemental costs added by amendment). See P.S. 57, as amended by Rev. Rul. 56–596. In the case of a profit-sharing plan, contributions must be recurring and substantial. See section 1.401–1(b)(2) of the regulations. A determination as to whether a suspension of contributions under a profit-sharing plan constitutes a discontinuance will be made upon consideration of the facts and circumstances of the particular case. For factors in determining whether a suspension of contributions under a profit-sharing plan constitutes a discontinuance, see Rev. Rul. 60–2, C.B. 1960–1, 164. Provision may, however, be made that benefits be suspended for any period of time during which primary insurance benefits under the Federal Social Security Act are discontinued because of employment after retirement date. See part 2(n) hereof and Rev. Rul. 82, C.B. 1953–1, 288.

(2) *Curtailments.*—Where a plan which requires employee contributions is amended so as to make it noncontributory, and provision is also made for a refund of employee contributions, the plan is curtailed but its status for qualification is thereby not adversely affected if the prohibited discrimination does not result. See Rev. Rul. 61–79, C.B. 1961–1, 138, amplifying Rev. Rul. 55–14, C.B. 1955–1, 302.

(g) TOPHEAVINESS.—Paragraph (5) of section 401(a) of the Code provides, in part, that a plan shall not be considered discriminatory within the meaning of paragraphs (3)(B) or (4) of such section merely because the contributions or benefits of or on behalf of the employees under the plan bear a uniform relationship to the total compensation, or the basic or regular rate of compensation, of such employees. However, in the case of pension and annuity plans which are based on a salary classification, i.e., exclusion of employees earning less than a specified amount, such as $4,800 per annum, the benefits under the plan must integrate with those provided under the Social Security Act or similar public retirement plan. See part 4(j) hereof. If under the benefit formula of a pension or annuity plan benefits are provided which bear a uniform relationship to compensation, or which do not discriminate in favor of the group with respect to which discrimination is prohibited when social security or similar Federal or State retirement benefits are taken into account, the benefits and contributions are not discriminatory provided the plan contains adequate safeguards against discrimination in the event of termination of the plan or failure to meet the current costs during the first ten years. See paragraph (e) hereof. A pension or annuity plan which is not in conformance with the aforesaid does not comply with the requirements of paragraph (4) of section 401(a) of the Code, with respect to nondiscrimination as to contributions or benefits. A ceiling or similar limitation on the amount of benefits is not required, however, in view of the provisions of section 401(a)(5) of the Code, but a plan under which benefits are limited may be satisfactory whereas otherwise certain essential requirements may not be fully met.

(h) NORMAL RETIREMENT AGE.—The normal retirement age in a pension or annuity plan is the lowest age specified in the plan at which the employee has the right to retire without the consent of the employer and receive retirement benefits based on service to date of retirement at the full rate set forth in the plan (*i.e.* without actuarial or similar reduction because of retirement before some later specified age). Ordinarily, the normal retirement age under pension and annuity plans is 65, the same as under the old-age, survivors, and disability insurance provisions of the Social Security Act. A different age may be specified, provided that if it is lower than 65 it represents the age at which employees customarily retire in the particular company or industry and is not a device to accelerate funding. In profit-sharing or stock bonus plans, where there is a stated retirement age it is merely one of several events which may be designated as fixing the time for making distributions. Since the amount of the distributions is dependent upon profits, there is no definitely stated rate of benefits payable at such age. Consequently, the stated retirement age in a profit-sharing or stock bonus plan does not have the same significance as "normal retirement age" in a pension plan.

(i) OPTIONAL RETIREMENT PRIOR TO NORMAL RETIREMENT AGE.—Any reasonable optional early retirement age will generally be acceptable provided, however, that if the employer's consent is required, the value of the early retirement benefit does not exceed the value of the employee's vested benefits at that time. This requirement was first announced in Revenue Ruling 57–163, part 5(f), C.B. 1957–1, 128, at 149 originally published in I.R.B. 1957–16, 10, on April 22, 1957. Prior to that date, determination letters had been issued on the qualification of plans which provided for early retirement with the employer's consent if it appeared that the prohibited discrimination would not result because of such provision. Accordingly, such determination letters continue in effect unless and until revoked. See Rev. Rul. 58–151, C.B. 1958–1, 192, as amplified by Rev. Rul. 58–604, C.B. 1958–2, 147. As for provisions in disability and hardship cases, see paragraph (o) hereof. If the optional early retirement age is earlier than 65 (60 for women), and if integration with old-age, survivors', and disability insurance, or with the benefits under the Railroad Retirement Act, is involved (see part 4(j) hereof), the benefits which depend on integration must be appropriately limited. See paragraph 9 of Mim. 6641, C.B. 1951–1, 41, as modified by Rev. Rul. 61–75, C.B. 1961–1, 140, or paragraph 7 of Rev. Rul. 12, C.B. 1953–1, 290, at 292, whichever is applicable.

(j) PARTICIPATION AFTER NORMAL RETIREMENT AGE.—The normal retirement age is the time from which definitely determinable benefits under a pension plan become fixed and payable. Accordingly, an employee who has reached such age and has fulfilled the service requirement and other uniformly applicable provisions of the plan must be permitted to retire and to commence receiving the benefits payable thereunder. Arrangements, however, may be mutually made for continued employment beyond normal retirement age. In such event, provision may be made with respect to the treatment of the pension benefits such as, for example, payment as though the employee had actually retired, deferment to actual retirement without increment for the interval between normal retirement date and actual retirement,

or actuarial equivalent on actual retirement of the benefit at normal retirement age. Whatever provisions are made, however, must be uniformly applied to all participants.

(1) *Additional benefits for service after normal retirement age.*—Provision may be made for additional benefits on account of service after normal retirement age provided such provision is uniformly applicable to all employees under similar circumstances and does not result in the prohibited discrimination. In a unit-benefit plan, the units may be continued during the time of the extended service and the total computed to the time of actual retirement. Under a money-purchase plan, the regular rate of contributions may continue to actual retirement. Under a fixed-benefit plan the benefits payable at actual retirement may be the actuarial equivalent of those payable at normal retirement age.

(2) *Continued participation under a profit-sharing or stock bonus plan.*—A provision for continued participation under a profit-sharing or stock bonus plan and for contributions to provide additional benefits for employees who remain in employment beyond the stated age does not adversely affect the qualification of the plan, provided, however, that such provision is uniformly applied to all employees under similar circumstances and does not result in the prohibited discrimination.

(k) BASIS OF COMPENSATION ON WHICH BENEFITS ARE COMPUTED.—Section 401(a)(5) of the Code provides in part: "Neither shall a plan be considered discriminatory * * * merely because the contributions or benefits of or on behalf of the employees under the plan bear a uniform relationship *to the total compensation, or the basic or regular rate of compensation*, of such employees * * *." [Italics supplied.] Thus, total compensation (which may include bonuses, commissions, or overtime pay), basic compensation, or regular rate of compensation may be used, provided that whatever is used is consistently and uniformly applicable to all participants.

(l) FINAL PAY PLANS.—Section 1.401–1(b)(3) of the regulations provides in part: "* * * a plan is not for the exclusive benefit of employees in general if, by any device whatever, it discriminates either in eligibility requirements, contributions, or benefits in favor of employees who are officers, shareholders, persons whose principal duties consist in supervising the work of other employees, or the highly compensated employees. See section 401(a)(3), (4), and (5)." Thus, benefits computed at a uniform rate of compensation for all participants may be nondiscriminatory but if compensation is adjusted to favor one or a select few the plan may become discriminatory in operation. See section 401(a)(5) of the Code. For example, under a 50 percent fixed benefit plan, a $10,000-a-year officer who fulfills all requirements for retirement would be entitled to an annuity of $5,000, but if shortly before retirement his compensation is increased to $20,000 per annum his retirement annuity, computed on final salary, would be $10,000, or 100 percent of compensation before the increase, whereas others would only be receiving 50 percent. Section 1.401–1(b)(3) of the regulations also points out: "The law is concerned not only with the form of a plan but also with its effects in operation. For example, section 401(a)(5) specifies certain provi-

sions which of themselves are not discriminatory. However, this does not mean that a plan containing these provisions may not be discriminatory in actual operation." Accordingly, in any case where increases in compensation during the last five years of employment are taken into account for the purpose of computing benefits, provision is generally made that such benefits are to be based on compensation averaged over a period of at least five years. In a pension plan which provides both past and future service credits the past service credits may be computed on the average compensation for the five-year period immediately preceding the establishment of the plan.

(m) ADJUSTMENT OF BENEFITS DUE TO INCREASES OR DECREASES IN COMPENSATION.—Consistent and uniform bases of compensation for determining benefits under a plan are essential in order to preclude the prohibited discrimination. If benefits are based on compensation at the time the plan is established, and if certain highly compensated employees are within a few years of retirement, their benefits will be based on the highest, or nearly the highest, compensation, while lower paid employees who entered the service of the employer shortly before the plan was established will receive benefits based on the lowest, or nearly the lowest, compensation. To eliminate discrimination, a consistent and uniform application should prevail as between both groups, *e.g.*, where compensation within a few years before retirement, which includes salary increments since original employment, is used for the highly compensated employees, similar compensation should be used for the lower paid employees. Therefore, provision is to be made for increases in benefits when compensation on which benefits are computed is increased. See Mim. 5677, C.B. 1944, 320. Plans may also provide for decreases in benefits because of decreases in compensation but since the aforesaid result is not present such provision is not required.

(n) DISCRETION AS TO PAYMENT OF BENEFITS UNDER BASIC OPTIONS.—Plans may include various modes of settlement for payment of benefits if under each mode the distribution has the same value as a distribution determined under any other mode of settlement provided for under the plan, and further, if, upon retirement (or event calling for a distribution in a profit-sharing plan) each participant is entitled to a fully vested right in the amount which has been accumulated for his benefit. In an insured plan, any type of benefit which is provided under the options contained in the insurance contract is the actuarial equivalent of any other option. Consequently, discretion in the trustee to determine under which option benefits will be paid does not result in the prohibited discrimination. Similar discretion may be provided for in a profit-sharing plan which, for example, permits the trustee to determine whether lump-sum or periodic distributions are to be made in particular cases. The amounts distributable must be fully vested in the employees in either situation, and, if periodic distributions are to be made to some as against lump-sum payments to others, the present value of all such periodic amounts payable to any employee is to be equal to the immediate lump-sum otherwise distributable to him.

(o) PROVISIONS FOR DISABILITY AND HARDSHIP CASES.—Pension plans may contain provisions for early retirement because of disability

provided that the term "disability" is defined and the rules with respect thereto are uniformly and consistently applied to all employees in similar circumstances. Provisions may also be made in stock bonus and profit-sharing plans for accelerated distributions because of hardship provided that the term "hardship" is defined, the rules with respect thereto are uniformly and consistently applied, and the distributable portion does not exceed the employee's vested interest. Similar provisions, however, are not permissible under a pension plan, since, as provided for in section 1.401–1(b)(1)(i) of the regulations, such a plan is established and maintained "primarily to provide systematically for the payment of definitely determinable benefits to * * * employees over a period of years, usually for life, after retirement." See Rev. Rul. 56–693, C.B. 1956–2, 282, as modified by Rev. Rul. 60–323, C.B. 1960–2, 148.

(p) PROVISION THAT BENEFITS BE BASED ON CASH SURRENDER VALUE IN INSURED PLANS.—If an insured plan provides that benefits shall be based on cash surrender values, all contracts purchased must provide uniform cash surrender values with respect to all employees under similar circumstances.

(q) LOAN PRIVILEGES.—Provision may be made for the granting of loans to participants up to the extent of their vested interests subject to the application of specified uniform rules consistently followed. It should be noted, however, that so-called "loans" may constitute "distributions" if there is tacit understanding between the parties that collection is not intended.

(r) PAST SERVICE BENEFITS IN PLANS WHICH CONTAIN A MINIMUM AGE OR SERVICE REQUIREMENT FOR ELIGIBILITY.—A plan which contains a minimum age or service requirement for eligibility and provides for past service credits for all prior service of original, but not subsequent, participants will generally be considered objectionable within the purview of section 401(a)(3)(B) and (4) of the Code unless it can be demonstrated that such credits do not result in the prohibited discrimination. Where the difference is only one year, however, e.g., if there is a one-year waiting period for eligibility, but original participants are given credit for all prior service, including the one-year waiting period, and new participants do not receive credit based on the one year, such a provision may be acceptable. Provision may also be made for credits on account of past services rendered after attainment of a specified age or completion of minimum service, if applied to original as well as subsequent participants.

(s) RIGHT OF TRUSTEE TO BORROW ON INSURANCE CONTRACTS.—Provision may be made granting the trustee the right to borrow against the loan values of insurance contracts, provided, however, that in doing so the remaining interest of employees who are officers, etc., is proportionately no greater than the interest of other employees.

(t) EARMARKED INVESTMENTS.—Where amounts to be distributed to participants under a profit-sharing trust are measured by investments which have been earmarked for their respective accounts, the trustee is to invest each participant's interest proportionately, unless all participants have the right to direct the trustee to select the type of investment with respect to their individual shares.

APPENDIX

RULINGS INCORPORATED BY REFERENCE

COMMISSIONER'S MIMEOGRAPHS

Number	*Subsequent Action, if Any*	*Cumulative Bulletin Reference*
5539		1943, 499
5677		1944, 320
5717	(Modified by Revenue Ruling 61–10, C.B. 1961–1, 143)	1944, 321
5985	(Modified by Revenue Ruling 57–419, C.B. 1957–2, 264)	1946–1, 72
6020	(Modified by Revenue Ruling 59–402, C.B. 1959–2, 122)	1946–1, 74
6136	(Modified by Revenue Ruling 55–60, C.B. 1955–1, 37)	1947–1, 58
6394		1949–1, 118
6641	(Amended by Revenue Ruling 13, C.B. 1953–1, 294, and provisions extended to cover integration at $4,200 by Revenue Ruling 56–692, C.B. 1956–2, 287, and at $4,800 by Revenue Ruling 61–75, C.B. 1961–1, 140)	1951–1, 41

I.T. RULINGS

3350		1940–1, 64
3613		1943, 475
3614		1943, 476
3615		1943, 477
3660		1944, 136
3678		1944, 321
3685		1944, 324
3686		1944, 326
4020		1950–2, 61

REVENUE RULINGS

12		1953–1, 290
13	(Amending Mimeograph 6641, C.B. 1951–1, 41; amended by Revenue Ruling 61–75, C.B. 1961–1, 140)	1953–1, 294
33	(Modified by Revenue Ruling 57–163, C.B. 1957–1, 128, and the instant ruling)	1953–1, 267
82		1953–1, 288
109	(Referred to in Revenue Ruling 60–73, C.B. 1960–1, 155)	1953–1, 288
185	(Referred to in Revenue Ruling 60–337, C.B. 1960–2, 151)	1953–2, 202
54–51	(Amplified by Revenue Ruling 57–213, C.B. 1957–1, 157, and by Revenue Ruling 60–84, C.B. 1960–1, 159)	1954–1, 147
54–67		1954–1, 149
54–152		1954–1, 149
54–172		1954–1, 394
54–231		1954–1, 150
54–398	(Revokes P.S. 19, August 29, 1944)	1954–2, 239
55–14	(Amplified by Revenue Ruling 61–79, C.B. 1961–1, 138)	1955–1, 302
55–60	(Modifies Mimeograph 6136, C.B. 1947–1, 58, and P.S. 52)	1955–1, 37
55–81		1955–1, 392
55–186	(Modified by Revenue Ruling 56–596, C.B. 1956–2, 288)	1955–1, 39
55–276		1955–1, 401
55–629		1955–2, 588
55–681	(Supplementing P.S. 64, November 9, 1950)	1955–2, 585
55–748		1955–2, 234
56–23	(Modified by Revenue Ruling 57–546, C.B. 1957–2, 886)	1956–1, 598
56–267		1956–1, 206
56–432		1956–2, 284
56–497		1956–2, 284

Number	Subsequent Action, if Any	Cumulative Bulletin Reference
56–596	(Modifying P.S. 57, August 5, 1946, and Revenue Ruling 55–186, C.B. 1955–1, 39)	1956–2, 288
56–633		1956–2, 279
56–656		1956–2, 280
56–673		1956–2, 281
56–692	(Extending provisions of Mimeograph 6641, C.B. 1951–1, 41, as amended by Revenue Ruling 13, C.B. 1953–1, 294, to cover integration at $4,200)	1956–2, 287
56–693	(Modified by Revenue Ruling 60–323, C.B. 1960–2, 148)	1956–2, 282
57–77		1957–1, 158
57–163	(Modified by instant ruling)	1957–1, 128
57–213	(Amplifying Revenue Ruling 54–51, C.B. 1954–1, 147)	1957–1, 157
57–419	(Modifying Mimeograph 5985, C.B. 1946–1, 72, and revoking P.S. 55, January 9, 1946)	1957–2, 264
57–546	(Modifying Revenue Ruling 56–23, C.B. 1956–1, 598)	1957–1, 886
58–151	(Amplified by Revenue Ruling 58–604, C.B. 1958–2, 147)	1958–1, 192
58–604	(Amplifying Revenue Ruling 58–151, C.B. 1958–1, 192)	1958–2, 147
59–14		1959–1, 84
59–185		1959–1, 86
59–402	(Modifying Mimeograph 6020, C.B. 1946–1, 74)	1959–2, 122
60–2		1960–1, 164
60–33		1960–1, 152
60–73	(Makes reference to Revenue Ruling 109, C.B. 1953–1, 288)	1960–1, 155
60–83		1960–1, 157
60–84	(Amplifying Revenue Ruling 54–51, C.B. 1954–1, 147; see also Revenue Ruling 57–213, C.B. 1957–1, 157)	1960–1, 159
60–276	(Superseding Revenue Ruling 59–309, C.B. 1959–2, 117)	1960–2, 150
60–281		1960–2, 146
60–323	(Modifying Revenue Ruling 56–693, C.B. 1956–2, 282)	1960–2, 148
60–337	(Makes reference to Revenue Ruling 185, C.B. 1953–2, 202)	1960–2, 151
61–10	(Modifying Mimeograph 5717, C.B. 1944, 321)	C.B. 1961–1, 143
61–75	(Modifying Mimeograph 6641, C.B. 1951–1, 41, as amended by Revenue Ruling 13, C.B. 1953–1, 294)	C.B. 1961–1, 140
61–79	(Amplifying Revenue Ruling 55–14, C.B. 1955–1, 302)	C.B. 1961–1, 138

REVENUE PROCEDURES

56–12		1956–1, 1029
56–22		1956–2, 1380

STATUS OF P.S. RELEASES

The following list is designed to give current information as to the status of P.S. Releases issued under the Internal Revenue Code of 1939, which, to the extent consistent with the Internal Revenue Code of 1954 and the regulations thereunder, remain effective, except as indicated:

P.S. NO.	DATE	STATUS
1	May 9, 1944	Administrative—inapplicable as a result of action taken on P.S. 2 by Revenue Ruling 2, C.B. 1953–1, 484, 488.
2	July 29, 1944	Administrative—revoked by Revenue Ruling 2, C.B. 1953–1, 484, 488.
3	July 29, 1944	Outstanding.
4	July 29, 1944	Outstanding.

P.S. NO.	DATE	STATUS
5	July 29, 1944	Applicable under Mimeographed 5539, C.B. 1943, 499.
6	July 29, 1944	Revoked by Revenue Ruling 55–748, C.B. 1955–2, 234.
7	July 29, 1944	Outstanding; see, however, Mimeograph 6136, C.B. 1947–1, 58, as modified by Revenue Ruling 55–60, C.B. 1955–1, 37.
8	August 4, 1944	Outstanding; see, however, P.S. 38, October 7, 1944, for more detailed provisions.
9	August 4, 1944	Outstanding, except for provision as to wartime restriction which is no longer applicable.
10	August 10, 1944	Obsolete as a result of issuance of I.T. 4020, C.B. 1950–2, 61.
11	August 10, 1944	Outstanding; see, however, Part 5(t) of instant ruling.
12	August 10, 1944	Obsolete as a result of decision in *Saalfield Publishing Co., Inc.*, 11 T.C. 756; Acquiescence, C.B. 1952–2, 3.
13	August 24, 1944	Outstanding under prior law; as to current position, see Regulations, section 1.401–3(e), as amended by T.D. 6447, C.B. 1960–1, 163.
14	August 24, 1944	Outstanding; see also Regulations, section 1.401–1(d).
15	August 24, 1944	Modified; see Part 2(e)(4) of instant ruling.
16	August 24, 1944	Obsolete as a result of new definition of "profit-sharing plan"; Regulations, section 1.401–1(b)(1)(ii).
17	August 24, 1944	Modified by Revenue Ruling 55–758, C.B. 1955–2, 587; see also Regulations, section 1.401–1(e).
18	August 24, 1944	Outstanding.
19	August 29, 1944	Revoked by Revenue Ruling 54–398, C.B. 1954–2, 239.
20	August 29, 1944	Obsolete as a result of issuance of I.T. 4020, C.B. 1950–2, 61.
21	August 29, 1944	Obsolete as a result of new definition of "profit-sharing plan"; Regulations, section 1.401–1(b)(1)(ii).
22	September 2, 1944	Outstanding, but see instant ruling, Part 5(c).
23	September 2, 1944	Outstanding, but see instant ruling, Part 2(e)(1).
24	September 2, 1944	Outstanding, except as to provision for definite formula; see Regulations, section 1.401–1(b)(1)(ii).
25	September 2, 1944	Outstanding.
26	September 2, 1944	Outstanding; subject, however, to minimum funding prescribed in P.S. No. 57, as modified by Revenue Ruling 56–596, C.B. 1956–2, 288.
27	September 2, 1944	Outstanding.
28	September 2, 1944	Outstanding; see also I.T.'s 3685 and 3686, C.B. 1944, 324 and 326, respectively, and Revenue Ruling 57–77, C.B. 1957–1, 158.
29	September 16, 1944	Outstanding.
30	September 16, 1944	Outstanding; see also I.T. 3615, C.B. 1943, 477, and current integration rules; Regulations, section 1.401–3(e), as amended by T.D. 6447, C.B. 1960–1, 163.
31	September 16, 1944	Outstanding.
32	September 20, 1944	Outstanding.

P.S. NO.	DATE	STATUS
33	September 20, 1944	Obsolete as a result of new definition of "profit-sharing plan"; Regulations, section 1.401–1(b)(1)(ii).
34	September 23, 1944	Outstanding under prior law; see, however, Revenue Ruling 12, C.B. 1953–1, 290.
35	October 2, 1944	Revised November 16, 1944.
35 Revised	November 16, 1944	Modified by Revenue Ruling 54–172, C.B. 1954–1, 394.
36	October 2, 1944	Outstanding.
37	October 7, 1944	Outstanding; see also Regulations, section 1.401–1(b)(3).
38	October 7, 1944	Outstanding; see also P.S. 8, August 4, 1944.
39	October 16, 1944	Obsolete as a result of issuance of I.T. 4020, C.B. 1950–2, 61.
40	October 19, 1944	Obsolete as a result of new definition of "profit-sharing plan"; Regulations, section 1.401–1(b)(1)(ii).
41	November 9, 1944	Obsolete as a result of issuance of I.T. 4020, C.B. 1950–2, 61.
42	November 11, 1944	Outstanding.
43	November 18, 1944	Outstanding, except for second paragraph which has been rendered obsolete as a result of position set forth in Regulations, section 1.403(a)–1(a).
44	December 11, 1944	Outstanding, except for Salary Stabilization provisions which are no longer applicable.
45	January 26, 1945	Outstanding.
46	February 10, 1945	Obsolete as a result of new definition of "profit-sharing plan"; Regulations, section 1.401–1(b)(1)(ii).
47	February 20, 1945	Applicable to rulings issued prior to March 2, 1945; current position set forth in Revenue Ruling 60–276, C.B. 1960–2, 150.
48	March 8, 1945	Applicable under the Internal Revenue Code of 1939; see, however, Regulations, section 1.6033–1(a)(3) as to provisions under the Internal Revenue Code of 1954.
49	June 16, 1945	Modified by instant ruling, Part 2(r); see also Revenue Procedure 56–12, Exhibit "B," C.B. 1956–1, 1029, 1035.
50	July 12, 1945	Outstanding.
51—Part A	July 31, 1945	Outstanding.
51—Part B	July 31, 1945	Outstanding under prior law; see, however, Internal Revenue Code of 1954, section 401(a)(1) and 404(a)(3)(B).
52	August 9, 1945	Modified by Revenue Ruling 55–60, C.B. 1955–1, 37.
53	October 4, 1945	Outstanding under prior law.
54	January 5, 1946	Applicable to calendar year 1942 or to a fiscal year which commenced in 1942.
55	January 9, 1946	Revoked by Revenue Ruling 57–419, C.B. 1957–2, 264.
56	June 27, 1946	Outstanding.
57	August 5, 1946	Outstanding, except penultimate paragraph modified by Revenue Ruling 56–596, C.B. 1956–2, 288.
58	January 30, 1947	Revised March 7, 1947.
58 Revised	March 7, 1947	Reissued as Revenue Ruling 55–747, C.B. 1955–2, 228.
59	February 25, 1947	Outstanding; also published as I.T. 3847, C.B. 1947–1, 65; see Regulations, section 1.402(a)–1(a)(6)(ii).
60	June 19, 1947	Procedure on terminations under prior law; see Revenue Procedure 56–12, Exhibit "A," C.B. 1956–1, 1029, 1034, for present requirements.

P.S. NO.	DATE	STATUS
61	August 12, 1947	Applicable under prior law; see also G.C.M. 25358, C.B. 1947–2, 9; inapplicable under the Internal Revenue Code of 1954, as to which see section 403(a)(2).
62	May 5, 1950	Outstanding under prior law; see, however, Internal Revenue Code of 1954, section 381(c)(11) and (20).
63	June 6, 1950	Outstanding; see also Regulations, section 1.402(a)–1(a)(5).
64	November 9, 1950	Outstanding; reissued as, and supplemented by, Revenue Ruling 55–681, C.B. 1955–2, 585.
65	November 10, 1950	Applicable under prior law, but last paragraph now obsolete as a result of position set forth in Regulations at section 1.403(a)–1(d).
66	November 10, 1950	Inapplicable to distributions of insurance contracts after October 26, 1956, as to which see Regulations, section 1.402(a)–1(a)(2), and Revenue Ruling 57–191, C.B. 1957–1, 162.
67	August 26, 1951	Outstanding.
68	July 3, 1951	Applicable with respect to compliance with the wage-stabilization requirements under the Defense Production Act of 1950; current position set forth in Revenue Ruling 60–276, C.B. 1960–2, 150.

Rev. Rul. 61–164

The purchase by a trust established under an employees' profit-sharing plan of incidental amounts of life, accident or health insurance for the benefit of an employee or his family, with funds allocated to his account that have not been accumulated for the period prescribed by the plan for the deferment of distributions, will not prevent qualification of the plan under section 401(a) of the Internal Revenue Code of 1954.

Advice has been requested as to the effect upon the qualification of an employees' profit-sharing plan under section 401(a) of the Internal Revenue Code of 1954 of a provision in the plan for the purchase of major medical hospitalization insurance for the employees.

An employer established an employees' profit-sharing plan and, in addition, provided the employees with group hospitalization insurance. This insurance coverage was extended to include major medical benefits. Its cost was paid by the trust established under the plan with funds that had not been accumulated for the period prescribed by the plan for the deferment of distributions. Each participant's account under the plan was charged with the cost of the additional benefits obtained for him. The plan does not prohibit the use in this manner of funds allocated to the participating employees' accounts.

A profit-sharing plan within the meaning of section 401 is primarily a plan of deferred compensation, but the amount allocated to the account of a participant may be used to provide for him or his family incidental life or accident or health insurance. Section 1.401–1(b)(1)(ii) of the Income Tax Regulations.

The use of trust funds to pay the cost of major medical insurance for an employee or his beneficiaries is a "distribution" within the

meaning of section 402 of the Code. If such insurance may be purchased only with funds that have been accumulated for the period required by the plan for the deferment of distributions, there is no limit to the amount of such insurance that may be purchased. If, however, the plan permits the use of funds that have not been so accumulated to purchase such insurance, the amount of the premiums must be no more than "incidental". Section 1.401–1(b)(1)(ii) of the regulations.

There is no provision in the instant profit-sharing plan that requires the accumulation of funds for the period prescribed by the plan for the deferment of distributions before they can be used to purchase the major medical insurance. Accordingly, the trust established under the profit-sharing plan will not qualify under section 401(a) if the cost of such insurance is more than "incidental" in relation to the amounts credited to the respective employee's account that have not been so accumulated.

Distributions, in the form of one or more permissible benefits such as life, accident or health insurance (to the extent that each such benefit constitutes a "distribution"), will be treated as "incidental" if in the aggregate they do not exceed 25 percent of the funds allocated to a participant's account that have not been so accumulated. This treatment is consistent with the acquiescence in *Raymond J. Moore*, 45 B.T.A. 1073, C.B. 1943, 17, and with Revenue Ruling 54–51, C.B. 1954–1, 147. In the *Moore* case, the cost of the pure insurance element in the retirement income contract (which alone constituted a "distribution" to the employee) purchased by the trust varied from approximately 17 percent for an employee age 25 at date of issue to 6 percent for an employee age 55 at the date of issue. Revenue Ruling 54–51 treated as "incidental" the purchase by a qualified profit-sharing trust of ordinary life insurance where (1) the aggregate premiums in the case of each participant was less than one-half of the aggregate contributions allocated to his account at any particular time; and (2) the plan required the trustee to convert the entire value of the life insurance contract at or before retirement to provide periodic income so that no portion of such value might be used to continue life insurance protection beyond retirement. The cost of the pure insurance protection in such contract (which alone constituted a "distribution" to the employee) was approximately one half of its total cost.

Accordingly, that part of the cost of the permissible benefit which was a "distribution" could not exceed 25 percent of the funds allocated to an employee's account that had not been accumulated for the period prescribed by the plan for the deferment of distributions. This percentage exceeds that permitted in the *Moore* case and represents the maximum that will be treated as "incidental."

The foregoing interpretation of "incidental" will be applied with respect to qualified plans providing one or more life or accident or health insurance benefits for participants with funds that have not been accumulated for the period prescribed by the plan for the deferment of distributions, as follows:

(1) If only ordinary life insurance contracts are purchased, the amount expended for premiums may not exceed that percentage permitted in Revenue Ruling 54–51.

(2) If only accident and/or health insurance contracts (including hospitalization, major medical, or similar types of insurance) are purchased, the amount expended for premiums may not exceed 25 percent of the funds allocated to an employee's account that have not been accumulated for the period prescribed by the plan for the deferment of distributions.

(3) If both ordinary life and accident and/or health insurance contracts are purchased, the amount expended for the accident and/or health insurance premiums plus one-half of the amount expended for the ordinary life insurance premiums may not, in the aggregate, exceed 25 percent of the funds allocated to an employee's account that have not been accumulated for the period prescribed by the plan for the deferment of distributions. At no time during the life of the plan may this percentage be exceeded.

The following example will illustrate the interpretation of the term "incidental." The account of an employee who participates in a profit-sharing trust has been allocated $1,000, no part of which has been accumulated for the period prescribed by the plan for the deferment of distributions:

(1) If only ordinary life insurance contracts are purchased by the trust for the employee, not more than $500 may be used to pay the premiums for such contract.

(2) If only accident and/or health insurance contracts are purchased, not more than $250 may be used to pay the premiums for such contracts.

(3) If both ordinary life insurance contracts and accident and/or health insurance contracts are purchased and $300 has been expended to pay the premiums for the ordinary life insurance, not more than $100 may be used to pay the premiums for the accident and/or health insurance contracts.

Where a trust established under a profit-sharing plan is committed to the payment of annual premiums for permissible insurance benefits for its participants, a reduction in profits which would be accompanied by a reduction in employer contributions under the plan might result in either (a) failure to pay the premiums due or (b) payment of the premiums with funds that have not been accumulated for the period prescribed by the plan for the deferment of distributions in an amount in excess of that which is "incidental". The latter alternative will result in disqualification of the trust under section 401(a) of the Code.

The amendment of an existing plan to provide permissible benefits will not be considered a curtailment of the plan if the employer's contributions to the plan are not reduced thereby.

Accordingly, it is held that the purchase by a trust established under an employees' profit-sharing plan of major medical hospitalization insurance, which constitutes a "distribution" to an employee of funds allocated to his account that have not been accumulated for the period prescribed by the plan for the deferment of distributions, will be treated as "incidental" and will not, therefore, prevent qualification of the trust under section 401(a) of the Code if the amount expended, when added to other permissible benefits (to the extent that each such benefit constitutes a "distribution") also purchased by the trust with

funds allocated to his account that have not been accumulated for the period prescribed by the plan for the deferment of distributions, does not exceed 25 percent of the total of the funds allocated to his account that have not been so accumulated.

Rev. Rul. 61–218

Title 28, chapter 17, of the United States Code provides for the "Resignation and Retirement of Judges." Section 371(a) thereof provides for lifetime payments of 100 percent of his salary to a justice or judge of the United States who resigns or retires after attaining 70 years of age with 10 years of service or after attaining age 65 with 15 years of service. A similar provision is contained in section 373 with respect to judges in Territories and Possessions of the United States. Section 372 provides for lifetime payments of one-half of his salary to a justice or judge who, with less than 10 years of service, is retired for disability. Section 375 provides for the payment of an annuity of $5,000 annually to the widows of justices of the Supreme Court of the United States. Under the provisions of section 376 of Title 28, Federal judges may elect to provide for the payment of annuities to their widows and surviving dependent children. For this purpose three percent is withheld from salary payments made to a judge both before and after retirement. Such withheld amounts are deposited in the Treasury of the United States to the credit of a fund known as "judicial survivors annuity fund." A widow's annuity, under section 376, is computed on a scale based upon years of judicial service of her husband. *Held*, while each of the above provisions constitutes a separate program for the specific beneficiaries named, the programs as a whole constitute one plan for the exclusive benefit of employees or their beneficiaries. See section 401(a)(3) of the Internal Revenue Code of 1954. *Held further*, such plan constitutes a qualified plan under section 401(a) of the Code.

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26 CFR 1.401–3: Requirements as to coverage. Rev. Rul. 61–147

Guides for determining whether a pension or annuity plan of a railroad employer is integrated with benefits provided by the Railroad Retirement Act as amended through 1960.

1. *Introduction.*—Section 1.401–3(e) of the Income Tax Regulations provides that if a classification of employees under a plan results in relatively or proportionately greater benefits for employees earning above any specified salary amount or rate than for those below such salary amount or rate, it may be found to be discriminatory within the meaning of section 401(a)(3)(B) of the Internal Revenue Code of 1954. It is further provided, however, that if the relative or proportionate differences in benefits which result from such classification are approximately offset by the benefits which are provided by the Social Security Act, or by other Federal or State laws, and which are not attributable to employee contributions thereunder, the plan will not be considered discriminatory merely because of such differences. See also section 1.401–4(b) of the regulations.

Guides for determining whether a plan is integrated with the benefits provided under the Railroad Retirement Act as amended through 1960 are set forth below.

2. *Definitions.*—Where used herein certain terms will have the meaning indicated below:

(a) The term "plan" means a pension plan as defined in section 1.401–1(b)(1)(i) of the regulations, or an annuity plan as defined in section 1.404(a)–3(a) of the regulations, and in which benefits are related to service for an employer as defined in part I section 1 of the Railroad Retirement Act, 45 U.S.C., Sec. 228a as amended.

(b) The term "service" refers to service for the employer providing the plan and may include service for associated employers joining in the plan so that their employees are covered by the same plan.

(c) The term "integrated" as applied to a plan or benefits under a plan means that differences in proportionate benefits favoring employees earning above any specified rate of compensation as compared with those earning below such rate resulting from a classification and/or difference in benefit rates under such plan will be considered approximately offset by the Railroad Retirement Act benefits which are not attributable to employee contributions thereunder, so that the plan is not considered discriminatory under the provisions of the regulations referred to in paragraph 1 by reason of such differences.

(d) The term "$4,800 excess plan" means a plan under which employees earning less than $4,800 a year are excluded from benefits, either by an eligibility requirement or by a benefit formula basing benefits only on compensation in excess of $4,800 a year.

3. *Basic rule for plans meeting certain conditions.*—A $4,800 excess plan is integrated with the benefits under the Railroad Retirement Act if the rate of normal annual retirement benefits under the plan for each year of credited service cannot exceed 1.75 percent of annual compensation in excess of $4,800, *provided* that the plan conforms to all of the following conditions:

(a) The rate of normal retirement benefit for each year of credited service is applied to the *actual* compensation (or some lower amount) in excess of $4,800 for each year of such service, past or future.

(b) There are no benefits payable in case of death before retirement.

(c) The normal form of retirement benefit is a straight life annuity payable only to the retired employee.

(d) Normal retirement age is not lower than age 65 for men and not lower than age 60 for women and, if benefits of any kind are payable in case of retirement or severance of employment before normal retirement age, such benefits are appropriately adjusted in accordance with paragraph 10.

(e) The employees do not contribute.

4. *Benefits based on compensation, other than actual compensation, in excess of $4,800.*—A $4,800 excess plan which conforms to all the conditions of paragraph 3, except that benefits are based on compen-

sation other than actual compensation in each year of credited service, is integrated:

(a) If the rate of normal retirement benefit for each year of credited service does not exceed 1.40 percent of the annual compensation in excess of $4,800 averaged over a definite period of at least 10 consecutive years; or

(b) If the rate of normal retirement benefit for each year of credited service does not exceed 1.15 percent of the annual compensation in excess of $4,800 averaged over a definite period of at least 5 (but less than 10) consecutive years; or

(c) If the rate of normal retirement benefit for each year of credited future service does not exceed 1.75 percent of the *actual* compensation in excess of $4,800 in each year of credited future service and the rate of normal retirement benefit for each year of credited prior service does not exceed

(i) 1.40 percent of the annual compensation in excess of $4,800 averaged over a definite period of at least 10 consecutive years prior to the date on which an employee becomes eligible for membership in the plan; or

(ii) 1.15 percent of the annual compensation in excess of $4,800, as of the date on which an employee becomes eligible for membership in the plan, or as of some definite earlier date, or averaged over a definite period of less than 10 consecutive years.

For the purposes of this paragraph 4, it is not acceptable to define the definite period as the period which will produce the highest average compensation, or to define the definite date as the date on which compensation was highest. However, for the purposes of this paragraph, a specified number of consecutive years, ending at actual retirement, or at the earlier of actual retirement or normal retirement age, or at the age 5 years before the earlier of actual retirement or normal retirement age, is acceptable.

5. *Benefits in case of disability before normal retirement age.*—A $4,800 excess plan which conforms to the conditions of paragraph 3, 4(a), 4(b), or 4(c), except that it provides for an immediate life annuity benefit, in case of severance due to disability occurring before normal retirement age, equal to the normal retirement benefit accrued on account of service rendered prior to such severance, is integrated if the eligibility conditions necessary for payment of such disability benefits under the plan are substantially equivalent to the conditions necessary for payment of disability benefits under the Railroad Retirement Act and if the rate of normal annual retirement benefit for each year of credited service does not exceed 90 percent of the rate or rates determined from whichever of such paragraphs is applicable.

6. *Benefits in case of death before retirement.*—A $4,800 excess plan which conforms to the conditions of paragraph 3, 4(a), 4(b), 4(c), or 5, except that it provides benefits in case of death before retirement not exceeding the higher of the reserve or the total prior contributions on a typical individual level annual premium funding method (and no other death benefits or life insurance except those for which the current cost is included in the income of the employee), is integrated if the rate of normal retirement benefit for any employee does not

exceed ⅝ of the rate or rates specified in whichever of such paragraphs is applicable.

7. *Normal form of retirement benefit an annuity for 10 years certain and life thereafter.*—A $4,800 excess plan which conforms to the conditions of paragraph 3, 4(a), 4(b), 4(c), 5, or 6, except that the normal form of retirement benefit is an annuity for 10 years certain and life thereafter is integrated if the rate of normal annual retirement benefit for each year of credited service does not exceed 90 percent of the rate or rates determined from whichever of such paragraphs is applicable.

8. *Widow's benefit payable in the event of death after the employee's normal retirement age or date, equal to one-half of the benefit payable to the retired employee.*—A $4,800 excess plan which conforms to the conditions of paragraph 3, 4(a), 4(b), 4(c), 5, or 6, except that, in the event of the death of any retired employee, when such death occurs after the retired employee's normal retirement age or date, a straight life annuity will be paid to the employee's widow in an amount equal to one-half of the retirement benefit payable to the retired employee, without regard to the age of the employee's widow, is integrated if the rate of normal retirement benefit, for any married employee, for each year of credited service, does not exceed 80 percent of the rate or rates determined from whichever of such paragraphs is applicable.

9. *Widow's benefit, payable in the event of death of an active or retired employee, equal to one-half of the employee's retirement benefit or one-half of the employee's accrued benefit, according to whether the employee was retired or active at the time of his death.*— A $4,800 excess plan which conforms to the conditions of paragraph 3, 4(a), 4(b), 4(c) or 5, except that, in the event of the death of any active or retired employee, a straight life annuity will be paid to the employee's widow in an amount equal to one-half of the employee's retirement benefit or one-half of the employee's accrued benefit, according to whether the employee was retired or active at the time of his death, without regard to the age of the employee's widow, is integrated if the rate of normal retirement benefit for any married employee, for each year of credited service, does not exceed 70 percent of the rate or rates determined from whichever of such paragraphs is applicable.

10. *Retirement or severance benefits beginning before age 65 (60 for women).*—If a $4,800 excess plan provides benefits attributable to employer contributions in case of retirement or severance of employment before age 65 for men or 60 for women, and if such retirement or severance benefits are not on account of disability as defined in paragraph 5, then in order for such plan to be integrated, such retirement or severance benefits cannot exceed the actuarial equivalent at the time of retirement or severance of the maximum benefits accrued to the time of such retirement or severance, determined in accordance with whichever of the preceding paragraphs is applicable. Where such early retirement or severance benefits are paid in the form of an annuity beginning before age 65 (60 for women) this requirement will be considered satisfied if the annual benefits on such early retirement or severance do not exceed such maximum accrued benefits reduced by one-fifteenth thereof for each year that the age of the employee at the time such benefits begin is less than age 65 (60 for women), or are equal in value to the reserve for normal retirement benefits

accumulated under a typical level premium funding method or unit credit cost method.

11. *Increase for employee contributions.*—A contributory $4,800 excess plan is integrated if the annual retirement benefit of any employee whose benefits do not commence before age 65 (60 for women) cannot exceed the applicable amount determined in accordance with the above guides, increased by one-tenth of his aggregate contributions *exclusive of those applicable to the current cost of insurance or death benefits in excess of the reserve or cash value.* If the benefits commence before age 65 (60 for women) such increase must be reduced by one-fifteenth for each year that the age of the employee at the time of commencement of such benefits is less than 65 (60 for women). Such increases are applicable regardless of the form of retirement benefit or provision for death benefits. It should be noted that where the plan provides for return of only *employee* contributions and interest thereon in case of death before or after retirement, such as when the retirement benefits are on a modified cash refund form, a reduction in otherwise allowable limits on account of such death benefits is not required. It should further be noted that if the increase for employee contributions is expressed in the form of a percentage of compensation, such percentage must be applied to the same compensation as such contributions were, even though compensation averaged over a shorter period is used as the basis for benefits attributable to employer contributions.

12. *Money purchase plans.*—A $4,800 excess plan which provides benefits with respect to service after the inception of the plan from employer contributions of a fixed amount or fixed percentage of each employee's compensation after the effective date of the plan is integrated if (a) the rate of employer *contributions* used for the benefit of any employee cannot exceed in any year 13 percent of such employee's *actual* compensation in excess of $4,800 in that year, and (b) the benefits for prior service of any employee do not exceed the amounts acceptable for prior service credits, as set forth in whichever of the preceding paragraphs is applicable.

13. *Offset plans.*—The term "offset plan" means a plan in which no employee and no portion of compensation is explicitly excluded by reason of a minimum compensation requirement and in which all the provisions including the benefit rates apply uniformly to all covered employees regardless of compensation except that the benefits otherwise provided by the plan formula are reduced or offset by a percentage of the employee's retirement annuity under the Railroad Retirement Act. An offset plan which conforms to conditions (b), (c), and (e) listed in paragraph 3 is integrated if the offset does not exceed 90 percent of the retirement annuity for which the employee is immediately eligible under the Railroad Retirement Act as amended through 1960. If the plan is as described in the preceding sentence except that it provides for death benefits of the form described in paragraph 6, the offset must not exceed 80 percent of such retirement annuity. If the plan is as described above except that the normal form of retirement benefit is an annuity for 10 years certain and life thereafter, the offset must not exceed 81 percent if the plan does not include death benefits of the form described in paragraph 6, or 72 percent if the plan does

include such death benefits. If the plan is as described above but provides for benefits described in any of the other preceding paragraphs, the offset must not exceed 90 percent, adjusted in accordance with the guides or factors in whichever of such paragraphs are applicable.

14. *Permissible minimum benefits.*—A plan is integrated if it conforms to the guides set forth in paragraphs 3 through 13 except that it provides a minimum retirement benefit not in excess of $240 a year, or $8 a year per year of service, plus increase for employee contributions as set forth in paragraph 11, or for minimum employer contributions with respect to any employee of $60 a year. However, such minimum is not to be used as a tolerance and may not be taken into account in determining whether higher benefits conform to the above guides. These limits on minimum benefits do not apply where (a) there is no minimum compensation requirement for obtaining the minimum benefits, and (b) the formula for determining the minimum benefits does not involve integration requirements in any other way.

15. *Optional forms of benefits.*—No adjustment is required to the rate or rates determined in accordance with whichever of the preceding paragraphs are applicable, on account of optional forms of benefits available under the plan, if the payments under the optional forms are determined as the actuarial equivalent of the normal form of benefit.

16. *Applicability of Revenue Ruling 12, C.B. 1953–1, 290.*—A $3,600 excess plan, as defined in Revenue Ruling 12, C.B. 1953–1, 290, will be considered integrated with the benefits provided under the Railroad Retirement Act if it conforms to the provisions of that ruling. The limits contained in that ruling may also be applied in the case of a plan under which employees earning less than $4,200 a year are excluded from benefits, by substituting $4,200 for $3,600 wherever it appears in that ruling.

A plan will also be considered integrated with the benefits provided under the Railroad Retirement Act if that portion of the benefits prior to any specified date conforms to the provisions of Revenue Ruling 12, and that portion of the benefits attributable to service subsequent thereto satisfies the applicable provisions of this ruling.

PART II.—MISCELLANEOUS PROVISIONS

SECTION 421.—EMPLOYEE STOCK OPTIONS

26 CFR 1.421–4: Modification, extension or renewal. Rev. Rul. 61–219

The cancellation of a restricted stock option prior to its expiration, at a time when the market value of the stock subject to the option was below the option price, and the immediate substitution therefor of a new option substantially similar except that the option price is reduced and the expiration date is extended, constitutes a modification and extension of the option to which the rules prescribed in section 421(e)(1) of the Internal Revenue Code of 1954 are applicable, subject to the exception provided therein.

Revenue Ruling 59–55, C.B.1959–1, 94, clarified.

Advice has been requested as to the Federal income tax consequences of the substitution of a new stock option for an old stock option under the circumstances described below.

A corporation which granted a restricted stock option in 1955, rescinded that option prior to its expiration date at a time when the market value of the stock subject to the option was below the option price. Immediately upon rescission of the old option, the corporation granted the optionee a new option substantially similar to the old option in all respects except that the option price was reduced and the expiration date was extended.

Section 421(e)(1)(A) of the Internal Revenue Code of 1954 provides that if the terms of any option to purchase stock are modified, extended, or renewed, such modification, extension, or renewal shall be considered as the granting of a new option. For the purpose of determining whether such new option meets the pricing requirements of section 421(d)(1)(A) of the Code, the general rule prescribed in section 421(e)(1)(B) of the Code provides that the fair market value of the stock subject to the option shall be considered as—

> (i) the fair market value of such stock on the date of the original granting of the option,
> (ii) the fair market value of such stock on the date of the making of such modification, extension, or renewal, or
> (iii) the fair market value of such stock at the time of the making of any intervening modification, extension, or renewal, whichever is the highest.

Section 421(e)(1)(A) of the Code applies with respect to any modification, extension, or renewal, but section 421(e)(1)(B) of the Code does not apply if the aggregate of the monthly average fair market values of the stock subject to the option for the 12 consecutive calendar months before the date of the modification, extension, or renewal, divided by 12, is an amount less than 80 percent of the fair market value of such stock on the date of the original granting of the option or the date of the making of any intervening modification, extension, or renewal, whichever is highest.

Section 421(e)(2) of the Code defines the term "modification" to mean (with certain exceptions not here pertinent) any change in the terms of the option which gives the employees additional benefits under the option. Under section 1.421–4(c)(2) of the Income Tax Regulations, an "extension" of an option refers to the granting by the corporation to the optionee of an additional period of time within which to exercise the option beyond the time originally prescribed.

In accordance with the above provisions, a change in the terms of an existing option to reduce the option price and extend the expiration date makes section 421(e)(1)(B) of the Code applicable in every case except where the single exception relating to the 80 percent rule provided in the last sentence of section 421(e)(1) makes it inapplicable.

The restrictions imposed by section 421(e) of the Code upon the modification, extension, or renewal of options may not be avoided by terminating an old option and replacing it with a new option similar in all material respects except for a reduction in the option price and an extension of the expiration date. Where such changes are made, they are considered as no more than a modification and extension of the old option, regardless of the purpose for the changes.

Accordingly, it is held that, under the circumstances involved here, the rescission of the old option and the granting of the new option constitute a modification and extension to which the rules prescribed in section 421(e)(1) of the Code are applicable, subject to the exception provided therein. The same result would obtain even in the absence of an extension.

In Revenue Ruling 59–55, C.B. 1959–1, 94, it is held that "new options issued at a more favorable price will qualify as restricted stock options provided that they comply with the provisions of section 421 of the Code." The conclusion reached herein is intended to clarify Revenue Ruling 59–55 to make it clear that the rules prescribed in section 421(e)(1) of the Code will be applied where a modification is made in the form of a new option.

Where there is a considerable delay in the granting of a new option after rescission of the old option, or a substantial change in the terms of the option, a determination whether there is a modification of the old option involves questions of fact to be resolved on the basis of the circumstances in each particular case. However, the result will not be changed merely by reason of a slight delay in the granting of a new option or a nominal change in the terms of the option.

Nothing in this ruling is intended to affect the granting of new options after the expiration of the term of old options.

SUBCHAPTER E.—ACCOUNTING PERIODS AND METHODS OF ACCOUNTING

PART II.—METHODS OF ACCOUNTING

Subpart A.—Methods of Accounting in General

SECTION 446.—GENERAL RULE FOR METHODS OF ACCOUNTING

26 CFR 1.446–1: General rule for methods of accounting.

Taxable year of inclusion of prepaid membership dues. See Ct.D. 1869, page 245.

Subpart B.—Taxable Year for Which Items of Gross Income Included

SECTION 451.—GENERAL RULE FOR TAXABLE YEAR OF INCLUSION

26 CFR 1.451–1: General rule for taxable year of inclusion.

Proceeds of an embezzlement. See Rev. Rul. 61–185, page 9.

Taxable year of inclusion of prepaid membership dues. See Ct.D. 1865, page 245.

26 CFR 1.451–2: Constructive receipt of income.

Cash payment due on new United States obligations charged against accrued interest payable on United States obligations surrendered. See Rev. Rul. 61–138, page 136.

SECTION 453.—INSTALLMENT METHOD

26 CFR 1.453–9: Gain or loss on disposition of installment obligations. Rev. Rul. 61–215

The taxpayer, an inventor, was a substantial stockholder in two corporations, both organized under the laws of the State of *R*. In 1955, he sold two patents to one of the corporations and, in 1958, he sold another patent to the other corporation. Each agreement of sale provided for payment to him by the purchaser-corporation of a specified sum (price) in fixed installments over a period of years, and he elected to return his income from the sales on the installment method under section 453 (a) and (b) of the Internal Revenue Code of 1954.

In 1959, for purposes of more efficient and economical engineering, manufacture, sales, distribution, and accounting, the two corporations, then solvent, having the same officers and directors, and operating successfully, entered into a statutory merger. Under the merger agreement, the surviving corporation became vested with all rights and property, including the patent or patents purchased from the taxpayer, and assumed all obligations and liabilities, including those for installment payments remaining to be made to the taxpayer, of each of the constituent corporations.

The merger was a "reorganization," as defined in section 368(a)(1)(A) of the Code, which resulted in no recognized gain or loss to either of the corporations, or to their stockholders, under sections 361 and 354 of the Code, respectively. The outstanding installment obligations of each of the constituent corporations were not changed in amounts and maturities. The surviving corporation continued both its former business and the business of its merged constituent.

Held, there was, in essence, not a substitution of a new or materially different obligor or obligation with respect to the outstanding installment obligations owing to the taxpayer by either of the constituent corporations. Accordingly, there was no satisfaction or disposition of the installment obligations of either corporation resulting in gain or loss to the taxpayer under section 453(d) of the Code. Therefore, the taxpayer should continue to return income from the patent sales on the installment method under section 453 (a) and (b) of the Code.

Subpart C.—Taxable Year for Which Deductions Taken

SECTION 461.—GENERAL RULE FOR TAXABLE YEAR OF DEDUCTION

26 CFR 1.461–1: General rule for taxable year of deduction.

Accrual of liability for bonuses under a plan in which the employer is obligated to pay a bonus of at least two percent and not more than three percent of the company's profits. See Rev. Rul. 61–127, page 36.

Subpart D.—Inventories

SECTION 472.—LAST-IN, FIRST-OUT INVENTORIES

26 CFR 1.472–1: Last-in, first-out inventories. Rev. Rul. 61–193

Price indexes for July 1961, published by the Bureau of Labor Statistics on September 6, 1961, for use by department stores employing the retail inventory and last-in, first-out inventory methods.

The following price indexes for July 1961, published by the Bureau of Labor Statistics on September 6, 1961, for use by department stores employing the retail inventory and last-in, first-out inventory methods, are accepted by the Internal Revenue Service pursuant to section 1.472–1(k) of the Income Tax Regulations and Mimeograph 6244, C.B. 1948–1, 21, for appropriate application to inventories for taxable years of 12 months ended June 30, 1961 and July 31, 1961.

Indexes are given on a national basis for store total, for 20 major groups of departments, and for two special group combinations—soft and durable goods. The store total index includes all departments, including some not listed separately, with the following exceptions; candy, foods, liquor, tobacco, paints, and wallpaper, as well as contract departments.

Bureau of Labor Statistics, Department Store Inventory Price Indexes, by Department Groups

[January 1941=100]

	Department group	July 1961	July 1960	Percent change* from July 1960 to July 1961
I	Piece goods	203.4	203.3	0
II	Domestics and draperies	204.2	201.8	1.2
III	Women's and children's shoes	264.8	262.8	.8
IV	Men's and boys' shoes	254.4	253.5	.4
V	Infant's wear	176.2	175.6	.3
VI	Women's underwear	179.4	177.0	1.4
VII	Women's and girls' hosiery	157.8	157.4	.3
VIII	Women's and girls' accessories	188.5	182.3	3.4
IX	Women's outerwear and girls' wear	183.4	185.9	−1.3
X	Men's clothing	226.8	219.6	3.3
XI	Men's furnishings	199.3	200.0	−.4
XII	Boys' clothing and furnishings	212.9	209.4	1.7
XIII	Jewelry	180.1	177.6	1.4
XIV	Notions	168.8	166.7	1.3
XV	Toilet articles and drugs	197.3	196.5	.4
XVI	Furniture and bedding	227.6	224.8	1.2
XVII	Floor covering	193.4	194.7	−.7
XVIII	Housewares	228.1	230.0	−.8
XIX	Major appliances	130.2	131.1	−.7
XX	Radios and television sets	127.1	130.7	−2.8
	Groups I–XV: Soft goods	201.3	200.1	.6
	Groups XVI–XX: Durable goods	196.4	197.1	−.4
Store total		200.3	199.5	.4

*Absence of a minus sign before percent change in this column signifies price increase.

SUBCHAPTER F.—EXEMPT ORGANIZATIONS

PART I.—GENERAL RULE

SECTION 501.—EXEMPTION FROM TAX ON CORPORATIONS, CERTAIN TRUSTS, ETC.

26 CFR 1.501(c)(3)–1: Organization organized and operated for religious, charitable, scientific, testing for public safety, literary, or educational purposes, or for the prevention of cruelty to children or animals. (Also 1.501(c)(6)–1.) Rev. Rul. 61–170

An association composed of professional private duty nurses and practical nurses which supports and operates a nurses' registry primarily to afford greater employment opportunities for its members is not entitled to exemption from Federal income tax under section 501(a) of the Internal Revenue Code of 1954 as an organization described in section 501(c)(3) of the Code.

Furthermore, the association is not entitled to exemption as a business league described in section 501(c)(6) of the Code since its primary purpose is the operation of a regular business of a kind ordinarily carried on for profit and it is engaged in rendering particular services for individual persons rather than promoting the general business conditions of the nursing profession.

Revenue Ruling 55–656, C.B. 1955–2, 262, distinguished.

Advice has been requested whether an association composed of professional nurses and practical nurses which operates a nurses' registry primarily to afford greater employment opportunities for its members is entitled to exemption from Federal income tax.

The instant association was incorported as a nonprofit corporation for the general purpose of organizing private duty and practical nurses for their mutual benefit and in order to make their services more readily available when needed by the general public. The bylaws state that its specific purposes are to provide employment for its members as well as to organize an adequate and available nursing placement service for the community. The association is controlled by a board of trustees composed of professional nurses. Its membership is open to both registered and practical nurses who meet specified requirements. The organization maintains a registry of its members showing their respective qualifications and the types of services they perform. Reference and placement from the register are made on a rotating basis upon a request for nursing services. Continued membership in the organization is contingent upon continued demonstration of ability and the adherence to ethical standards prescribed by the organization.

The income of the organization is derived principally from membership dues, fees and assessments. Expenditures are for salaries, office supplies and expenses, and other miscellaneous expenses. No part of its net earnings inures to the benefit of any private shareholder or individual.

Section 501(c)(3) of the Code describes certain organizations which are exempt from taxation under section 501(a) of the Code. The exemption applies to any corporation, community chest, fund, or foundation, organized and operated exclusively for religious, chari-

table, scientific, testing for public safety, literary, or educational purposes, or for the prevention of cruelty to children or animals, no part of the net earnings of which inures to the benefit of any private shareholder or individual, no substantial part of the activities of which is carrying on propaganda, or otherwise attempting, to influence legislation, and which does not participate in, or intervene in (including the publishing or distributing of statements) any political campaign on behalf of any candidate for public office.

Section 1.501(c)(3)–1(a)(1) of the Income Tax Regulations provides that in order to be exempt as an organization described in section 501(c)(3), an organization must be both organized and operated exclusively for one or more of the purposes specified in such section. If an organization fails to meet either the organizational test or the operational test, it is not exempt.

Section 1.501(c)(3)–1(d)(ii) of the regulations provides that an organization is not organized or operated exclusively for one or more of the purposes specified in section 501(c)(3) unless it serves a public rather than a private interest. Thus, to meet the requirements of section 501(c)(3), it is necessary for an organization to establish that it is not organized or operated for the benefit of private interests such as designated individuals, the creator or his family, shareholders of the organization, or persons controlled, directly or indirectly, by such private interests.

On the basis of the information presented, the instant organization is primarily engaged in the performance of personal services by operating an employment service principally for the benefits of its members. Public participation in the management and support of the organization is negligible. This is shown by the fact that it draws its support primarily from members and is controlled by a board of trustees composed of professional nurses, without public participation of any kind. Therefore, the organization is not free from substantial private considerations in the operation of its nurses' register.

Accordingly, it is held that the instant organization does not qualify for exemption from Federal income tax under section 501(a) of the Code as an organization described in section 501(c)(3) of the Code since it is shown that the organization is not organized and operated exclusively for charitable purposes or for any of the other purposes specified therein.

The instant situation is distinguishable from Revenue Ruling 55–656, C.B. 1955–2, 262, wherein it is held that the organization involved therein was exempt from Federal income tax as a charitable organization described in section 501(c)(3) of the Code, since it was primarily controlled and supported by the general public for the public benefit and did not exist primarily for the purpose of providing an employment agency for the benefit of members as is the case with the instant association.

Consideration has also been given to the question of whether the instant association qualifies for exemption as a business league under section 501(c)(6) of the Code.

Section 1.501(c)(6)–1 of the Income Tax Regulations describes a business league as an organization of persons having some common business, the purpose of which is to promote such common interest and not to engage in a regular business of a kind ordinarily carried

on for profit. Such an organization is of the same general class as a chamber of commerce or board of trade. Thus, its activities should be directed to the improvement of business conditions of one or more lines of business as distinguished from the performance of particular services for individual persons. An organization whose purpose is to engage in a regular business of a kind ordinarily carried on for profit even though the business is conducted on a cooperative basis or produces only sufficient income to be self-sustaining, is not a business league.

Based on its stated purposes and activities, the instant association is organized and operated primarily as an employment agency for the benefit of its members. As such, its functions are substantially similar to those of a commercial employment agency. Thus, it is engaged in a regular business of a kind ordinarily carried on for profit and is rendering particular services for individual persons rather than promoting the general business conditions of the nursing profession.

Accordingly, it is held that the instant association, which maintains a nurses' registry of its member nurses and assigns them to places of employment, is not entitled to exemption from Federal income tax as an organization described in section 501(c)(6) of the Code. Compare G.C.M. 20941, C.B. 1939–1 (Part I), 186, which holds that a nurses' association incorporated and operated for the betterment of the profession is entitled to exemption from Federal income taxation as a business league.

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26 CFR 1.501(c)(4)–1: Civic organizations and local associations of employees. Rev. Rul. 61–153

A nonprofit corporation, having no capital stock, no assets and no income, was established for the sole purpose of cooperating with the parent-teacher association of a local school district in its activities, by reviewing the proposals of and designating the insurance company allowed to solicit accident insurance from the students, the teachers, and the other employees of the school district. *Held*, it qualifies as an organization not organized for profit but operated exclusively for the promotion of social welfare under the provisions of section 501(c)(4) of the Internal Revenue Code of 1954 and is exempt from Federal income tax under section 501(a) of the Code.

Advice has been requested whether the organization described below qualifies for exemption from tax under section 501(a) of the Internal Revenue Code of 1954.

M corporation was organized under the nonprofit corporation law of a state without capital stock for the purpose of cooperating with a parent-teacher association of a school district in carrying on certain activities. These activities consist solely of an annual selection of the insurance company which is to be allowed to solicit accident insurance from the students, the teachers and the other employees of the particular school district. The selection is based on proposals submitted to the corporation by the insurers. The corporation has no assets and no income, the expenses being borne by donations by citizens. The membership consists of fifteen members of the parent-teacher association who are designated by that organization.

Section 501(c) of the Code describes certain organizations exempt from tax under section 501(a) of the Code and reads, in part, as follows:

> (4) Civic leagues or organizations not organized for profit but operated exclusively for the promotion of social welfare * * *.

Section 1.501(c)(4)–1 of the Income Tax Regulations provides, in part, as follows:

> (a) *Civic organizations.*—(1) *In general.*—A civic league or organization may be exempt as an organization described in section 501(c)(4) if:
> (i) It is not organized or operated for profit; and
> (ii) It is operated exclusively for the promotion of social welfare.
> (2) *Promotion of social welfare.*—(i) *In general.*—An organization is operated exclusively for the promotion of social welfare if it is primarily engaged in promoting in some way the common good and general welfare of the people of the community. An organization embraced within this section is one which is operated primarily for the purpose of bringing about civic betterments and social improvements * * *.

It is held that the *M* corporation qualifies as an organization not organized for profit but operated exclusively for the promotion of social welfare under the provisions of section 501(c)(4) of the Code and is, therefore, exempt from Federal income tax under section 501(a) of the Code.

Rev. Rul. 61–158

> An organization created exclusively for the promotion of social welfare which conducts weekly drawings among members of the general public as its principal activity and uses the profits therefrom primarily for the payment of its general expenses is not entitled to exemption from Federal income tax as an organization described in section 501(c)(4) of the Internal Revenue Code of 1954.

Advice has been requested whether a nonprofit organization, created exclusively for the promotion of social welfare, which conducts a weekly drawing among members of the general public as its principal activity and uses the profits therefrom primarily for the payment of its general expenses, is entitled to exemption from Federal income tax under section 501(c)(4) of the Internal Revenue Code of 1954.

The instant organization was formed as a nonprofit corporation under state law exclusively for the promotion of social welfare. Its bylaws provide that all of its net profits above reasonable operating expenses shall be devoted exclusively to social welfare purposes and that no part of its net earnings shall inure to the benefit of any member or other private individual.

The organization owns its quarters consisting of a meeting-hall, dining room and bar. The dining room and bar facilities are open from three to five evenings each week for members only. Members meet at regular intervals and pay only nominal monthly dues.

The organization also conducts weekly drawings which are managed by two full-time paid employees. The tickets for the drawings are sold to the general public primarily by non-members who otherwise have regular employment. Each salesman receives a commission of 25 percent of the selling price of each ticket he sells. The drawings are held at the organization's meeting-hall each Saturday

evening. Cash prizes are paid to the holders of the three winning tickets.

Income attributable to the operation of the weekly drawings constitutes the primary source of overall gross receipts. An analysis of the gross receipts and disbursements discloses that the major portion of the gross profits from all sources was used to pay expenses of the organization, leaving only a small portion for furtherance of the organization's stated purposes.

Section 501(c) of the Code describes certain organizations which are exempt from Federal income tax under section 501(a) of the Code and reads, in part, as follows:

> (4) Civic leagues or organizations not organized for profit but operated exclusively for the promotion of social welfare, or local associations of employees, the membership of which is limited to the employees of a designated person or persons in a particular municipality, and the net earnings of which are devoted exclusively to charitable, educational, or recreational purposes.

Section 1.501(c)(4)–1 of the Income Tax Regulations provides in general that a civic league or organization may be exempt if both of the following conditions are met. The first condition is that it must not be organized or operated for profit. The second condition is that it must be operated exclusively for the promotion of social welfare. An organization is operated exclusively for the promotion of social welfare if it is primarily engaged in promoting in some way the common good and general welfare of the people of the community.

To be embraced within the scope of section 501(c)(4) of the Code an organization must be one which is operated primarily for the purpose of bringing about civic betterments and social improvements. An organization is not operated primarily for the promotion of social welfare if its primary activity is operating a social club for the benefit, pleasure or recreation of its members, or is carrying on a business with the general public in a manner similar to organizations which are operated for profit.

Under the foregoing regulations, an organization which carries on a business with the general public as a primary activity for profit is not entitled to exemption from Federal income tax under section 501(c)(4) of the Code, even though it may formally be organized exclusively for social welfare purposes.

The instant organization conducts weekly drawings among the general public with the participation of nonmember soliciting agents. Its gross profits from drawings are the primary source of its income. Only a small portion of the gross profits is used in the furtherance of the organization's stated purposes, the balance of such profits being used for the payment of general expenses. Thus, members are relieved from paying a larger share of the expenses than otherwise would have been the case.

The instant organization, by conducting a lottery on a weekly basis with the general public and using almost the entire proceeds therefrom to pay general expenses of the organization in the circumstances described above, is not operating exclusively for the promotion of social welfare, but is considered to be engaged in a business for profit. Accordingly, it is held that the organization is not entitled to exemption from Federal income tax under section 501(c)(4) of the Code.

26 CFR 1.501(c)(6)–1: Business leagues, chambers of commerce, real estate boards, and boards of trade. Rev. Rul. 61–177

A corporation organized and operated primarily for the purpose of promoting a common business interest and bettering the business conditions of one or more lines of business, which otherwise meets the tests for exemption under section 501(c)(6) of the Internal Revenue Code of 1954, is exempt under that section as a business league even though its sole activity is directed to the influencing of legislation which is germane to such common business interest. Revenue Ruling 54–442, C.B.1954–2, 131, modified.

Advice has been requested whether an organization formed for the purpose of promoting a common business interest and bettering the business conditions of one or more lines of business which otherwise meet the tests for exemption from Federal income tax as an organization described in section 501(c)(6) of the Internal Revenue Code of 1954, may qualify for exemption under that section where its sole or principal activity is the advocacy of legislation beneficial to such common business interest.

The membership of the instant organization is composed of business groups and individuals representing diverse lines of endeavor and geographic areas. They are united for the purpose of promoting a common business interest and improving their business conditions by working for the enactment of legislation designed to improve their competitive standing in the various lines of business, industry, etc., in which they are engaged.

Section 501(c)(6) of the Code describes certain organizations exempt from Federal income tax under section 501(a) of the Code and reads as follows:

> Business leagues, chambers of commerce, real-estate boards, or boards of trade, not organized for profit and no part of the net earnings of which inures to the benefit of any private shareholder or individual.

Section 1.501(c)(6)–1 of the Income Tax Regulations provides, in part, as follows:

> A business league is an association of persons having some common business interest, the purpose of which is to promote such common interest and not to engage in a regular business of a kind ordinarily carried on for profit. It is an organization of the same general class as a chamber of commerce or board of trade. Thus, its activities should be directed to the improvement of business conditions of one or more lines of business as distinguished from the performance of particular services for individual persons. * * *

There is no requirement, by statute or regulations, that a business league, chamber of commerce, etc., in order to be considered exempt as such, must refrain from carrying on propaganda or influencing legislation.

The objectives sought by the instant organization can be attained only through legislation. It follows, therefore, that its legislative activities are germane to the attainment of its objectives. Accordingly, it is held that it qualifies for exemption from Federal income tax as a business league within the contemplation of section 501(c)(6) of the Code even though its sole activity is the advocacy of legislation.

Revenue Ruling 54–442, C.B.1954–2, 131, relating to the exemption of business leagues from Federal income taxation, is hereby modified

to the extent that it suggests that engaging in other than incidental legislative activities will necessarily disqualify an organization from exemption under section 101(7) of the Internal Revenue Code of 1939, now section 501(c)(6) of the Internal Revenue Code of 1954.

However, with respect to dues, assessments, or other payments to an organization of the nature described in the second paragraph of this ruling, it should be noted that section 1.162–15(c) of the Income Tax Regulations provides that dues and other payments to an organization, such as a labor union or a trade association, which otherwise meet the requirements of the regulations under section 162, are deductible in full unless a substantial part of the organization's activities consists of making expenditures for lobbying purposes, for the promotion or defeat of legislation, for political campaign purposes (including the support of or opposition to any candidate for public office), or for carrying on propaganda (including advertising) related to any of the foregoing purposes. If a substantial part of the activities of the organization consists of one or more of those so specified, deduction will be allowed only for such portion of such dues and other payments as the taxpayer can clearly establish is attributable to activities other than those so specified. The determination as to whether such specified activities constitute a substantial part of an organization's activities shall be based on all the facts and circumstances. In no event shall special assessments or similar payments (including an increase in dues) made to any organization for any of such specified purposes be deductible.

An organization which considers itself within the scope of this Revenue Ruling should, in order to establish exemption under section 501(c)(6) of the Code, file an application on Form 1024, Exemption Application, with the District Director of Internal Revenue for the Internal Revenue District in which is located the principal place of business or principal office of the organization. See section 1.501(a)–1 of the Income Tax Regulations.

An association of professional nurses and practical nurses which operates a nurses registry. See Rev. Rul. 61–170, page 112.

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26 CFR 1.501(c)(13)–1: Cemetery companies. Rev. Rul. 61–137

> To acquire property with which to operate, a newly organized cemetery company purchased land for an undeterminable total purchase price which is to be paid for on the basis of a percentage of the gross proceeds realized from the sale of individual lots. *Held*, the organization is not entitled to exemption from Federal income tax under section 501(c)(13) of the Internal Revenue Code of 1954.

The Internal Revenue Service has been requested to advise whether a cemetery company which purchases cemetery property for no fixed total price but instead for an undeterminable price based on a percentage of the proceeds from the sale of individual lots is entitled to exemption as a cemetery company described in section 501(c)(13) of the Internal Revenue Code of 1954.

The organization was incorporated under the laws of its state for the purpose of owning and operating a nonprofit cemetery company for the burial or disposal of human remains, with powers to do all things necessary or incident to the carrying out of such purposes. The articles of incorporation provide that the organization shall be under the direction and control of seven trustees. Under the bylaws, each lot owner is declared to be a member with one vote in the proceedings of the organization. The articles also provide that no part of the net earnings of the organization shall inure to any private shareholder or individual.

The information presented discloses that subsequent to its organization but prior to the commencing of sales operations, the organization purchased a tract of land from its organizers. The land was conveyed to the organization pursuant to a contract of sale providing for a purchase price of 35 percent of the sales price of any and all cemetery graves or lots sold from such land. There was no stipulation in the contract of sale stating the total amount to be paid for the land. The reasonable appraised value of the acreage at the time of conveyance was less than one-half of the amount which the vendor could reasonably expect to realize under his contract with the cemetery company on the basis of current lot prices.

The activities of the instant corporation consist of owning, operating and maintaining a cemetery for the interment of human remains. The receipts are derived from sales of grave sites, burial services and interment supplies. Expenditures are made for salaries, commissions to salesmen of burial sites, taxes, payments on cemetery property, insurance, maintenance of cemetery property, payments into the perpetual care fund and miscellaneous operating expenses.

Section 501(c) of the Code describes certain organizations exempt from income tax under section 501(a) and reads, in part, as follows:

> (13) Cemetery companies owned and operated exclusively for the benefit of their members or which are not operated for profit; and any corporation chartered solely for burial purposes as a cemetery corporation and not permitted by its charter to engage in any business not necessarily incident to that purpose, no part of the net earnings of which inures to the benefit of any private shareholder or individual.

In *Forest Lawn Memorial Park Association, Inc.*, v. *Commissioner*, 45 B.T.A. 1091 (1941), where the association entered into a contract for the purchase of cemetery lands on the basis of a percentage of the gross proceeds from the sale of indivdual lots, etc., the United States Board of Tax Appeals held, in part, that there was no inurement of the organization's net earnings to the benefit of any private individual, because the amounts paid as the purchase price of the land were deductions from gross receipts and thus never became a part of the organization's net earnings. The *Forest Lawn Memorial Park Association, Inc.*, case is not followed as a precedent in the disposition of similar cases. See nonacquiescence, C.B. 1960–2, 8. Also, the Board's holding in that case is contrary in principle to the decisions in *Texas Trade School* v. *Commissioner*, 30 T.C. 642 (1958), affirmed, 272 Fed. (2d) 168 (1959); *Mabee Petroleum Corporation* v. *United States*, 203 Fed (2d) 872 (1953); *Northern Illinois College of Optometry*, Tax Court Memorandum Opinion, entered August 23, 1943. The first of the cited cases involved the payment of excessive rentals and the latter two involved

the payment of excessive compensation. The courts found that such payments constituted inurement of net earnings of the organizations to the payees.

Where a cemetery company acquires land at an undeterminable price, to be paid for on the basis of a percentage of the proceeds from the sale of individual lots from the tract, the vendor of the land has a continuing interest in the land. Any appreciation in value, whether it be due to the state of the market generally or the cemetery's own efforts in undertaking capital improvements, etc., will result in a benefit to the vendor of the land. Continuing participation in the earnings of the cemetery company will also ordinarily result in receipt by the vendor of a total price substantially in excess of the reasonable value of the land at the time of its sale to the cemetery company. Under these circumstances it is concluded that the purchase price is unreasonable and that a cemetery company which enters into such a contract of sale may not qualify for exemption under section 501(c)(13) of the Code.

In the instant case, the facts show that no fixed purchase price has been set for the property, the amount received by the vendor is based on a percentage of the sale prices of individual lots sold each year, and if a normal selling period is assumed the vendor stands to receive ultimately for the property an amount more than double the value of the land at the time of its sale to the cemetery corporation.

Applying the foregoing reasoning to these facts, it is held that the instant organization is not entitled to exemption from Federal income tax as a cemetery company described in section 501(c)(13) of the Internal Revenue Code of 1954.

SUBCHAPTER I.—NATURAL RESOURCES

PART I.—DEDUCTIONS

SECTION 611.—ALLOWANCE OF DEDUCTION FOR DEPLETION

26 CFR 1.611–1: Allowance of deduction for depletion.

Trust or estate as member of a partnership or beneficiary of another trust. See Rev. Rul. 61–211, page 124.

SECTION 613.—PERCENTAGE DEPLETION

26 CFR 1.613–3: Gross income from the property.

Rules for making the election regarding the computation of the percentage depletion allowance for certain clays and shale used in the manufacture of certain products for taxable years beginning before 1961. See T.D. 6575, page 261.

SECTION 614.—DEFINITION OF PROPERTY

26 CFR 1.614–2: Election to aggregate separate operating mineral interests under section 614(b). (Also 1.614–3, 1.614–4.) Rev. Rul. 61–194 [1]

An election with respect to the treatment of operating mineral interests required under section 614(b), (c), or (d) of the Internal Revenue Code of 1954, will not be invalidated by the mere failure to submit therewith an amended return or claim for refund or credit or the details and computation of depletion allowable for the taxable period subsequent to the first taxable year for which the election is applicable.

In order to facilitate the audit and examination of income tax returns involving aggregation of operating mineral interests, the procedure prescribed herein may be followed at the option of taxpayers involved.

Sections 1.614–2(d)(2), 1.614–3(f)(5), and 1.614–4(e) of the Income Tax Regulations provide for the manner in which taxpayers are to make certain elections required under section 614(b), (c), and (d) of the Internal Revenue Code of 1954 with respect to the treatment of separate operating mineral interests. The elections must be made within the time prescribed by law for filing the return (including extensions of time therefor). Where such time falls before May 1, 1961, the election must be made no later than such date or within the period of an extension granted pursuant to section 1.614–7 of the regulations. The elections are binding on the taxpayer for the first taxable year for which the election is effective and all subsequent taxable years unless consent to a different treatment is obtained from the Commissioner of Internal Revenue.

The election for such first taxable year forms the basis for the treatment of such operating mineral interests for subsequent taxable years and for the treatment of subsequent additions and acquisitions of other separate operating mineral interests.

The regulations require that the elections under the applicable provisions of the Code must be made by a statement attached to the income tax return, amended return if necessary, or, if appropriate, claim for refund or credit, of the taxpayer for the taxable year for which the elections are effective. The statement must include a general description, accompanied by appropriately marked maps, if necessary, which accurately circumscribe the scope of the aggregation and identify the properties to be treated separately as well as a description of the operating unit in sufficient detail to show that the aggregated operating mineral interests are properly within a single operating unit.

The question whether a taxpayer has properly identified and selected the separate operating mineral interests which he elected to aggregate or treat separately for the first taxable year is a matter

[1] Based on Technical Information Release 337, dated September 13, 1961.

to be determined in the audit and examination of the taxpayer's return for such year. In the case of elections for the first taxable year to which the elections are effective, the statement of election, identification of properties and election thereto, and computation of depletion must be complete in all detail. However, where the statement of election required by regulations under section 614 of the Code is filed, setting forth sufficient information to identify the operating mineral interests involved and the elections applicable to such interests, the mere failure to submit therewith an amended return or claim for refund or credit or the details and computation of depletion allowable for the taxable period subsequent to the first taxable year for which the election is applicable will not be construed as invalidating such elections, provided the taxpayer upon request files an amended return, if necessary, and, if appropriate, a claim for refund or credit, and provided that the taxpayer upon request makes such details or computations for subsequent years available to the Service within a reasonable length of time.

This procedure will be followed only where the taxpayer further indicates in the statement attached to the amended return or claim that (1) he will submit whatever waivers of the statute of limitation on assessment are requested by the district director for the years involved, and (2) he will file the necessary details and computations for taxable years subsequent to the first taxable year for which the elections are effective as soon as practicable upon completion of the examination of the return for such first taxable year.

It is emphasized that this procedure does not affect the time for filing the elections under section 614 (b), (c), or (d) of the Code, including elections with respect to operating mineral interests added or acquired after the first taxable year for which an election is effective.

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26 CFR 1.614–3: Rules relating to separate operating mineral interests in the case of mines.

Procedure to facilitate the audit and examination of income tax returns of taxpayers involved in making elections with respect to the treatment of mineral interests for depletion purposes. See Rev. Rul. 61–194, page 121.

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26 CFR 1.614–4: 1939 Code treatment with respect to separate operating mineral interest in the case of oil and gas wells.

Procedure to facilitate the audit and examination of income tax returns of taxpayers involved in making elections with respect to the treatment of mineral interests for depletion purposes. See Rev. Rul. 61–194, page 121.

SUBCHAPTER J.—ESTATES, TRUSTS, BENEFICIARIES, AND DECEDENTS

PART I.—ESTATES, TRUSTS, AND BENEFICIARIES

Subpart A.—General Rules for Taxation of Estates and Trusts

SECTION 641.—IMPOSITION OF TAX

26 CFR 1.641(b)-2: Filing of returns and payment of the tax. T.D. 6580 [1]

TITLE 26—INTERNAL REVENUE.—CHAPTER I, SUBCHAPTER A, PART 1.—INCOME TAX; TAXABLE YEARS BEGINNING AFTER DECEMBER 31, 1953

Amendment of the Income Tax Regulations under section 641 of the Internal Revenue Code of 1954, relating to imposition of tax on estates and trusts.

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

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

The Service has received a number of inquiries concerning the application of paragraph (b) of § 1.641(b)-2 of the Income Tax Regulations (26 CFR Part 1) to the bankrupt estate of an individual. Some of these inquiries have been prompted by the order of the referee in bankruptcy entered on February 27, 1961, in the case of *In the matter of John Henry Kirby, No. 1717 in Bankruptcy* (USDC SD Texas, Houston Division). In that case it was held that the bankrupt estate of an individual is not liable for Federal income tax on the income earned during bankruptcy proceedings. In support of his order, the referee relied in part upon the above-mentioned provisions of the regulations. The case is now pending on a petition to the District Court for review of the referee's order. In order to obviate future inquiries and to prevent further misunderstanding as to the application of paragraph (b) of § 1.641 (b)-2 to the bankrupt estate of an individual, as in the referee's order in the *Kirby* case, the regulations are amended as follows:

Paragraph (b) of § 1.641(b)-2 is amended to read as follows:

§ 1.641(b)-2 FILING OF RETURNS AND PAYMENT OF THE TAX.

* * * * * * *

(b) The estate of an infant, incompetent, or other person under a disability, or, in general, of an individual or corporation in receivership or a corporation in bankruptcy is not a taxable entity separate from the person for whom the fiduciary is acting, in that respect differing from the estate of a deceased person or of a trust. See section 6012(b) (2) and (3) for provisions relating to the obligation of the fiduciary with respect to returns of such persons.

Because the amendment made herein merely clarifies an ambiguity appearing in the regulations, and since the amendment reflects a position already publicly adopted by the Internal Revenue Service in litigation, public participation would not be helpful and, therefore, it is found that it is unnecessary to issue this Treasury Decision with

[1] 26 F.R. 11486.

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 such Act.

(This Treasury Decision is issued under the authority contained in section 7805 of the Internal Revenue Code of 1954 (68A Stat. 917; 26 U.S.C. 7805).)

MORTIMER M. CAPLIN,
Commissioner of Internal Revenue.

Approved November 29, 1961.

STANLEY S. SURREY,
Assistant Secretary of the Treasury.

(Filed by the Division of the Federal Register on December 4, 1961, 8:46 a.m., and published in the issue of the Federal Register for December 5, 1961, 26 F.R. 11486)

SECTION 642.—SPECIAL RULES FOR CREDITS AND DEDUCTIONS

26 CFR 1.642(e)–1: Depreciation and depletion. (Also Sections 167, 611, 702; 1.167(g)–1, 1.611–1, 1.702–1.) Rev. Rul. 61–211

> Where a trust or an estate is entitled, as a member of a partnership or as an income beneficiary of another trust, to a portion of the depreciation or depletion deduction allowable to the partnership or the other trust, its distributive share of such deductions may be apportioned between the recipient trust and its income beneficiaries or the estate and its heirs, legatees and devisees, as the case may be, in the manner prescribed by sections 167(g) and 611(b) of the Internal Revenue Code of 1954 and the regulations thereunder.

Advice has been requested whether any depreciation or depletion claimed and allowable as a deduction to a partnership or another trust, of which an estate or trust is a member or a beneficiary, must be brought over to the return of the estate or trust and allocated to the fiduciary and beneficiary.

Section 642(e) of the Internal Revenue Code of 1954 provides that an estate or trust shall be allowed the deduction for depreciation and depletion only to the extent not allowable to beneficiaries under sections 167(g) and 611(b) of the Code.

Section 702 of the Code provides, in substance, that, in determining his income tax, each partner shall take into account separately his distributive share of the partnership's items of income, gain, loss, deduction, or credit, to the extent provided by the Code and by regulations prescribed by the Secretary of the Treasury or his delegate. The character of any such item included in a partner's distributive share shall be determined as if the item were realized by the partner directly from the source from which realized by the partnership.

Sections 167(g) and 611(b)(3) and (4) of the Code relate, respectively, to the allowable depreciation deduction in the case of life tenants and beneficiaries of trusts and estates and to the allowable deduction for depletion in the case of property held in trust or by an estate.

Section 1.167(g)–1(b) of the Income Tax Regulations provides, in part, that if depreciable property is held in trust, the allowable deduction is to be apportioned between the income beneficiaries and the

trustee on the basis of the trust income allocable to each, unless the governing instrument (or local law) requires or permits the trustee to maintain a reserve for depreciation in any amount. In the case of an estate, the allowable deduction shall be apportioned between the estate and the heirs, legatees, and devisees on the basis of the income of the estate which is allocable to each.

Section 1.611–1(c) of the regulations provides, in part, that if mineral property or timber property is held in trust, the allowable deduction for depletion is to be apportioned between the income beneficiaries and the trustee on the basis of the trust income from such property allocable to each, unless the governing instrument (or local law) requires or permits the trustee to maintain a reserve for depletion in any amount. In the case of mineral property or timber property held by an estate, the deduction for depletion shall be apportioned between the estate and its heirs, legatees, and devisees on the basis of income of the estate which is allocable to each.

If a partnership agreement provides for a special allocation of depreciation or depletion to a partner which is a trust or an estate, such trust or estate may determine its share of the partnership deduction for depreciation and depletion as if it were realized directly from the depreciable or depletable partnership property. Therefore, such a partner is considered the holder of a share of the partnership depreciable or depletable property for the purpose of any allocation of the deductions between the trust and its beneficiaries, or the estate and its heirs, legatees and devisees, as the case may be.

Since, in the case of property held in trust, the depreciation or depletion deduction allowable under sections 167 and 611 of the Code, respectively, may be apportioned between the beneficiaries and the trustee in the manner prescribed by those sections and the regulations thereunder, similar treatment should be accorded to the beneficiary and trustee of a trust which is the beneficiary of another trust. Likewise, similar treatment should be accorded where an estate is the beneficiary of a trust.

Accordingly, it is held that where a trust or an estate is entitled, as a member of a partnership or as an income beneficiary of another trust, to a portion of the depreciation or depletion deduction allowable to the partnership or the other trust, its distributive share of such deductions may be apportioned between the recipient trust and its income beneficiaries or the estate and its heirs, legatees and devisees, as the case may be, in the manner prescribed by sections 167(g) and 611(b) of the Code and the regulations thereunder.

Subpart E.—Grantors and Others Treated as Substantial Owners

SECTION 673.—REVERSIONARY INTERESTS

26 CFR 1.673(a)–1: Reversionary interests; income payable to beneficiaries other than certain charitable organizations; general rule. (Also Sections 170, 677; 1.170–2, 1.677(b)–1.) — Rev. Rul. 61–223

The grantor of a trust does not have a "reversionary interest" within the meaning of section 673 of the Internal Revenue Code of

1954 merely because trust income or corpus, in the discretion of a corporate trustee, may be applied for the support and maintenance of the grantor's minor child. Income from such a trust is not taxable to the grantor, under subpart E, subchapter J, chapter 1, subtitle A of the Code, except to the extent actually used for the support and maintenance of the minor child.

However, in such a case the grantor does have a "reversionary interest" in such trust, as that term is used in section 170(b)(1)(D) of the Code, since there is a possibility that income or corpus in excess of the five percent referred to in section 170(b)(1)(D)(ii) of the Code may be used for the "benefit of the grantor" in supporting the minor child. Therefore, no deduction for a charitable contribution is allowable to the grantor for so-called charitable charges placed upon the trust by the grantor where neither particular property or fund nor an interest in any particular property or fund is dedicated solely for charitable purposes.

Advice has been requested (1) whether the grantor of the trust described below has a "reversionary interest" in such trust, for the purpose of determining whether the grantor is taxable on trust income, and (2) whether the grantor is entitled to deductions for charitable contributions for the amounts of certain so-called charitable charges placed on the trust.

In 1959, the grantor created a trust for both a charitable and a private purpose. The grantor named himself and a corporate bank as trustees. The trust is to continue during the lives of the grantor's wife and minor child for the benefit of a class consisting of the wife, the child, the child's wife, the child's issue, and the spouses of his issue. Upon the death of the two measuring lives, the remainder is to be paid to a class of remaindermen, not relevant for the purposes of this Revenue Ruling.

The trust agreement provides that the sum of $11x$ dollars shall constitute a charge upon the trust fund to be satisfied by payments to be made to qualified charitable organizations (organizations qualifying under section 170(c) of the Internal Revenue Code of 1954) over a period of 44 years or less, with interest compounded annually at three and one-half percent. The payments may be made out of income or principal within the discretion of the corporate trustee. However, each payment reduces the portion of the charged placed upon the trust fund for charitable purposes by the amount of such payment.

In making payments to other than the charitable organizations, the trust instrument provides that the trust fund cannot be reduced to an amount less than 150 percent of the unsatisfied charge. The trust instrument further provides that the grantor shall have the power to increase the charitable charge upon the trust at any time but only on condition that the amount of his contribution to corpus equals at least 150 percent of the additional charge for charitable purposes. Pursuant to this provision, the grantor added property to the trust in 1960, increasing the total charitable charge by $81x$ dollars.

After the corporate trustee has set aside sums for charitable purposes, the grantor has the power to name the charitable donees and the amount that each is to receive. The trust is declared to be irrevocable but can be terminated by the corporate trustee with the consent of the grantor's wife, which is required during her lifetime.

The trust instrument provides that the corporate trustee has the discretionary power to apply trust income or corpus for the use of the

grantor's minor child "for his care, comfort, education and welfare," etc. The instrument further provides that, if the corporate trustee makes a payment to the minor child, the trustee shall be relieved of all responsibility with respect to such a payment and shall not be accountable for the application or use thereof.

Under section 673 of the Code, the grantor is considered to be the owner of any portion of a trust (and, in effect, taxable on the income therefrom) in which he has a reversionary interest in either the corpus or the income therefrom which will or may reasonably be expected to take effect in possession or enjoyment within ten years.

Section 677(b) of the Code provides, in part, that the income of a trust shall not be considered taxable to the grantor under section 677(a), or any other provision of the chapter (chapter 1 of the Code), merely because such income in the discretion of another person, the trustee or the grantor acting as trustee, may be applied or distributed for the support or maintenance of a beneficiary whom the grantor is legally obligated to support or maintain, except to the extent that such income is so applied or distributed.

Based on the foregoing, it is held that the grantor does not have a "reversionary interest" in the above-described trust, within the meaning of section 673 of the Code, merely because trust corpus or income, in the discretion of a corporate trustee, may be used for the support of the grantor's minor child. Accordingly, income from the trust is not taxable to the grantor, under subpart E, subchapter J, chapter 1, subtitle A of the Code, except to the extent actually used for the support and maintenance of the minor child. To the extent that income is so used, the amount thereof is includible in the gross income of the grantor under section 677(b) of the Code, even though he does not have a reversionary interest in the trust within the meaning of section 673 of the Code.

Whether the taxpayer is entitled to deductions for the so-called charitable charges placed upon the trust in 1959 and 1960 is determined under the provisions of section 170 of the Code, which relates to the deduction of charitable contributions.

Section 170(b)(1)(D) of the Code provides, in part, that no charitable deduction may be taken for the value of any interest in property transferred in trust if the settlor has a reversionary interest in the corpus on income which exceeds five percent of the value of the property.

Section 1.170-2(d) of the Income Tax Regulations provides, in part, as follows:

> For purposes of this paragraph, the term "reversionary interest" means a *possibility* that after the possession or enjoyment of property or its income has been obtained by a charitable donee, the property or its income may revest in the grantor or his estate, or may be subject to a power exercisable by the grantor *or a nonadverse party* (within the meaning of section 672(b)), or both, to revest in, or return to or *for the benefit of*, the grantor or his estate the property or income therefrom. * * *. (Italics supplied.)

The trust instrument does not by its terms set up two separate trusts, one a trust with charitable purposes and one a noncharitable trust. No property or fund, and neither any definite interest in any particular property or fund, is dedicated solely to charitable purposes. Moreover, the corporate trustee, a nonadverse party, has the discre-

tionary power to pay trust income or corpus for the use of the grantor's minor child. Because of the grantor's legal obligation to support his child, there is a possibility that corpus or income may be used for the "benefit of the grantor" as those words are used in the provisions of the regulation quoted above.

The definition of a "reversionary interest" for purposes of section 170(b)(1)(D) of the Code is independent of that term as used in section 673 of the Code. Also, under the provisions of section 677(b) of the Code, income of a trust of this type must actually be used to discharge the grantor's obligations in order to be taxable to the grantor. However, under section 170(b)(1)(D) of the Code, it is enough if the property or income can be used for the benefit of the grantor.

Based upon the above-stated facts, it is held that the grantor has a "reversionary interest" in the instant trust, as that term is used in section 170(b)(1)(D) of the Code, since there is a possibility that corpus or income in excess of the 5 percent referred to in section 170(b)(1)(D)(ii) of the Code may be used for the "benefit of the grantor" in supporting the minor child. Therefore, no deduction is allowable to the grantor for the contributions made to the trust in 1959 and 1960 in the form of so-called charitable charges placed upon the trust.

SECTION 674.—POWER TO CONTROL BENEFICIAL ENJOYMENT

26 CFR 1.674(a)-1: Power to control beneficial enjoyment; scope of section 674.

An investment trust established under New York State law by banks as grantors. See Rev. Rul. 61-175, page 128.

SECTION 677.—INCOME FOR BENEFIT OF GRANTOR

26 CFR 1.677(a)-1: Income for benefit of grantor; general rule. Rev. Rul. 61-175
(Also Sections 674, 7701; 1.674(a)-1, 301.7701-4.)

> Upon the creation of an investment trust under the New York Banking Law, in which each of the several grantor banks reserves an income interest in proportion to its contribution, each grantor bank is treated as the owner of its portion of the trust and all income, deductions and credits attributable thereto are treated as those of the bank.

Advice has been requested whether, in the case of a trust established under New York State law by several savings banks as their medium for certain security transactions, the grantor banks should take as their own the deductions attributable to the trust.

The banks entered into a trust agreement with a trust company in order to fulfill the requirements of section 235(20) of the New York Banking Law, Volume 4, McKinney's Consolidated Laws of New York, Annotated, enabling banks to invest in certain federally guaranteed securities, mortgages, and deeds of trust. Under the pro-

visions of the trust instrument, the trustee acquired as part of the trust corpus certain mortgages and issued certificates of participating interest to each grantor bank.

The trustee cannot vary the investment portfolio of the trust. Therefore, the trust is not considered an association taxable as a corporation. See section 7701(a)(3) of the Internal Revenue Code of 1954 and section 301.7701–4(c) of the Regulations on Procedure and Administration.

The interests in the income of the trust, including capital gains, have been reserved to the grantors in proportion to their respective contributions. Therefore, under the provisions of section 677(a) of the Code, each grantor bank is to be treated as the owner of an aliquot portion of the trust. In addition, each grantor bank is to be so treated under the provisions of section 674(a) of the Code because the beneficial enjoyment of the corpus and the income therefrom is subject to a power of disposition in each bank as to its proportionate interest, by reason of a power to assign which is expressly reserved in the governing instrument and also by reason of the rule of New York State law that grantors cannot create a spendthrift trust with respect to reserved interests, but necessarily retain a power to convey them or to cause them to be reached by persons to whom they are under legal obligation. See section 34 of the New York Personal Property Law, Volume 40, McKinney's Consolidated Laws of New York, Annotated, and *Newton* v. *Hunt et al.*, 119 N.Y. Supp. 3, affirmed, 95 N.E. 1134.

Since each bank is an owner of a portion of the trust, it is held that all income, deductions and credits attributable thereto are to be treated as those of that bank, under section 671 of the Code.

Any income which is taxable to the certificate holders under section 671 of the Code should not be reported on the Form 1041, but such income and the amounts of deductions and credits applicable thereto should be shown in a separate statement to be attached to the Form 1041. See section 1.671–4 of the Income Tax Regulations.

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26 CFR 1.677(b)–1: Trusts for support.

Application of section 677(b) of the Code, where income or corpus may be used for child support and the grantor of the trust does not have a reversionary interest in the trust under section 673 of the Code. See Rev. Rul. 61–223, page 125.

SUBCHAPTER K.—PARTNERS AND PARTNERSHIPS

PART I.—DETERMINATION OF TAX LIABILITY

SECTION 702.—INCOME AND CREDITS OF PARTNER

26 CFR 1.702–1: Income and credits of partner.

Trust or estate as member of a partnership. See Rev. Rul. 61–211, page 124.

SUBCHAPTER L.—INSURANCE COMPANIES

PART I.—LIFE INSURANCE COMPANIES

Subpart E.—Miscellaneous Provisions

SECTION 819.—FOREIGN LIFE INSURANCE COMPANIES

26 CFR 1.819–2: Foreign life insurance companies.

Percentage for purposes of declaration of estimated income tax by foreign life insurance companies for the taxable year 1961. See T.D. 6567, page 547.

PART III.—OTHER INSURANCE COMPANIES

SECTION 832.—INSURANCE COMPANY TAXABLE INCOME

26 CFR 1.832–1: Gross income. Rev. Rul. 61–167

Reserves for "fidelity and surety losses incurred but not reported" which are required by the United States Department of the Treasury to be maintained by companies transacting fidelity and surety business on Government contracts are not deductible either as "losses incurred" or "unearned premiums," in determining insurance company taxable income under section 832 of the Internal Revenue Code of 1954.

Advice has been requested whether reserves for "fidelity and surety losses incurred but not reported" which are required by the United States Department of the Treasury to be maintained by companies writing fidelity and surety bonds in connection with United States Government contracts are deductible by such companies either as "losses incurred" or as "unearned premiums," in determining insurance company taxable income under section 832 of the Internal Revenue Code of 1954.

The taxpayer is a fidelity and surety company engaged in writing surety bonds on United States Government contracts and is taxable under section 831 of the Code as an insurance company (other than life or mutual).

Under Treasury Department regulations, all companies transacting fidelity and surety business on contracts in favor of the United States are required to file complete annual financial reports with the Department. These reports are to be made on forms approved by the National Convention of Insurance Commissioners. The Treasury Department regulations also provide that such companies are required to maintain reserves for losses incurred but not reported with respect to fidelity and surety bonds. These reserves consist of specified portions of a company's net fidelity and surety premiums in force on the closing date applicable to the annual financial statement and are based on a prescribed percentage rate determined with reference to the number of years which a company has transacted fidelity and surety business.

In the Underwriting and Investment Exhibit of the insurance Convention Statement, filed with the taxpayer's return, the above-mentioned "reserve for losses incurred but not reported" is included in, and treated as a part of, the deduction claimed for "losses incurred."

Section 832(b)(1) of the Code, in defining taxable income of certain insurance companies, provides, in part, that gross income earned from investment income and underwriting income is computed on the basis of the underwriting and investment exhibit of the annual statement approved by the National Convention of Insurance Commissioners.

The taxpayer contends that the amounts placed in the reserve by him are properly deductible under section 832 of the Code as "losses incurred," since the maintenance of the reserve is required by the Treasury Department and such amounts are included as a part of the deduction claimed for "losses incurred" in the underwriting and investment exhibit of the financial statement approved by the National Convention of Insurance Commissioners.

In determining allowable deductions under section 832 of the Code, section 832(c) provides, in part, that a deduction shall be allowed for "losses incurred" as defined in section 832(b)(5) of the Code, which provides as follows:

> (5) LOSSES INCURRED.—The term "losses incurred" means losses incurred during the taxable year on insurance contracts, computed as follows:
>
> (A) To losses paid during the taxable year, add salvage and reinsurance recoverable outstanding at the end of the preceding taxable year and deduct salvage and reinsurance recoverable outstanding at the end of the taxable year.
>
> (B) To the result so obtained, add all unpaid losses outstanding at the end of the taxable year and deduct unpaid losses outstanding at the end of the preceding taxable year.

Section 1.832–1 of the Income Tax Regulations provides, in part, that in computing "losses incurred" the determination of unpaid losses at the close of each year must represent actual unpaid losses stated in amounts which, based upon the facts in each case and the company's experience with similar cases, can be said to represent a fair and reasonable estimate of the amount the company will be required to pay.

The District Director of Internal Revenue may require every insurance company to which section 832 of the Code applies to submit such detailed information with respect to its actual experience as is deemed necessary to establish the reasonableness of the deduction for "losses incurred."

Section 832(b) of the Code provides, in part, that the term "gross income," in the case of an insurance company subject to the tax imposed by section 831, means the sum of the combined amount earned during the taxable year from investment income and from underwriting income computed on the basis of the underwriting and investment exhibit of the annual statement approved by the National Convention of Insurance Commissioners.

However, it has long been the position of the Internal Revenue Service that the Convention Form is to be used only as a general guide in computing the gross income of an insurance company other than life or mutual. See *Pacific Employers Insurance Co.* v. *Commissioner*, 89 Fed. (2d) 186, Ct. D. 1268, C.B. 1937–2, 312; *Commissioner* v.

United States Guarantee Co., 190 Fed. (2d) 152; and Rev. Rul. 60–306, C.B. 1960–2, 211.

In addition, section 1.832–1(a) of the regulations provides, in part, that the underwriting and investment exhibit is presumed to reflect the true net income of the company and, insofar as it is not inconsistent with the provisions of the Internal Revenue Code of 1954, it will be recognized and used as a basis for that purpose.

Therefore, the deductibility of amounts as "losses incurred" is contingent upon compliance with the provisions of section 832 of the Code and the regulations thereunder. Those provisions do not provide for the deduction of reserves for unpaid losses, but, instead, provide that the part of the deduction for losses incurred which represents unpaid losses at the close of the taxable year comprise only "actual unpaid losses" which, based on the facts of each case and the company's experience in similar cases, can be said to represent a fair and reasonable estimate of the amount the company will be required to pay. The fact that the maintenance of a particular reserve may be required by the Treasury Department and that such reserve is included in and is a part of the deduction claimed as "losses incurred" on the underwriting and investment exhibit of the annual statement approved by the National Convention of Insurance Commissioners does not qualify such a reserve as deductible "losses incurred" for Federal income tax purposes in the absence of compliance with the provisions of section 832 of the Code and the regulations thereunder.

The reserve maintained by the taxpayer in this case does not comprise actual losses which, based on the facts of each case and the company's experience in similar cases, can be said to represent a fair and reasonable estimate of the amount the company will be required to pay but, in fact, constitutes a contingency reserve, computed on the basis of a percentage rate established by the Treasury Department, which the taxpayer is required to maintain as a condition of writing surety bonds on United States Government contracts.

With respect to whether the reserve constitutes "unearned premiums" deductible under section 832(b)(4) of the Code, it may be stated that such term is generally defined to mean that portion of net premiums which the insurance company has not yet had time to earn or, more precisely, that portion of the premiums paid by the policyholder which must be returned to him on cancellation of the policy, and which is in direct proportion to the unexpired term which the policy has to run. See Rev. Rul. 55–693, C.B. 1955–2, 284.

In some instances, amounts required by a state statute to be placed in reserve have been recognized as having all of the attributes that pertain to "unearned premiums" and have been treated as such for income tax purposes, which such amounts were (1) withdrawn by statute from the use of the company for its general purposes, (2) impressed with a trust in favor of contract holders until the risk was carried for the definite period provided by the statute, and (3) available for reinsurance of the contract in the event the company became insolvent or were to be returned to the contract holder if not used for such purpose. See *Early, Jr.* v. *Lawyers Title Insurance Corporation*, 132 Fed. (2d) 42; I.T. 3798, C.B. 1946–1, 127; and Rev. Rul. 57–48, C.B. 1957–1, 212.

In view of the foregoing, the reserve maintained by the taxpayer in this case does not qualify as "unearned premiums" since such reserve

is lacking in the recognized attributes appertaining to "unearned premiums."

Accordingly, it is held that reserves for "fidelity and surety losses incurred but not reported," which are required by the Treasury Department to be maintained by companies transacting fidelity and surety business on Government contracts, are not deductible for Federal income tax purposes, under section 832 of the Code, either as "losses incurred" or as "unearned premiums."

SUBCHAPTER N.—TAX BASED ON INCOME FROM SOURCES WITHIN OR WITHOUT THE UNITED STATES

PART I.—DETERMINATION OF SOURCES OF INCOME

SECTION 862.—INCOME FROM SOURCES WITHOUT THE UNITED STATES

26 CFR 1.862–1: Income specifically from sources without the United States. (Also Sections 921, 931; 1.921–1, 1.931.1.)

Rev. Rul. 61–195 [1]

Certain Western Hemisphere trade corporations and foreign corporations are placing their marine insurance on goods exported from this country with foreign insurance underwriters and others are placing their marine insurance on goods imported to this country with foreign underwriters because of fear that the Internal Revenue Service might consider either the domicil of the insurance underwriter or the place of execution of the insurance contract in determining the source of the income derived from the sale of the goods.

Revenue Ruling 60–278, C.B. 1960–2, 214, holds that when insured goods are lost in transit the residence status (domestic or foreign) of the insurance company is wholly immaterial to the determination of the source of gain from insurance proceeds received as a result of the loss because the situs of the property at the time of the loss determines the source of the gain.

The situs of the goods in transit is determined under the general principle of law that goods remain at their original situs until they have acquired a permanent situs elsewhere.

The source of income from the purchase and sale of personal property is determined under sections 861 through 864 of the Internal Revenue Code of 1954 and the regulations thereunder.

The Service will not consider either the choice of underwriter or the place of execution of a marine insurance contract in determining where the property is sold or the source of the income derived from the sale. A taxpayer will not be considered as engaged in trade or business in a country merely by virtue of the fact that it has placed its marine insurance with an underwriter located in that country or has executed the insurance contract there.

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[1] Based on Technical Information Release 335, dated September 18, 1961.

PART III.—INCOME FROM SOURCES WITHOUT THE UNITED STATES

Subpart C.—Western Hemisphere Trade Corporations

SECTION 921.—DEFINITION OF WESTERN HEMISPHERE TRADE CORPORATIONS

26 CFR 1.921–1: Definition of Western Hemisphere trade corporation.

Whether the choice of an underwriter or the place of execution of a marine insurance contract affects the determination of where the property is sold or the source of the income derived from the sale. See Rev. Rul. 61–195, page 133.

Subpart D.—Possessions of the United States

SECTION 931.—INCOME FROM SOURCES WITHIN POSSESSIONS OF THE UNITED STATES

26 CFR 1.931–1: Citizens of the United States and domestic corporations deriving income from sources within a certain possession of the United States.

Whether the choice of an underwriter or the place of execution of a marine insurance contract affects the determination of where the property is sold or the source of the income derived from the sale. See Rev. Rul. 61–195, page 133.

SUBCHAPTER O.—GAIN OR LOSS ON DISPOSITION OF PROPERTY

PART III.—COMMON NONTAXABLE EXCHANGES

SECTION 1031.—EXCHANGE OF PROPERTY HELD FOR PRODUCTIVE USE OR INVESTMENT

26 CFR 1.1031(d)–1: Property acquired upon a tax-free exchange.

Basis of United States obligations acquired in a tax-free exchange for United States obligations and cash. See Rev. Rul. 61–138, page 136.

SECTION 1033.—INVOLUNTARY CONVERSIONS

26 CFR 1.1033(e)–1: Destruction or disposition of livestock because of disease. Rev. Rul. 61–216
(Also Sections 165, 1231; 1.165–6, 1.1231–1.)

Losses due to the death of livestock from disease, whether or not of epidemic proportions, come within the provisions of section 1033(e) of the Internal Revenue Code of 1954 and will be treated as resulting from an involuntary conversion under section 1231(a) of

the Code, as amended by section 49(a) of the Technical Amendments Act of 1958.

Death of livestock from disease is not considered to be a casualty as that term is used in sections 165(c)(3) and 1231(a) of the Code, as amended. Losses sustained, by reason of the death of livestock from disease, are not among those losses excepted from the application of the provisions of section 1231(a) of the Code.

A series of questions has been presented to the Internal Revenue Service regarding the treatment, for Federal income tax purposes, of losses due to the death of livestock from disease in view of section 1033(e) of the Internal Revenue Code of 1954 and section 1231(a) of the Code as amended by section 49(a) of the Technical Amendments Act of 1958, 26 U.S.C. 1231, C.B.1958–3, 254, at 290.

Section 1033(a) of the Code provides for the nonrecognition of gain resulting from certain involuntary conversions of property into money or other property under prescribed conditions. Under section 1033(e) of the Code, if livestock are destroyed by or on account of disease, or are sold or exchanged because of disease, such destruction or such sale or exchange shall be treated as an involuntary conversion.

Section 1231(a) of the Code provides that if, during the taxable year, the recognized gains on sales or exchanges of property used in the trade or business, plus the recognized gains from the compulsory or involuntary conversion of property used in the trade or business and capital assets held for more than six months into other property or money, exceed the recognized losses from such sales, exchanges, and conversions, such gains and losses shall be considered as gains and losses from sales or exchanges of capital assets held for more than six months. If such gains do not exceed such losses, such gains and losses shall not be considered as gains and losses from sales or exchanges of capital assets.

Section 49(a) of the Technical Amendments Act of 1958, *supra*, amended section 1231(a) of the Code to provide, in the case of any property used in the trade or business and of any capital asset held for more than six months and held for the production of income, that that section would not apply to any loss in respect of which the taxpayer is not compensated for by insurance in any amount, arising from fire, storm, shipwreck, or other casualty, or from theft.

The questions presented relative to the treatment of losses due to the death of livestock from disease, together with the answers thereto, are as follows:

Question 1. Is the treatment provided by section 1231(a) of the Code applicable to a loss caused by the death of livestock from disease?

Answer. Section 1033(e) of the Code provides that the destruction, sale or exchange of livestock because of disease is to be treated as an involuntary conversion to which section 1033 of the Code applies. While section 1033 of the Code does not by its terms deal specially with *losses* resulting from the death of diseased livestock, such destruction, sale or exchange does constitute an involuntary conversion for purposes of section 1231(a) of the Code. See section 1.1033(e)–1(c) of the Income Tax Regulations. Accordingly, the treatment provided by section 1231(a) of the Code is applicable in appropriate cases to a loss caused by the death of livestock from disease, assuming such diseased livestock are property used in the trade or business or capital assets held for more than six months.

Question 2. Does normal death loss from a disease in a herd constitute destruction by disease within the meaning of section 1033(e) of the Code, when the disease is not of a nature which would spread quickly and disastrously through a herd?

Answer. Section 1033(e) of the Code and the pertinent Income Tax Regulations make no distinction between the types of prevalency of diseases to be considered as falling within section 1033(a) of the Code. Therefore, whether there is normal death loss from disease in a herd or whether the disease reaches epidemic proportions, loss resulting therefrom will fall within the provisions of section 1033(e) of the Code as a loss resulting from an involuntary conversion subject to the treatment afforded such losses by section 1231(a) of the Code.

Question 3. Are losses caused by the destruction of livestock by or on account of disease, and treated as losses from involuntary conversion for purposes of section 1231(a) of the Code, also to be treated as losses specifically excluded from the tax treatment of section 1231(a) of the Code by the last sentence thereof as losses arising from "other casualty?"

Answer. Losses due to the death of livestock from a "casualty," within the meaning of that term as used in the last sentence of section 1231(a) of the Code, are specifically excluded from the tax treatment prescribed by section 1231(a) of the Code even though such losses result from an "involuntary conversion" for purposes of that section. The term "other casualty" as used in both section 165(c)(3) and section 1231(a) of the Code, as amended, denotes a loss arising from a cause analogous to a fire, storm, or shipwreck and embraces losses arising suddenly or unexpectedly. Although such "suddenness" test need not be satisfied in order to have a particular occurrence constitute a "destruction" for purposes of the involuntary conversion provisions of section 1033 and 1231(a) of the Code, provided the causes of destruction otherwise fall within the general concept of a casualty, "suddenness" is an essential element of a "casualty" for purposes of section 165(c)(3) of the Code and for purposes of determining those losses which are excepted by the last sentence of section 1231(a) of the Code from treatment under that section of the Code. See Revenue Ruling 59–102, C.B. 1959–1, 200, and the cases cited therein and S. Report No. 1983, 85th Cong., C.B. 1959–3, 922, at 995. Therefore, since disease generally does not qualify under the "suddenness" test as a casualty, losses due to the death of livestock from disease ordinarily are not casualty losses within the meaning of section 1231(a) of the Code and are not entitled to the treatment afforded casualty losses under section 165(c)(3) of the Code.

SECTION 1037.—CERTAIN EXCHANGES OF UNITED STATES OBLIGATIONS

(Also Sections 451, 1031; 26 CFR 1.451–2, 1.1031(d)–1.) Rev. Rul. 61–138

Under the provisions of section 1037(a) of the Internal Revenue Code of 1954, no gain or loss will be recognized upon the exchange of 2⅝ percent Treasury Notes of Series A–1963 due February 15, 1963, or 2¼ percent Treasury Bonds of 1959–62 due June 15, 1962,

solely for 3⅝ percent Treasury Bonds of 1967 issued at par, or upon the exchange of the 2¼ percent Treasury Bonds of 1959–62 due December 15, 1962, solely for the 3⅝ percent Treasury Bonds of 1967 issued at 100.30 percent of their face value.

The 3⅝ percent Treasury Bonds of 1967 which were offered by the Secretary of the Treasury in Treasury Department Circular No. 1059, dated March 20, 1961, 26 F.R. 2530, were issued in exchange (1) at par for 2⅝ percent Treasury Notes of Series A–1963, dated April 15, 1958, due February 15, 1963; (2) at par for 2¼ percent Treasury Bonds of 1959–62, dated June 1, 1945, due June 15, 1962; or (3) at 100.30 percent of their face value for 2¼ percent Treasury Bonds of 1959–62, dated November 15, 1945, due December 15, 1962.

The income derived from the bonds is subject to all taxes imposed under the Internal Revenue Code of 1954. The bonds are subject to estate, inheritance, gift or other excise taxes, whether Federal or State, but are 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. The bonds will be acceptable to secure deposits of public moneys. They will not be acceptable in payment of taxes.

Under the authority of section 1037(a) of the Code, the Secretary of the Treasury has declared that no gain or loss shall be recognized, for Federal income tax purposes, upon the exchange with the United States of the 2⅝ percent Treasury Notes of Series A–1963 due February 15, 1963, or the 2¼ percent Treasury Bonds of 1959–62 due June 15, 1962, solely for the 3⅝ percent Treasury Bonds of 1967 issued at par, or upon the exchange of the 2¼ percent Treasury Bonds of 1959–62 due December 15, 1962, solely for the 3⅝ percent Treasury Bonds of 1967 issued at 100.30 percent of their face value. D.C. No. 1059.

Gain or loss, if any, upon the obligations surrendered in exchange will be taken into account upon the disposition or redemption of the new obligations.

Treasury Department Circular No. 1059 provides that accrued interest from December 15, 1960, to March 15, 1961, in the amount of $5.56319 per $1,000, on the 2¼ percent Treasury Bonds of 1959–62 due December 15, 1962, will be credited; the payment of $3.00 per $1,000 due to the United States will be charged; and the difference of $2.56319 per $1,000 will be paid to subscribers. The full amount of this interest, $5.56319 per $1,000, is constructively received by taxpayers on the cash receipts and disbursements method of accounting and includible in their gross income, in the taxable year in which so credited. Accrual method taxpayers will report the interest of $5.56319 per $1,000 ratably for the taxable period in which earned. The basis of the new bonds issued at 100.30 percent of their face value will be the basis of the old bonds due December 15, 1962, increased by $3.00 per $1,000.

SUBCHAPTER P.—CAPITAL GAINS AND LOSSES

PART IV.—SPECIAL RULES FOR DETERMINING CAPITAL GAINS AND LOSSES

SECTION 1231.—PROPERTY USED IN THE TRADE OR BUSINESS AND INVOLUNTARY CONVERSIONS

26 CFR 1.1231–1: Gains and losses from the sale or exchanges of certain property used in the trade or business.

Losses due to the death of livestock from disease. See Rev. Rul. 61–216, page 134.

SUBCHAPTER S.—ELECTION OF CERTAIN SMALL BUSINESS CORPORATIONS AS TO TAXABLE STATUS

SECTION 1372.—ELECTION BY SMALL BUSINESS CORPORATION

26 CFR 1.1372–3: Shareholders' consent.

Requests for extension of time for filing consent by new shareholders or a husband or wife who has failed to file a timely consent. See Rev. Proc. 61–30, page 568.

CHAPTER 2.—TAX ON SELF-EMPLOYMENT INCOME

SECTION 1402.—DEFINITIONS

Certain remuneration of lay missionaries erroneously reported as net earnings from self-employment. See Rev. Proc. 61–19, page 551.

Certificate filed by fiduciaries or survivors on or before April 15, 1962. See Rev. Proc. 61–35, page 574.

26 CFR 1.1402(c)–1: Trade or business.

Status, for Federal employment tax purposes, of registered and practical nurses. See Rev. Rul. 61–196, page 155.

26 CFR 1.1402(e)–1: Election by ministers, members of religious orders, and Christian Science practitioners for self-employment coverage. Rev. Rul. 61–187 [1]

After June 30, 1961, a minister, a member of a religious order, or a Christian Science practitioner may not withdraw a waiver certificate on Form 2031 which was filed in order to elect social security coverage as a self-employed individual.

[1] Based on News Release IR–385, dated June 30, 1961.

After June 30, 1961, ministers, members of religious orders, and Christian Science practitioners will not be permitted to withdraw a Waiver Certificate, Form 2031, filed for the purpose of electing social security coverage and paying the self-employment tax as if self-employed.

In a few instances certificates have been withdrawn after they were filed with the Internal Revenue Service. This was permitted if a written request for withdrawal was made on or before the due date for filing the individual's income tax return for the first taxable year for which the certificate was effective.

Under existing law a certificate on Form 2031 is always effective for the taxable year immediately *preceding* the earliest taxable year for which the due date for filing the individual's income tax return has not expired. Consequently, when a certificate is now filed, the due date for filing the individual's income tax return, for the first taxable year for which the certificate is effective, has already expired. The principle under which certificates were withdrawn in the past no longer can be applied, particularly in view of the section of the law which provides that an effective certificate is irrevocable.

A revision of the applicable regulations is in course of preparation and will be issued at the earliest practicable date.

CHAPTER 3.—WITHHOLDING OF TAX ON NONRESIDENT ALIENS AND FOREIGN CORPORATIONS AND TAX-FREE COVENANT BONDS

SUBCHAPTER A.—NONRESIDENT ALIENS AND FOREIGN CORPORATIONS

SECTION 1442.—WITHHOLDING OF TAX ON FOREIGN CORPORATIONS

26 CFR 1.1442–1: Withholding of tax on foreign corporations.

The general and withholding regulations under the tax convention between the United States and Canada amended to reflect the increase in rate of tax with respect to dividends paid by related corporations after December 20, 1960. See T.D. 6576, page 289.

SUBCHAPTER C.—APPLICATION OF WITHHOLDING PROVISIONS

SECTION 1464.—REFUNDS AND CREDITS WITH RESPECT TO WITHHELD TAX

26 CFR 1.1464–1: Refunds and credits. Rev. Rul. 61–207

Where a withholding agent has withheld income tax in excess of the correct amount required under chapter 3 of the Internal Revenue Code of 1954 and has reported and paid the entire amount of such tax to the Internal Revenue Service, the refund or credit of the overpayment is required to be claimed by and made to the

taxpayer from whose income the amount of such tax was withheld, even though the withholding agent has reimbursed the taxpayer for the amount of the excess tax withheld.
Revenue Ruling 57–567, C.B. 1957–2, 609, distinguished.

Advice has been requested whether income tax in excess of the correct amount required to be withheld under chapter 3 of the Internal Revenue Code of 1954 and paid to the Internal Revenue Service may be refunded to the withholding agent where the agent has reimbursed the taxpayer for the amount of the excess tax withheld.

Section 1441 of the Code requires generally that all persons having the control, receipt, custody, disposal, or payment of interest, dividends, rents, salaries, wages, premiums, annuities, compensations, remunerations, emoluments, or other fixed or determinable annual or periodical gains, profits, and income, etc., of any nonresident alien individual, or of any partnership not engaged in trade or business within the United States and composed in whole or in part of nonresident aliens, shall deduct and withhold from such items a tax equal to 30 percent thereof.

Section 1442 of the Code contains a similar provision with respect to foreign corporations subject to tax and not engaged in trade or business within the United States.

Illustrative of the circumstances under which excess tax may be withheld are the following examples:

1. A withholding agent withholds $30 from $100 of dividend income of a nonresident alien who is a resident of a foreign country with which the United States has established an income tax treaty. The balance of $70 is remitted to the alien. The withholding agent reports the withheld amount on a return Form 1042, U.S. Annual Return of Income Tax To Be Paid At Source, and pays the withheld tax to the Internal Revenue Service. Subsequently, the agent is informed by the alien that because he is a resident in a treaty country, only $15 should have been withheld. The withholding agent then reimburses the alien for the $15 withheld in excess of the applicable treaty rate and files a claim with the Internal Revenue Service for a refund of $15.

2. A United States citizen residing in a foreign country furnishes a written statement to the withholding agent that he is a United States citizen. Subsequently, tax is withheld from dividend income of the United States citizen. The agent reports the withheld amount on a return, Form 1042, and pays the tax to the Internal Revenue Service. The citizen then informs the withholding agent of the erroneous withholding. The agent reimburses the citizen for the amount erroneously withheld and files a claim for refund of that amount.

3. In this example the facts are the same as in example 2 except that the written statement of United States citizenship was not furnished to the withholding agent until after the withheld tax was reported on a return, Form 1042, and paid to the Internal Revenue Service.

Section 1.1464–1 of the Income Tax Regulations provides specifically that the refund or credit of an overpayment of tax which has actually been withheld at the source under chapter 3 of the Code shall

be made to the taxpayer from whose income the amount of such tax was in fact withheld.

In each of the examples set forth above, the income involved is dividend income that is owned by the nonresident alien or the United States citizen and from which the withholding agent has withheld the overpaid tax under chapter 3 of the Code. Since the amount of the overpaid tax was actually withheld from income belonging to the nonresident alien or citizen of the United States, and was reported as withheld and paid to the Internal Revenue Service, the refund or credit of the overpayment is required to be made to such alien or citizen in accordance with the terms of the regulations.

Revenue Ruling 57–567, C.B. 1957–2, 609, involved withholding of tax from a dividend payment made to a nonresident alien who, because he had sold his stock prior to the ex-dividend date, was not entitled to the dividend. Following the rules of the New York Stock Exchange, the purchaser of the stock, a United States resident, was reimbursed in the full amount of the dividend by the seller. Hence, the requirement of section 1.1464–1 of the Income Tax Regulations was not applicable since no tax was in fact withheld from the income of the taxpayer, the purchasing shareholder. Accordingly, under the circumstances described in Revenue Ruling 57–567, it was held that a refund of withheld tax may be made to the withholding agent where the tax has been withheld from a payment not constituting income in the hands of the recipient.

Under the facts of this case, it is held that where the withholding agent withheld income tax in excess of the correct amount required under chapter 3 of the Code and reported and paid the entire amount of such tax to the Internal Revenue Service, the refund or credit of the amount of the overpayment is required to be claimed by and made to the taxpayer from whose income the amount of such tax was withheld, even though the withholding agent has reimbursed the taxpayer for the amount of the excess tax withheld. See section 1.1464–1 of the regulations.

Revenue Ruling 57–567, C.B. 1957–2, 609, is distinguished.

CHAPTER 4.—RULES APPLICABLE TO RECOVERY OF EXCESSIVE PROFITS ON GOVERNMENT CONTRACTS

SUBCHAPTER A.—RECOVERY OF EXCESSIVE PROFITS ON GOVERNMENT CONTRACTS

SECTION 1471.—RECOVERY OF EXCESSIVE PROFITS ON GOVERNMENT CONTRACTS

26 CFR 1.1471–1: Recovery of excessive profits on government contracts. Rev. Rul. 61–122

The recodification of the profit-limiting provisions of the Vinson Act in 1956 in no way limits the operative effect of the provisions of the Renegotiation Act of 1951, as amended and extended, which renders the profit-limiting provisions of the Vinson Act inapplicable to prime contracts and subcontracts, the receipts or accruals under

which are subject to the Renegotiation Act or would be so subject except for the provisions of section 106(e) of that Act.

Where a prime contract is exempt from the profit-limiting provisions of the Vinson Act, prior to or subsequent to its recodification, by virtue of provisions of the Renegotiation Act, all subcontracts made under that prime contract are likewise exempt even though those subcontracts themselves are not subject to the Renegotiation Act. Therefore, no part of profits realized on such subcontracts is subject to recovery collection under section 1471 of the Internal Revenue Code of 1954.

Revenue Ruling 55–173, C.B. 1955–1, 104, modified.

Advice has been requested concerning the effect, if any, of the recodification of the profit-limiting provisions of the Vinson Act, 34 U.S.C. 496 and 10 U.S.C. 311, repealed and reenacted as sections 2382 and 7300 of Title 10 of the United States Code, and whether, under the circumstances described below, a subcontractor is subject to such profit-limiting provisions either prior to or subsequent to their recodification and, thus, subject to the excessive profits recovery provisions of section 1471 of the Internal Revenue Code of 1954.

The subcontracts in the instant case relate to certain standard commercial articles used in the production of naval aircraft and were entered into with a prime contractor who is subject to the Renegotiation Act of 1951, as amended and extended to June 30, 1962. See the Act of March 23, 1951, Public Law 9, 65 Stat. 7, C.B. 1951–1, 180; the Act of September 1, 1954, Public Law 764, 68 Stat. 1116, C.B. 1955–1, 620; the Act of August 3, 1955, Public Law 216, 69 Stat. 447, C.B. 1955–2, 754; the Act of August 1, 1956, Public Law 870, 70 Stat. 786, C.B. 1956–2, 1183; the Act of September 6, 1958, Public Law 85–930, 72 Stat. 1789; and the Act of July 13, 1959, Public Law 86–89, 73 Stat. 210, C.B. 1959–2, 680, all at 50 U.S.C. App. 1211–1233. The subcontracts were performed and completed during the taxable years 1953 to 1958, inclusive. If the profit-limiting provisions of the Vinson Act are applicable in the instant case, a portion of the profits realized would be subject to collection by the Government as excessive profits under section 1471 of the Code.

As originally enacted, the Vinson Act imposed certain profit limitations on contracts for the construction or manufacture of any naval vessel, army or navy aircraft, or any portion thereof. Section 3(b) of the Vinson Act provided, in part, that no contract shall be entered into unless the contractor agreed to repay all profits realized on such contract in excess of a specified percentage of the total contract price and further agreed to make no subcontract unless the subcontractor agreed to the same profit-limiting provisions.

The Vinson Act was repealed in 1956 by section 53 of the Act of August 10, 1956, Public Law 1028, 84th Cong., 70A Stat. 641. However, its profit-limiting provisions were reenacted and recodified at that time as sections 2382 and 7300 of Title 10 of the United States Code. As reenacted, these provisions cover contracts for the construction or manufacture of military aircraft and naval vessels or any part thereof. In this regard, section 50 of the Act of August 10, 1956, provides as follows:

If on the effective date of this Act a provision of law that is restated in this Act and repealed by section 53 would have been in a suspended or temporarily superseded status but for its repeal, the provisions of this Act that restate that provision have the same suspended or temporarily superseded status.

The Renegotiation Act of 1951, *supra*, provides for renegotiation on account of excessive profits realized on contracts entered into with specified governmental departments and for such renegotiation of subcontracts made with respect to such contracts. However, section 106(e) of that Act as set forth in the Act of August 1, 1956, *supra*, 50 U.S.C. 1216(e), exempts contracts and subcontracts for standard commercial articles and services from coverage.

Due to the overlapping coverage of the Vinson Act, section 102(d), the predecessor of the present section 102(e) of the Renegotiation Act, as enacted in 1951 and extended to 1955, provided, in part, that the profit-limiting provisions of the Vinson Act (referred to by that section as the Act of March 27, 1934, 48 Stat. 503, 505, as amended and supplemented) do not apply to any contract or subcontract, the receipts or accruals of which are subject to the provisions of the Renegotiation Act. In 1955, section 102(d) (now section 102(e)) of the Renegotiation Act was amended by the Act of August 3, 1955, *supra*, to provide that the Vinson Act shall not apply to contracts or subcontracts which would be subject to the Renegotiation Act except for the provisions of section 106(a)(8), which was the predecessor of section 106(e) of that Act, relating to the exemption for standard commercial articles or services. This amendment applies to amounts received or accrued after December 31, 1953, under such contracts or subcontracts. The section, which appears at 50 U.S.C. 1212(e), has been extended for the years subsequent to the recodification of the profit-limiting provisions of the Vinson Act.

For the period after 1953, by virtue of the amendment made by the Act of August 3, 1955, profits realized on contracts for standard commercial articles, as provided in that Act, are not subject to the profit-limiting provisions of the Vinson Act. The repeal and recodification of these provisions as section 2382 and section 7300 of Title 10 of the United States Code in no way limited the effect of section 102(e) of the Renegotiation Act to render the provisions inoperative.

For the year 1953, the profit-limiting provisions of the Vinson Act are also inapplicable in the instant case. These provisions only apply to subcontracts where the prime contract is subject to the same provisions. If a prime contract is not subject to the profit-limiting provisions of the Vinson Act, all subcontracts made thereunder are also not subject to those provisions. See *Aluminum Company of America* v. *Commissioner*, 23 T.C. 189, acquiescence, C.B. 1956–1, 3, and Revenue Ruling 56–282, C.B. 1956–1, 701. In the instant case the prime contract is subject to the Renegotiation Act and, therefore, is not subject to the profit-limiting provisions of the Vinson Act.

Accordingly, it is held that in the instant case no part of the profits realized on the subcontracts in question is subject to recovery collection under section 1471 of the Code.

Revenue Ruling 55–173, C.B. 1955–1, 104, holds, *inter alia*, that the profit-limiting provisions of the Vinson Act apply to contracts and subcontracts otherwise subject to those provisions, if they are exempted from renegotiation under section 106(a)(8) of the Renegotiation Act of 1951, as amended to the date of promulgation of that ruling, or are otherwise not subject to renegotiation. As noted above, however, the Act of August 3, 1955, *supra*, amended section 102(d)

of such Renegotiation Act to provide specifically that, as to amounts received or accrued after December 31, 1953, the contract or subcontract would still be exempt from those provisions in such case in the same manner as if the Renegotiation Act had applied to those amounts. Thus, Revenue Ruling 55–173 is modified to the extent that it is inconsistent with the Act of August 3, 1955.

Revenue Ruling 55–173 also indicated that the Renegotiation Act of 1951, as amended to the date of promulgation of that ruling, effected exemption of a subcontract from the profit-limiting provisions of the Vinson Act only in those situations where the subcontract itself was subject to renegotiation under the terms of such Renegotiation Act. However, in the *Aluminum Company* case, *supra*, the Tax Court of the United States held that where a prime contract was exempt under Subchapter E of Chapter 2 of the Internal Revenue Code of 1939 from the profit-limiting provisions of the Vinson Act because entered into in a taxable year to which the excess profits tax applied, subcontracts under such prime contract were also exempt even though entered into in a year of the subcontractor to which the excess profits tax did not apply. The court stated that the applicability to the subcontract of the profit-limiting provisions of the Vinson Act, by the terms of that Act, depended upon whether they applied to the prime contract.

The holding in the *Aluminum Company* case and its reasoning were followed in Revenue Ruling 56–282, *supra*. Accordingly, the portion of Revenue Ruling 55–173 dealing with the applicability of profit-limiting provisions of the Vinson Act to amounts received or accrued under subcontracts not themselves subject to renegotiation is modified to conform to Revenue Ruling 56–282 and the instant revenue ruling in cases where the prime contract is subject to renegotiation under the Renegotiation Act of 1951, as amended, or (as to amounts received or accrued after December 31, 1953) is exempt from renegotiation under section 106(e) or the earlier corresponding section 106(a)(8) of that Act.

CHAPTER 6.—CONSOLIDATED RETURNS

SUBCHAPTER A.—RETURNS AND PAYMENT OF TAX

SECTION 1502.—REGULATIONS

26 CFR 1.1502–13: Changes in affiliated group during taxable year.

Treatment of consolidated net operating loss of an affiliated group filing a consolidated return upon termination of the affiliation. See Rev. Rul. 61–224, page 145.

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26 CFR 1.1502–30: Computation of tax.

The treatment of a consolidated return in which a Western Hemisphere trade corporation had a net loss. See Rev. Rul. 61–143, page 146.

26 CFR 1.1502–31: Bases of tax computation. Rev. Rul. 61–224
(Also Section 172; 1.172–1, 1.1502–13.)

Where an affiliated group of corporations filing consolidated returns is terminated prior to the close of a taxable year, a consolidated net operating loss carryover attributable to all the members of the group shall be applied in full against the consolidated income reported on the group's final consolidated income tax return, even though that income is attributable entirely to operations of the parent corporation.

Advice has been requested regarding the treatment to be accorded the consolidated net operating loss carryover of a group of affiliated corporations which is terminated prior to the close of the taxable year where the income reported on the group's final consolidated income tax return is attributable entirely to operations of the parent corporation.

The *M* corporation was the common parent of an affiliated group of corporations which filed consolidated income tax returns on the calendar-year basis for the years 1952 through 1956. Each of the corporations in the group sustained net operating losses during some or all of these years, and on December 31, 1956, the affiliated group had a consolidated net operating loss carryover. On March 1, 1957, the *N* corporation, a corporation not previously connected with the group, purchased all the stock of the *M* corporation and did not elect to file a consolidated return.

During the taxable year 1957 the *M* corporation had taxable income while its subsidiaries, for the period up to the March 1, 1957, termination, had losses. Thus, without taking into account any consolidated net operating loss carryover, the final consolidated return of the group would reflect taxable income all of which was attributable to the *M* corporation.

The specific question on which advice has been requested is whether, under the facts presented, the entire amount of the consolidated net operating loss carryover of the affiliated group is available as a deduction in computing the consolidated taxable income of the group for the taxable year 1957, or whether only that portion of the consolidated net operating loss carryover which is attributable to the *M* corporation is so available.

Section 1.1502–11(d) of the Income Tax Regulations provides, in part, that an affiliated group of corporations shall be considered as terminated if, as here, the common parent corporation ceases to be the common parent. Where there has been a complete termination of an affiliated group prior to the close of the taxable year of the group, section 1.1502–13(c) of the regulations provides that the consolidated return must include the income of the common parent corporation for its entire taxable year (excluding any portion of such year during which its income is included in the consolidated return of another affiliated group) and of each subsidiary for the period prior to the termination.

In Revenue Ruling 58–329, C.B. 1958–1, 337, the stock of a subsidiary corporation which was a member of an affiliated group filing consolidated returns was sold prior to the close of a taxable year of the group and a separate return was filed by the subsidiary for the short period following the sale. It was held that a consolidated net operating loss carryover incurred during the period of affiliation at-

tributable to the subsidiary whose stock was sold shall be carried over first to the consolidated return of the affiliated group for the taxable year in which its stock was sold, and any amount thereof not absorbed in such consolidated return which is still available for carryover is then to be carried over to the separate return of the subsidiary for the short period following the sale of its stock.

In other words, there is no requirement that a consolidated net operating loss incurred by the members of the affiliated group during a period of affiliation for which consolidated returns were filed shall be applied as a carryover to the subsequent consolidated return of the group in proportion to the respective income of each of the members of the group included therein. Accordingly, the consolidated net operating loss carryover attributable to all the members of the group shall be applied first against the consolidated income reported on the final consolidated return of the group without regard to the facts that the subsidiaries to which the loss carryover is attributable were not included in the final consolidated return for the entire taxable year and that they reported losses, rather than income, for the portion thereof before termination of the affiliated group.

In view of the foregoing, it is held that where an affiliated group of corporations filing consolidated returns is terminated during a taxable year and the group files a final consolidated return for that year, the consolidated net operating loss carryover attributable to all the members of the group shall be applied in full against the consolidated income for the taxable year of termination, even though that income is attributable entirely to operations of the parent corporation.

SECTION 1503.—COMPUTATION AND PAYMENT OF TAX

26 CFR 1.1503–1: Computation and payment of tax. Rev. Rul. 61–143

(Also Section 1502; 1.1502–30.)

> Where an affiliated group of corporations contains two regulated public utilities, each having taxable income for the taxable year, and a Western Hemisphere trade corporation having a net loss for that year, the net loss of the Western Hemisphere trade corporation must be subtracted from the total taxable income of the two regulated public utilities in computing the portion, if any, of the consolidated taxable income of the entire affiliated group which is to be excluded therefrom in determining the amount of consolidated taxable income that is subject to the additional tax of two percent imposed by section 1503(a) of the Internal Revenue Code of 1954.

Advice has been requested whether, upon making a consolidated income tax return of an affiliated group of corporations, a net loss of a Western Hemisphere trade corporation, included therein, should be subtracted from the total taxable income of two regulated public utilities, also included therein, in computing the portion, if any, of the consolidated taxable income of the entire affiliated group that is not subject to the additional two percent tax imposed by section 1503(a) of the Internal Revenue Code of 1954.

A parent corporation and its 20 subsidiaries were privileged to file a consolidated income tax return for the current taxable year. The consolidated return included taxable income of two regulated public

utilities totaling $15x$ dollars and a net loss of a Western Hemisphere trade corporation of $2x$ dollars. The entire affiliated group reported consolidated taxable income of $63x$ dollars which included, in addition to the consolidated taxable income of $13x$ dollars of the regulated public utilities and the Western Hemisphere trade corporation, $50x$ dollars consolidated taxable income of the 18 other corporations included in the affiliated group.

Section 1503(b) of the Code provides that if the affiliated group includes one or more Western Hemisphere trade corporations or one or more regulated public utilities, the increase of 2 percent provided in section 1503(a) shall be applied only on the amount by which the consolidated taxable income of the affiliated group exceeds the portion, *if any*, of the consolidated taxable income attributable to the Western Hemisphere trade corporations *and* regulated public utilities included in such group.

Section 1.1503–1(b) of the Income Tax Regulations provides that if the affiliated group includes one or more Western Hemisphere trade corporations or one or more regulated public utilities, the increase in tax described in section 1503(a) shall be applied in a manner provided in the regulations under section 1502.

Section 1.1502–30(b)(1) of the regulations provides that if the affiliated group filing a consolidated return includes a Western Hemisphere trade corporation *or* a regulated public utility, the increase of 2 percent, provided in section 1503(a) of the Code, in the corporation surtax rate shall be applied only on that portion of the consolidated taxable income attributable to the members of the group other than the Western Hemisphere trade corporation *or* the regulated public utility without any increase with respect to any partially tax exempt interest of such Western Hemisphere trade corporation or such regulated public utility. Inasmuch as such regulation merely relates to a case where a Western Hemisphere trade corporation *or* a regulated public utility is included in the affiliated group, it has no decisive bearing on the issue considered in the instant case where a Western Hemisphere trade corporation *and* two regulated public utilities are included in the affiliated group involved.

In Senate Report No. 2375, 81st Cong., 2nd Sess., C.B. 1950–2, 483, at 535, relating to the amendment of section 141(c) of the 1939 Code (the predecessor of section 1503 of the 1954 Code) by section 121(f) of the Revenue Act of 1950, it is stated:

> Subsection (f) of section 121, for which there is no corresponding provision in the bill as passed by the House, amends section 141(c) (relating to computation and payment of tax on consolidated returns) to provide that in the case of an affiliated group of corporations including one or more Western Hemisphere trade corporations filing a consolidated return the 2 percent additional tax shall be applied on the amount by which the consolidated corporation surtax net income of the affiliated group exceeds the portion of the consolidated corporation surtax net income attributable to the Western Hemisphere trade corporations. If the consolidated corporation surtax net income of the Western Hemisphere trade corporations is less than zero, the 2 percent additional tax shall be applied against the consolidated corporation surtax net income of the entire affiliated group, including the Western Hemisphere trade corporations.

Thus, under section 141(c) of the 1939 Code, the consolidated *net income, if any*, of Western Hemisphere trade corporations included in the consolidated net income of an affiliated group was excluded for the purposes of the two percent additional tax. However, if the

Western Hemisphere trade corporations included in the affiliated group had a consolidated *net loss*, such consolidated net loss was not excluded in the determination of the consolidated net income subject to the 2 percent additional tax. Otherwise, a larger amount would be subject to such additional tax than is subject to the regular tax. Although the provisions of section 141(c) of the 1939 Code were broadened in section 1503 of the 1954 Code to include regulated public utilities, there is no indication in section 1503(b), or in the history of that legislation, of any different intent with respect to the treatment of consolidated net income, or consolidated net loss, of Western Hemisphere trade corporations *and* regulated public utilities included in affiliated groups filing consolidated returns.

Hence, if such a Western Hemisphere trade corporation has net income of $15x$ dollars and such a regulated public utility has a net loss of $5x$ dollars, the amount of their consolidated *net income* of $10x$ dollars is to be excluded from the consolidated net income of the entire affiliated group in determining the extent the latter is subject to the two percent additional tax; whereas, if they have *no* consolidated *net income*, or they have a consolidated *net loss*, there is no amount to be so excluded, for *no portion* of the consolidated net income of the entire affiliated group is attributable to them.

Applying the specific language of section 1503(b), *supra*, here pertinent, "the consolidated taxable income of the affiliated group" in the instant case is $63x$ dollars; "the portion (if any) of the consolidated taxable income attributable to the Western Hemisphere trade corporations and regulated public utilities included in such group" is $15x$ dollars minus $2x$ dollars, or $13x$ dollars; and "the amount by which" $63x$ dollars "exceeds" $13x$ dollars is $50x$ dollars, to which "the increase of 2 percent provided in subsection (a) shall be applied."

Accordingly, in the instant case, it is held that the net loss of the Western Hemisphere trade corporation ($2x$ dollars) must be subtracted from the total taxable income of the two regulated public utilities ($15x$ dollars) in computing the portion, if any, of the consolidated taxable income of the entire affiliated group which is to be excluded therefrom ($13x$ dollars) in determining the amount of consolidated taxable income that is subject to the additional two percent tax imposed by section 1503(a) of the Code.

SUBTITLE B.—ESTATE AND GIFT TAXES

CHAPTER 11.—ESTATE TAX

SUBCHAPTER A.—ESTATES OF CITIZENS OR RESIDENTS

PART II.—CREDITS AGAINST TAX

SECTION 2013.—CREDIT FOR TAX ON PRIOR TRANSFERS

26 CFR 20.2013–1: Credit for tax on prior transfers. Rev. Rul. 61–208

In computing the credit for tax on prior transfers under the "second limitation" of section 2013(c)(1) of the Internal Revenue

Code of 1954, the marital deduction and charitable deduction to be used in computing the tax described in subparagraph (A) of such section are the same as the respective amounts allowed as deductions in the final determination of the decedent's taxable estate.

Advice has been requested as to the method of computing the credit for tax on prior transfers where the amount of the marital deduction or charitable deduction depends on the amount of Federal estate tax due and the so-called "second limitation" of section 2013(c) of the Internal Revenue Code of 1954 applies.

Section 2013 of the Code provides, in general, that the estate of a decedent is allowed a credit for the estate tax paid on property transferred to the decedent from a transferor who died within ten years before, or within two years, after, the decedent's death. The amount of the credit which may be taken by the decedent's estate on the transferred property is subject to two limitations.

The "first limitation," section 2013(b), limits the amount of the credit which may be taken to that portion of the transferor's estate tax which is attributable to the property transferred to the decedent.

The "second limitation" is contained in section 2013(c)(1) of the Code, which provides as follows:

> The credit provided in this section shall not exceed the amount by which—
>
> (A) the estate tax imposed by section 2001 or section 2101 (after deducting the credits for State death taxes, gift tax, and foreign death taxes provided for in sections 2011, 2012, and 2014) computed without regard to this section, exceeds
>
> (B) such tax computed by excluding from the decedent's gross estate the value of such property transferred and, if applicable, by making the adjustment hereinafter indicated.
>
> If any deduction is otherwise allowable under section 2055 or section 2106(a)(2) (relating to charitable deduction) then, for the purpose of the computation indicated in subparagraph (B), the amount of such deduction shall be reduced by that part of such deduction which the value of such property transferred bears to the decedent's entire gross estate reduced by the deductions allowed under sections 2053 and 2054, or section 2106(a)(1) (relating to deduction for expenses, losses, etc.). * * *.

The same basic problem is presented whether the estate involves the marital or charitable deduction. The only difference is that the charitable deduction is not limited to a percentage of the adjusted gross estate. The method of handling the marital deduction 50-percent limitation is expressly treated in Revenue Ruling 60-161, C.B. 1960-1, 367.

The marital deduction and charitable deduction to be used in computing the tax described in subparagraph (A) of section 2013(c)(1) are the same as the respective amounts actually allowed as marital and charitable deductions in the final determination of the decedent's taxable estate. They (subject to the 50-percent limitation as to the amount of the marital deduction) are also the actual amounts which pass, after taxes, to the surviving spouse and to charity.

The amount of the charitable deduction which is referred to as "otherwise allowable" in subparagraph (B) of section 2013(c)(1) is the amount actually allowed as a charitable deduction in the final determination of the taxable estate, which, in turn, is the amount actually passing to charity, after payment of all death taxes chargeable to the charitable interest.

The manner (*i.e.*, by specific, general, or residuary bequest) in which the marital or charitable bequest is made is immaterial, except to the extent that the amount of the bequest allowable as a deduction is, by reason of the provisions of section 2056(b)(4)(A), section 2055(c), or section 2106(a)(2)(C), reduced by the amount of any death taxes actually payable out of such bequest. For example, it is immaterial whether charity receives (1) property worth $30*x* by specific bequest free of death taxes or (2) a residuary estate worth $40*x* which is subject to payment of $10*x* in Federal and State death taxes. In either case the amount of the "second limitation" will be the same.

The substance of this Revenue Ruling is reflected in new instructions for part II of Schedule R in the latest edition of the estate tax return, Form 706, revised July 1961.

Pursuant to authority contained in section 7805(b) of the Internal Revenue Code of 1954, this ruling will not be applied in the case of estate tax returns filed prior to November 27, 1961, nor in the case of those returns the statutory period for the filing of which, not including any extensions of time for filing granted pursuant to law, expires not later than December 27, 1961.

PART III.—GROSS ESTATE

SECTION 2032.—ALTERNATE VALUATION

26 CFR 20.2032–1: Alternate valuation. Rev. Rul. 61–128

Section 20.2032–1(b)(2) of the Estate Tax Regulations provides, in part, that if the alternate valuation method of valuing the gross estate is to be used, section 2032(c) of the Internal Revenue Code of 1954 requires that the executor must so elect on the estate tax return required under section 6018 of the Code. In the instant case, the executor failed to designate an election in the box in item 23 of the General Information on the estate tax return with respect to the alternate valuation. However, the values for the various items of property included in the gross estate were shown in the appropriate schedules under the column headed "Alternate Value." The computation of the tax and the taxable estate were based upon the values determined under the alternate valuation method. *Held*, whether an election has been made is to be determined from all the facts disclosed in the estate tax return filed. Accordingly, the alternate valuation provisions of section 2032 of the Code may be used by the executor under the above-stated facts.

SECTION 2041.—POWERS OF APPOINTMENT

26 CFR 20.2041–1: Powers of appointment; in general. Rev. Rul. 61–129 [1]

The Internal Revenue Service will follow the recent decision of the United States Court of Appeals for the Eighth Circuit in *United States* v. *Winifred H. Turner, Executrix*, filed March 8, 1961.

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[1] Based on Technical Information Release 320, dated June 1, 1961.

The Court of Appeals held that the decedent's husband had created for her a general power of appointment when he entered into an agreement with an insurance company in 1935, even though he retained the privilege of altering or revoking the agreement.

The Service had argued that, since the husband had such a privilege of revocation, the power in the wife was not created until the husband died in 1948 without exercising it.

Under the court's ruling, the insurance proceeds were not taxable as part of the decedent's gross estate, for the decedent died in 1955 without having exercised the power, and section 2041(a)(1) of the Internal Revenue Code of 1954 provides for inclusion of a general power of appointment created on or before October 21, 1942, only if such power was exercised under certain conditions.

The decision in the *Turner* case follows the holdings in (*United States* v. *Merchants National Bank of Mobile*, 261 Fed. (2d) 570 (1958); *United States* v. *Walter A. Hubner*, et al., 285 Fed. (2d) 29 (1960); *Arthur B. Hyman, et al.* v. *United States*, 187 Fed. Supp. 661 (1960); and *Estate of Ernestina Rosenthal, et al.* v. *Commissioner*, 34 T.C. 144 (1960).

Revenue Ruling 278, C.B. 1953–2, 267, will be revoked and consideration will be given to conforming section 20.2041–1(e) of the regulations to accord with the decision in the *Turner* case.

SECTION 2042.—PROCEEDS OF LIFE INSURANCE

26 CFR 20.2042–1: Proceeds of life insurance. Rev. Rul. 61–123

> Where an airline passenger, prior to his death in an airplane crash, purchased an accident insurance policy on his life, the proceeds of the policy are includible in his gross estate, even though as a practical matter it was impossible for him while the plane was in flight to exercise those incidents of ownership retained by him under the policy.

Advice has been requested whether the proceeds of an accident insurance policy are includible in the gross estate of the insured decedent who purchased the policy and shortly thereafter died in an airplane crash.

The decedent, prior to his death purchased an accident insurance policy at an airport terminal. After filling in the beneficiary designation, he mailed the policy insuring his life to the beneficiary and boarded the plane. Subsequently, the plane crashed and the insured was killed.

Among the provisions in the policy in question was one which reserved to the insured the right to change the beneficiary. Representatives for the insured's estate contend that the proceeds of the life insurance policy should not be included in his gross estate. They maintain that while the decedent was flying in the plane he was unable to change the beneficiary so that as a practical matter the insured retained no incidents of ownership at the time of his death.

Section 2042 of the Internal Revenue Code of 1954 provides in part:

The value of the gross estate shall include the value of all property—

* * * * * * *

(2) RECEIVABLE BY OTHER BENEFICIARIES.—To the extent of the amount receivable by all other beneficiaries as insurance under policies on the life of the decedent with respect to which the decedent possessed at his death any of the incidents of ownership, exercisable either alone or in conjunction with any other person. * * *

Section 20.2042–1(c)(2) of the Estate Tax Regulations provides, in part, that the term "incidents of ownership" includes the power to change the beneficiary, to surrender or cancel the policy, to assign the policy, to revoke an assignment, to pledge the policy for a loan, etc.

Under the provisions of the policy, the decedent was the only one who had control over the policy. By reason of his right to determine the ultimate beneficiary, he had the power at any time until his death to determine the ultimate distributee. Whether or not he could have exercised this right at any particular time is immaterial. All that is required by the statute and regulations thereunder is that, on the date of death, the decedent possessed any of the incidents of ownership, exercisable alone or in conjunction with any other person. For analogous situations see *Estate of Edward L. Hurd* v. *Commissioner*, 6 T.C. 819, affirmed, 160 Fed. (2d) 610; *Estate of Charles S. Inman* v. *Commissioner*, 18 T.C. 522, reversed on other grounds, 203 Fed. (2d) 679; and *Estate of Virginia H. West* v. *Commissioner*, 9 T.C. 736, affirmed, 173 Fed. (2d) 505.

In view of the foregoing, it is held that the decedent at his death possessed an incident of ownership within the meaning of section 2042(2) of the Code in the above mentioned insurance policy on his life. Accordingly, the proceeds of such policy are includible in his gross estate for Federal estate tax purposes.

SUBTITLE C.—EMPLOYMENT TAXES

CHAPTER 21.—FEDERAL INSURANCE CONTRIBUTIONS ACT

SUBCHAPTER C.—GENERAL PROVISIONS

SECTION 3121.—DEFINITIONS

26 CFR 31.3121(b)(8)–2: Services in employ of religious, charitable, educational, or certain other organizations exempt from income tax.

Certain remuneration of lay missionaries erroneously reported as net earnings from self-employment. See Rev. Proc. 61–19, page 551.

26 CFR 31.3121(d)–1: Who are employees. (Also Sections 3306, 3401; 31.3306(i)–1, 31.3401(c)–1.) Rev. Rul. 61–178

A physician maintains a private practice and also renders medical treatment to employees of a company on its premises on a part-time basis. He is required to conform to the company's policies and procedures, is subject to supervision by the company's head physician, works a regular fixed hour schedule six days a week, and is extended all the benefits and privileges of the company's regular employees, such as vacations, sick pay, etc. *Held*, the physician is an employee of the company for Federal employment tax purposes with respect to services performed therefor.

Rev. Rul. 84, C.B. 1953–1,404 distinguished.

Advice has been requested whether a physician performing medical services for an industrial corporation under the circumstances set forth herein is an employee for Federal employment tax purposes.

The physician in question performs medical services for the corporation on a part-time basis and also maintains an office for the conduct of his private practice. His duties for the corporation consist of examining and treating, including minor surgical operations, those company employees who are in need of medical attention. He works a regular two-hour schedule each day six days a week for the corporation, is subject to censure for any deviation from the schedule, and is on call at any time in case of an emergency at its plant. Further, he is not at liberty to respond to an emergency arising in his private practice during his working hours for the corporation. The physician performs his services on the corporation's premises and uses equipment and facilities furnished by the corporation. He is paid a monthly salary for his services, is given written and oral instructions in conformity with company policies and procedures, and is also given instructions by the corporation's head physician who is admittedly an employee of the corporation. In the event of a difference of opinion between the two physicians, final decisions and responsibilities rest with the head physician. The physician is required to submit written reports to the corporation relative to employee disabilities, progress, and final recovery. He is not permitted to engage assistants or to arrange for a substitute for himself in event of his inability to carry out his duties. Both the corporation and the physician retain the right to terminate the relationship at any time without either party incurring any liability for breach of contract. The corporation has extended to the physician all of the rights and benefits enjoyed by its employees, such as pensions, vacations, and sick pay.

Under section 3121(d)(2) of the Federal Insurance Contributions Act (chapter 21, subtitle C, Internal Revenue Code of 1954), the term "employee" means any individual who, under the usual common law rules applicable in determining the employer-employee relationship, has the status of an employee. Whether an individual is an employee under such rules depends upon the facts in each case. The guides for determining, under such rules, whether an employer-employee relationship exists, are found in section 31.3121(d)–1(c) of the Employment Tax Regulations.

Physicians who engage in the pursuit of an independent medical practice in which they offer their services to the public are generally

independent contractors and not employees. However, if the requisite control and supervision over a physician exist with respect to services performed for another, he is an employee rather than an independent contractor. Whether the requisite control and supervision exist is determined by the application of such factors as (1) the degree to which such individual has become integrated into the operating organization of the person or firm for which the services are performed; (2) the substantial nature, regularity, and continuity of his work for such person or firm; (3) the authority vested in or reserved by such person or firm to require compliance with its general policies; and (4) the degree to which the individual under consideration has been accorded the rights and privileges which such person or firm has created or established for its employees generally. These factors are emphasized in determining whether the requisite control exists because the high degree of skill required by a physician and the methods by which he works, being prescribed by the techniques and standards of his profession, make it difficult for the person or firm for which the services are performed to supervise him in the performance of his services.

Following the decision in *Willard Storage Battery Co.* v. *Carey*, 103 Fed. Supp. 7 (1952), the Service published Revenue Ruling 84, C.B. 1953–1, 404, which holds, in effect, that a physician engaged in the private practice of medicine, who also examines and treats company employees as a part-time service for the company, is not an employee of the company for Federal employment tax purposes. In the *Willard Storage Battery* Co. case, direct control and supervision were not contemplated by the company as to the details and means by which the physicians accomplished their work, and they were free to leave the company's premises during working hours if any emergency case in their private practice required their presence.

The facts in this case are distinguishable from those present in the *Willard Storage Battery Co.* case. Here the physician in question is integrated into the operating organization of the company; his services are of a substantial, regular and continuous nature; contemplation of an employer-employee relationship is evidenced by the extension of employee benefits and privileges to the physician by the company; and he is subject to the supervision of the company's head physician, an acknowledged employee, as to the manner in which his services are to be performed. See *Wendell E. James* v. *Commissioner*, 25 T.C. 1296 (1956), wherein the Tax Court of the United States held that a physician was an employee of a hospital, stating, at page 1301:

> * * * the control of an employer over the manner in which professional employees shall conduct the duties of their positions must necessarily be more tenuous and general than the control over nonprofessional employees. Yet, despite this absence of direct control over the manner in which professional men shall conduct their professional duties, it cannot be doubted that many professional men are employees. * * *

Accordingly, it is held under the facts in the instant case that the physician, with respect to the services he performs for the company on a part-time basis, is an employee for purposes of the taxes imposed under the Federal Insurance Contributions Act, the Federal Unemployment Tax Act, and for purposes of the Collection of In-

come Tax at Source on Wages (chapters 21, 23 and 24, respectively, subtitle C, Internal Revenue Code of 1954).

Revenue Ruling 84, C.B. 1953–1, 404, is hereby distinguished.

(Also Sections 1402, 3306, 3401; 1.1402(c)–1, 31.3306(i)–1, 31.3401(c)–1.) Rev. Rul. 61–196

Whether a nurse is self-employed or an employee depends upon the facts and circumstances of the case. Generally, licensed practical nurses and registered nurses engaged in private duty nursing are considered to be self-employed. However, when such nurses are on the regular staff of a hospital, clinic, nursing home, physician, etc., work for a salary and follow prescribed routines during fixed hours when not available for private duty nursing, they are employees. Mim. 6658 C.B. 1951–2, 168, superseded.

Reconsideration has been given to Mimeograph 6658, C.B. 1951–2, 168, which sets forth the position of the Internal Revenue Service with respect to the status of nurses for purposes of the Federal Insurance Contributions Act, the Federal Unemployment Tax Act, and the Collection of Income Tax at Source on Wages (chapters 21, 23, and 24, respectively, subtitle C, Internal Revenue Code of 1954).

Registered Nurses

(a) *Independent contractor.*—Registered nurses are skilled professionals who have been trained to render technical assistance in administering medications and treatment to the sick, wounded, or enfeebled. Although some of their duties may be domestic in nature, such duties are usually incidental to their regular professional duties. Registered nurses, by reason of their professional status, generally are independent contractors in the performance of private duty nursing services. They hold themselves out to the public as exercising an independent calling requiring specialized skills. Ordinarily, they have full discretion in administering their professional services and are not subject to sufficient direction or control to warrant the finding of an employment relationship, even though they may be subject to the supervision of the attending physician. Under such circumstances they are independent contractors and not employees for Federal employment tax purposes.

(b) *Employment relationship.*—Hospitals, clinics, nursing homes, public health agencies, etc., engage registered nurses on a full-time basis as a part of their regular staffs. Some physicians engage them as office attendants in connection with their private practice. The nurses work for a salary and follow prescribed routines during fixed hours. Although their duties are professional in nature, these nurses lose their individuality by integrating their services into the employer's business and by the employer's right to set the order of and supervise their services. These nurses are subject to the direction and control of the institution, agency, physician, etc., and are employees in every sense of the word.

Practical Nurses

In the past several years the status of practical nurses as a group has undergone a change from one of a practically domestic role to

that of a qualified semi-professional. Almost uniform statutes now in force in all fifty states require that before qualifying as a licensed practical nurse an individual must successfully complete a prescribed course of formal training and pass the state's licensing examination. By reason of these training and licensing requirements, the nursing and medical professions generally recognize licensed practical nurses as being qualified to render nursing services in all but the most acute or complex cases.

As is true in the case of registered nurses, licensed practical nurses are frequently engaged by hospitals, clinics, nursing homes, etc., on their regular staffs. In these situations the licensed practical nurses work for a salary, follow prescribed routines during fixed hours, and are otherwise subject to the direction and control of the institutions, etc., engaging them. Consequently, they are employees for Federal employment tax purposes.

Licensed practical nurses who perform private-duty nursing, as in the case of registered nurses, ordinarily have discretion in performing their nursing services. Although there may be situations where they follow the instructions of an attending physician or registered nurse, they are for the most part not subject to supervision or control by the person for whom they are rendering services. Thus, in private-duty nursing, licensed practical nurses usually perform their services under the same general conditions as registered nurses and, therefore, are ordinarily independent contractors and not employees for Federal employment tax purposes when performing services under such circumstances.

The conclusion in the preceding paragraph has no application to a licensed practical nurse who is engaged primarily to perform services of a household nature as distinguished from services involving the care of a private patient since under these circumstances she would be performing services as an employee for Federal employment tax purposes.

As in all situations where a determination as to the existence of either an employer-employee or independent contractor relationship is required, the complete factual data and all circumstances must be considered. The pertinent factors which must be considered are (a) the type and nature of the services performed; (b) the control exercised and by whom; (c) whether the individual is a licensed nurse; and (d) evidence establishing whether or not the services were performed in the conduct of an independent trade, business, or profession.

Nurses' aides, domestics, and other unlicensed individuals who continue to classify themselves as practical nurses are, in general, insufficiently trained or equipped to render professional or semi-professional services according to the professional concept of "nursing." Their services are normally those expected of maids and servants, i.e., bathing the individual, combing the individual's hair, reading, arranging bedding and clothing, preparing and serving meals, and occasionally giving oral medication left in their custody. As these and similar tasks are normally performed by domestics, the individuals performing them are, like other domestics, subject to virtually complete direction and control in the performance of the services regardless of whether they work for a medical institution, physician,

or in a private household and, therefore, are employees for Federal employment tax purposes.

The Self-Employment Contributions Act of 1954 (chapter 2, subtitle A, Internal Revenue Code of 1954) imposes for each taxable year a tax on the self-employment income of every individual. Thus, it may be stated that generally if a nurse is not an employee for Federal employment tax purposes the provisions of the Self-Employment Contributions Act may be applicable. Therefore, determinations whether tax liability may be incurred under that Act should be made with due regard to the applicable income tax provisions of the Code since an individual's status as a self-employed individual is initially dependent upon whether he is engaged in a trade or business. Doubtful cases should be submitted to the Internal Revenue Service for specific rulings.

Mim. 6658, C.B. 1951–2, 168, is hereby superseded.

CHAPTER 22.—RAILROAD RETIREMENT TAX ACT

SUBCHAPTER A.—TAX ON EMPLOYEES

SECTION 3201.—RATE OF TAX

26 CFR 31.3201–1: Measure of employee tax.

Instructions for computation of tax to be reported with respect to compensation paid after 1961 for services rendered after 1936 and before June 1, 1959. See Rev. Proc. 61–20, page 553.

SUBCHAPTER B.—TAX ON EMPLOYEE REPRESENTATIVES

SECTION 3211.—RATE OF TAX

26 CFR 31.3211–1: Measure of employee representative tax.

Instructions for computation of tax to be reported with respect to compensation paid after 1961 for services rendered after 1936 and before June 1, 1959. See Rev. Proc. 61–20, page 553.

SUBCHAPTER C.—TAX ON EMPLOYERS

SECTION 3221.—RATE OF TAX

26 CFR 31.3221–1: Measure of employer tax.

Instructions for computation of tax to be reported with respect to compensation paid after 1961 for services rendered after 1936 and before June 1, 1959. See Rev. Proc. 61–20, page 553.

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CHAPTER 23.—FEDERAL UNEMPLOYMENT TAX ACT

SECTION 3306.—DEFINITIONS

26 CFR 31.3306(i)–1: Who are employees.

Physician with a regular practice engaged by a company on a part-time basis. See Rev. Rul. 61–178, page 153.

Status, for Federal employment tax purposes, of registered and practical nurses. See Rev. Rul. 61–196, page 155.

CHAPTER 24.—COLLECTION OF INCOME TAX AT SOURCE ON WAGES

SECTION 3401.—DEFINITIONS

26 CFR 31.3401(c)–1: Employee.

Physician with a regular practice engaged by a company on a part-time basis. See Rev. Rul. 61–178, page 153.

Status, for Federal employment tax purposes, of registered and practical nurses. See Rev. Rul. 61–196, page 155.

SUBTITLE D.—MISCELLANEOUS EXCISE TAXES

CHAPTER 31.—RETAILERS EXCISE TAXES

SUBCHAPTER D.—LUGGAGE, HANDBAGS, ETC.

SECTION 4031.—IMPOSITION OF TAX

26 CFR 48.4031–1: Imposition of tax. Rev. Rul. 61–124

The retailers excise tax on luggage, handbags, etc., imposed by section 4031 of the Internal Revenue Code of 1954, does not apply to school bags which are especially designed for use by school children in carrying books, pencils, and other supplies to and from school and which, by reason of special features of design and construction, are distinguishable from "briefcases," "brief bags," and "ring binders, capable of closure on all sides."

The Internal Revenue Service has been asked whether the retailers excise tax on luggage, handbags, etc., applies to the school bags which are described below.

A retailer sells various types of school bags for use in carrying books and other school supplies. One type of bag is approximately 9½ inches by 14 inches by 3½ inches in size, is equipped with a plastic handle, and has a flap with a closure of the strap and buckle type.

The bag also has an open-face pocket for holding identification cards, and two outside compartments. One of the outside compartments has a closure of the strap and buckle type and is intended for use in carrying lunches, whereas the other compartment, which has a zipper closure, is designed for holding pens, pencils, and other school supplies. The bag is made of fabric material.

The retailer also sells other types of bags which vary in size from about 9½ inches by 13½ inches by 3½ inches to approximately 11 inches by 14 inches by 4¾ inches. These bags have many of the features of the type of bag described above. However, in addition, several of these bags have pictures of comic book, television, and story book characters imprinted on the outside of the bags or on the pockets. Most of these bags are made of rayon, plastic, or vinyl-coated materials of various colors.

Section 4031 of the Internal Revenue Code of 1954, as amended by the Excise Tax Technical Changes Act of 1958, Public Law 85–859, C.B. 1958–3, 92, imposes a tax upon certain articles, by whatever name called, sold at retail. Such articles include "briefcases," "brief bags," and "ring binders, capable of closure on all sides."

Section 48.4031–1(b)(2) of the Manufacturers and Retailers Excise Tax Regulations provides that the term "briefcases" includes, for purposes of the tax imposed by section 4031, articles commonly or commercially known and sold as such regardless of materials from which made or the purpose for which they are to be used. The term also includes so-called "portfolios," "envelopes," etc., capable of being closed on all four sides which are designed and constructed for carrying or conveying unfolded legal-size or letter-size papers, documents, etc. The term does not include "portfolios," "envelopes," etc., designed and constructed primarily for storage purposes.

Revenue Ruling 58–375, C.B. 1958–2, 752, which was based on the provisions of section 4031 of the Code prior to its amendment by the Excise Tax Technical Changes Act of 1958, holds that a bag (even though sold for use in carrying books and other school supplies) which is made of leather and equipped with handles for carrying, straps for closure purposes, but having no partitions, pockets, or zippers falls within the meaning of the term "brief cases made of leather or imitation leather" as used in section 4031 of the Code prior to its amendment.

Revenue Ruling 59–4, C.B. 1959–1, 295, sets forth a list of articles subject to the retailers excise tax and a list of articles not subject to the tax, under the provisions of section 4031, as amended by the Excise Tax Technical Changes Act of 1958. Included among the nontaxable articles are "school bags (not otherwise taxable as briefcases, brief bags, or ring binders)."

Bags, with or without partitions, which are especially designed for use by school children in carrying books, pencils, pens, and other supplies to and from school are not subject to the tax imposed by section 4031 of the Code, whether sold before or after the effective date of the Excise Tax Technical Changes Act of 1958. Such bags are generally distinguishable from "briefcases" by reason of special features of design and construction, such as, a lunch pocket, a name plate

holder, a pencil compartment on the outside of the case, comic or other fictional characters imprinted on or attached thereto, and plaid, pastel, or other colorful fabrics and bindings. The foregoing is not intended to be all-inclusive, but merely illustrative of the factors to be considered in determining the classification for tax purposes of the articles in question. The presence or absence of any one of these factors will not be a conclusive test.

The bags sold by the retailer in the instant case are considered to be especially designed for use by school children in carrying books, pencils, and other supplies to and from school and are not considered to be briefcases, brief bags, or ring binders, capable of closure on all sides, within the meaning of section 4031 of the Code. Accordingly, it is held that the tax imposed by that section does not apply to sales of those school bags.

Rev. Rul. 61–135

Certain portfolios or "pouches," are made of a heat resisting aluminized fabric lined with asbestos. They are recommended for use in the home and office as a protection for money, jewelry, valuable papers, etc., against destruction by fire. They have snap closure protective flaps and are offered in four standard sizes, varying from four inches by six inches to 12 inches by 14 inches. *Held*, such portfolios or pouches are not subject to the retailers excise tax imposed by section 4031 of the Internal Revenue Code of 1954.

Advice has been requested whether the retailers excise tax imposed on the sale of luggage, handbags, etc., by section 4031 of the Internal Revenue Code of 1954 applies to the sale of certain portfolios, or "pouches," which are described below.

The pouches in question are made of a heat resisting aluminized fabric lined with asbestos. They are recommended for use in the home and office as a protection for money, jewelry, valuable papers, etc., against destruction by fire. They have snap closure protective flaps and are offered in four standard sizes, varying from four inches by six inches to 12 inches by 14 inches.

Section 4031 of the Code imposes a tax on certain enumerated articles, by whatever name called, when sold at retail. Among the enumerated articles are "briefcases."

Section 48.4031–1(b)(2) of the Manufacturers and Retailers Excise Tax Regulations provides that the term "briefcases" includes so-called "portfolios," "envelopes," etc., capable of being closed on all four sides which are designed and constructed for carrying or conveying unfolded legal-size or letter-size papers, documents, etc., but that it does not include "portfolios," "envelopes," etc., designed and constructed primarily for storage purposes.

It is held that the pouches described are not "briefcases," as that term is used in section 4031, because they are designed and constructed primarily for storage purposes. Furthermore, such pouches do not fall within the classification of any of the other articles enumerated in section 4031. Accordingly, sales of such pouches are not subject to the retailers excise tax imposed by that section of the Code.

Rev. Rul. 61–204

The retailers excise tax on luggage, handbags, etc., imposed by section 4031 of the Internal Revenue Code of 1954, applies to sales at retail of "kits" which contain the major components from which taxable articles may be assembled without the performance of substantial or significant operations other than assembly.

Advice has been requested concerning the applicability of the retailers excise tax on luggage, handbags, etc., to the retail sales of certain so-called "kits," which are described below.

Section 4031 of the Internal Revenue Code of 1954 imposes a tax upon certain articles, by whatever name called, sold at retail. Included in the enumeration of taxable articles are billfolds, card and pass cases, key cases or containers, pocketbooks, purses and handbags, and wallets.

A company sells at retail numerous types of leathercraft "kits." These "kits" contain in precut but unassembled condition all of the major components of one or another of the articles enumerated in section 4031 of the Code, together with instructions for easy assembly. In some cases the "kits" contain instructions for the optional tooling of decorative designs. In some of the "kits" the precut leather components are prepunched for easy lacing, while in others there are instructions for the punching of the holes, which is to be done by the person who assembles the article. Some "kits" contain lacing, cement, coatings, bleaches, etc., but others do not.

After completing the assembly of the leather articles, the assembler ordinarily applies a leather "finisher" which contains certain ingredients which soften and waterproof the leather and tend to prevent the soiling of the articles. This "finishing" process consists of applying the liquid "finisher" in much the same manner as is used in applying liquid shoe polish.

The retailers excise taxes, as well as the manufacturers excise taxes, are imposed upon a wide variety of *articles*, which are enumerated in the statute either specifically or by class. These articles are no less taxable merely because in some instances they may be sold as "kits" in unassembled or "knockdown" condition. For example, see Revenue Ruling 55–125, C.B. 1955–1, 518, which relates to articles of jewelry sold in unassembled condition; Revenue Ruling 58–38, C.B. 1958–1, 376, which includes perfume ingredient "kits"; Revenue Ruling 167, C.B. 1953–2, 428, and Revenue Ruling 56–307, C.B. 1956–2, 808, which relate to radio receiving sets; Revenue Ruling 54–320, C.B. 1954–2, 411, which relates to table tennis tables; Revenue Ruling 56–306, C.B. 1956–2, 793, which relates to dry charge batteries; Revenue Ruling 57–496, C.B. 1957–2, 726, which relates to power lawn mowers; and Revenue Ruling 58–376, C.B. 1958–2, 810, which relates to ball point pens. See also the decision of the United States Court of Claims in the case of *George A. Hine* v. *United States*, 113 F. Supp. 340 (1953), which relates to sales of fishing rod "kits."

The same basic rationale which underlies the conclusions cited above applies to sales in unassembled condition of any of the articles subject to the retailers excise tax on luggage, handbags, etc. Therefore, the tax imposed by section 4031 of the Code applies to sales at retail of "kits" which contain the major components from which taxable articles may be assembled without the performance of sub-

stantial or significant operations other than assembly. On the other hand, the tax imposed by section 4031 of the Code does not apply to the sale of leather or other *materials* and *supplies* from which a taxable article may be produced only by the performance of substantial or significant cutting, shaping, or other operations in addition to assembly.

Whether a particular "kit" is taxable or nontaxable depends upon all of the facts relating to that "kit." However, there are set forth below some of the criteria which must be taken into account.

Lacing, cement, and similar assembly materials are not considered to be major components; therefore, the absence of such materials does not, of itself, make a "kit" nontaxable. The "finishing" process described above is not considered to be a substantial or significant operation; therefore, a "kit" which otherwise would be considered taxable is not made nontaxable because such "finishing" is recommended or required. The punching of holes in the leather components for the purpose of lacing them together is not considered to be a substantial or significant operation; therefore, the fact that such holes must be punched by the person who assembles the components does not preclude the taxability of the "kit." With respect to "kits" which contain the major components from which taxable articles may be assembled without the performance of substantial or significant operations other than assembly, the taxability of the articles is not affected by the fact that decorative tooling may be recommended to enhance the ornamental value of the assembled articles.

Accordingly, it is held that the retailers excise tax imposed by section 4031 of the Code applies to the sale at retail of the leathercraft "kits" described in the instant case.

SUBCHAPTER E.—SPECIAL FUELS

SECTION 4041.—IMPOSITION OF TAX

26 CFR 48.4041: Statutory provisions; imposition of tax. T.D.6574[1]

(Also Section 4071, 4081, 4222, 4261, 6421; 48.4071, 48.4081, 148.1–3, 49.4261, 48.6421 (c)–1.)

TITLE 26—INTERNAL REVENUE.—CHAPTER I, SUBCHAPTER D

PART 48.—MANUFACTURERS AND RETAILERS EXCISE TAXES

PART 49.—FACILITIES AND SERVICES EXCISE TAXES

PART 148.—CERTAIN EXCISE TAX MATTERS UNDER THE EXCISE TAX TECHNICAL CHANGES ACT OF 1958

Miscellaneous amendments to various excise tax regulations.

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

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

The Manufacturers and Retailers Excise Tax Regulations (26 CFR Part 48), the Facilities and Services Excise Tax Regulations

[1] 26 F.R. 9575.

(26 CFR Part 49), and the regulations in Part 148, Certain Excise Tax Matters Under the Excise Tax Technical Changes Act of 1958 (26 CFR Part 148), are amended in order to conform these regulations with the appropriate sections of the Federal-Aid Highway Act of 1961 (75 Stat. 122) [P.L. 87-61, page 309, this Bulletin] and the Tax Rate Extension Act of 1961 (75 Stat. 193) [P.L. 87-72, page 317, this Bulletin]. The Manufacturers and Retailers Excise Tax Regulations are also amended to eliminate the requirement that a claim in respect of gasoline used for nonhighway or local transit purposes shall include a statement as to the vendors of the gasoline and the total number of gallons of gasoline purchased from each vendor. These amendments of the regulations are as follows:

MANUFACTURERS AND RETAILERS EXCISE TAXES
(26 CFR Part 48)

PARAGRAPH 1. Section 48.4041 is amended by revising section 4041 (a), (b), and (c) and the historical note, and by deleting section 4041 (f). Section 4041 (a), (b), and (c) in § 48.4041 and the historical note, as so amended, read as follows:

§ 48.4041 STATUTORY PROVISIONS; IMPOSITION OF TAX.

SEC. 4041. IMPOSITION OF TAX.

(a) DIESEL FUEL.—There is hereby imposed a tax of 4 cents a gallon upon any liquid (other than any product taxable under section 4081)—

(1) Sold by any person to an owner, lessee, or other operator of a diesel-powered highway vehicle, for use as a fuel in such vehicle; or

(2) Used by any person as a fuel in a diesel-powered highway vehicle unless there was a taxable sale of such liquid under paragraph (1).

In the case of a liquid taxable under this subsection sold for use or used as a fuel in a diesel-powered highway vehicle (A) which (at the time of such sale or use) is not registered, and is not required to be registered, for highway use under the laws of any State or foreign country, or (B) which, in the case of a diesel-powered highway vehicle owned by the United States, is not used on the highway, the tax imposed by paragraph (1) or by paragraph (2) shall be 2 cents a gallon. If a liquid on which tax was imposed by paragraph (1) at the rate of 2 cents a gallon by reason of the preceding sentence is used as a fuel in a diesel-powered highway vehicle (A) which (at the time of such use) is registered, or is required to be registered, for highway use under the laws of any State or foreign country, or (B) which, in the case of a diesel-powered highway vehicle owned by the United States, is used on the highway, a tax of 2 cents a gallon shall be imposed under paragraph (2).

(b) SPECIAL MOTOR FUELS.—There is hereby imposed a tax of 4 cents a gallon upon benzol, benzene, naphtha, liquefied petroleum gas, or any other liquid (other than kerosene, gas oil, or fuel oil, or any product taxable under section 4081 or subsection (a) of this section)—

(1) Sold by any person to an owner, lessee, or other operator of a motor vehicle, motorboat, or airplane for use as a fuel for the propulsion of such motor vehicle, motorboat, or airplane; or

(2) Used by any person as a fuel for the propulsion of a motor vehicle, motorboat, or airplane unless there was a taxable sale of such liquid under paragraph (1).

In the case of a liquid taxable under this subsection sold for use or used otherwise than as a fuel for the propulsion of a highway vehicle (A) which (at the time of such sale or use) is registered, or is required to be registered, for highway use under the laws of any State or foreign country, or (B) which, in the case of a highway vehicle owned by the

United States, is used on the highway, the tax imposed by paragraph (1) or by paragraph (2) shall be 2 cents a gallon. If a liquid on which tax was imposed by paragraph (1) at the rate of 2 cents a gallon by reason of the preceding sentence is used as a fuel for the propulsion of a highway vehicle (A) which (at the time of such use) is registered, or is required to be registered, for highway use under the laws of any State or foreign country, or (B) which, in the case of a highway vehicle owned by the United States, is used on the highway, a tax of 2 cents a gallon shall be imposed under paragraph (2).

(c) RATE REDUCTION.—On and after October 1, 1972—

(1) The taxes imposed by this section shall be 1½ cents a gallon; and

(2) The second and third sentences of subsections (a) and (b) shall not apply.

* * * * * * *

(f) [Delete]

[Sec. 4041 as amended and in effect Jan. 1, 1959, and as amended by sec. 201(b), Federal-Aid Highway Act 1959 (73 Stat. 613) [P.L. 86-342, C.B. 1959-2, 697]; sec. 201 (a), (c), and (d), Federal-Aid Highway Act 1961 (75 Stat. 123, 124) [P.L. 87-61, page 309, this Bulletin]]

PAR. 2. Paragraph (c) (1) and (2) of § 48.4041-2 is amended to read as follows:

§ 48.4041-2 APPLICATION OF TAX ON SALE OF DIESEL FUEL.

* * * * * * *

(c) *Rate of tax.* * * *

(1) *Registered highway vehicles.*—Following are the rates applicable to the sale on or after January 1, 1959, of diesel fuel for use as a fuel in a diesel-powered highway vehicle which at the time of the sale is registered or required to be registered for highway use or in a diesel-powered highway vehicle owned by the United States which is used on the highway:

Diesel fuel sold	*Cents per gallon*
(i) January 1, 1959 to September 30, 1959, inclusive	3
(ii) October 1, 1959 to September 30, 1972, inclusive	4
(iii) On or after October 1, 1972	1½

(2) *Nonregistered highway vehicles.*—Following are the rates applicable to the sale on or after January 1, 1959, of diesel fuel for use in a diesel-powered highway vehicle which at the time of the sale is not registered and is not required to be registered for highway use (including a diesel-powered highway vehicle owned by the United States which is not used on the highway):

Diesel fuel sold	*Cents per gallon*
(i) January 1, 1959 to September 30, 1972, inclusive	2
(ii) On or after October 1, 1972	1½

PAR. 3. Paragraph (c) (1) and (2) of § 48.4041-3 is amended to read as follows:

§ 48.4041-3 APPLICATION OF TAX ON SALE OF SPECIAL MOTOR FUEL.

(c) *Rate of tax.* * * *

(1) *Registered highway vehicles.*—Following are the rates applicable to the sale on or after January 1, 1959, of special motor fuel for use as a fuel for the propulsion of a motor vehicle which at the time of the sale is registered or required to be registered for highway use or in a motor vehicle owned by the United States which is used on the highway:

Special motor fuel sold	*Cents per gallon*
(i) January 1, 1959 to September 30, 1959, inclusive	3
(ii) October 1, 1959 to September 30, 1972, inclusive	4
(iii) On or after October 1, 1972	1½

(2) *Motorboats, airplanes, and nonregistered motor vehicles.*—Following are the rates applicable to the sale on or after January 1, 1959, of special motor fuel for use as a fuel for the propulsion of a motorboat or airplane, or of a motor

vehicle which at the time of the sale is not registered and is not required to be registered for highway use (including a motor vehicle owned by the United States which is not used on the highway):

Special motor fuel sold	*Cents per gallon*
(i) January 1, 1959 to September 30, 1972, inclusive	2
(ii) On or after October 1, 1972	1½

PAR. 4. Paragraph (b) (1) and (2) of § 48.4041–5 is amended to read as follows:

§ 48.4041–5 APPLICATION OF TAX ON USE OF TAXABLE LIQUIDS.

* * * * * * *

(b) *Rate of tax.* * * *

(1) *Registered highway vehicles.*—Following are the rates applicable to the use on or after January 1, 1959, of taxable liquid as a fuel in a diesel-powered highway vehicle, or for the propulsion of a motor vehicle (i) which at the time of such use is registered or required to be registered for highway use, or (ii) in the case of such a vehicle owned by the United States which is used on the highway:

Taxable liquid used	*Cents per gallon*
(*a*) January 1, 1959 to September 30, 1959, inclusive, and no tax was imposed with respect to the sale of such liquid	3
(*b*) January 1, 1959 to September 30, 1959, inclusive, and tax at the rate of 2 cents per gallon was imposed with respect to the sale of such liquid	1
(*c*) October 1, 1959 to September 30, 1972, inclusive, and no tax was imposed with respect to the sale of such liquid	4
(*d*) October 1, 1959 to September 30, 1972, inclusive, and tax at the rate of 2 cents per gallon was imposed with respect to the sale of such liquid	2
(*e*) On or after October 1, 1972, and no tax was imposed with respect to the sale of such liquid	1½

(2) *Motorboats, airplanes, and nonregistered vehicles.*—Following are the rates applicable to the use on or after January 1, 1959, of taxable liquid as a fuel—

(i) For the propulsion of a motorboat or airplane,

(ii) In a diesel-powered highway vehicle, or for the propulsion of a motor vehicle, which at the time of such use is not registered and is not required to be registered for highway use, or

(iii) In a diesel-powered highway vehicle, or for the propulsion of a motor vehicle, owned by the United States which is not used on the highway:

Taxable liquid used	*Cents per gallon*
(*a*) January 1, 1959 to September 30, 1972, inclusive, and no tax was imposed with respect to the sale of such liquid	2
(*b*) On or after October 1, 1972, and no tax was imposed with respect to the sale of such liquid	1½

PAR. 5. Section 48.4071 is amended by revising subsections (a) and (c) of section 4071 and the historical note to read as follows:

§ 48.4071 STATUTORY PROVISIONS; IMPOSITION OF TAX.

SEC. 4071. IMPOSITION OF TAX.

(a) IMPOSITION AND RATE OF TAX.—There is hereby imposed upon the following articles, if wholly or in part of rubber, sold by the manufacturer, producer, or importer, a tax at the following rates:

(1) Tires of the type used on highway vehicles, 10 cents a pound.

(2) Other tires (other than laminated tires to which paragraph (5) applies), 5 cents a pound.

(3) Inner tubes for tires, 10 cents a pound.

(4) Tread rubber, 5 cents a pound.

(5) Laminated tires (not of the type used on highway vehicles) which consist wholly of scrap rubber from used tire casings with an internal metal fastening agent, 1 cent a pound.

* * * * * * *

(c) RATE REDUCTION.—On and after October 1, 1972—
(1) The tax imposed by paragraph (1) of subsection (a) shall be 5 cents a pound;
(2) The tax imposed by paragraph (3) of subsection (a) shall be 9 cents a pound; and
(3) Paragraph (4) of subsection (a) shall not apply.

[Sec. 4071 as amended and in effect Jan. 1, 1959, and as amended by sec. 202, Federal-Aid Highway Act 1961 (75 Stat. 124) [P.L. 87-61, page 309, this Bulletin]]

PAR. 6. Paragraph (b)(1) of § 48.4071-1 is amended to read as follows:

§ 48.4071-1 IMPOSITION AND RATES OF TAX.

* * * * * * *

(b) *Rates and computation of tax.*—(1) *Rates of tax.*—Tax is imposed upon each of the above-mentioned taxable articles at the rate applicable on the date on which the article is sold, as specified below:

(i) *Tires:*	
(*a*) Of the type used on highway vehicles:	
(*1*) For the period January 1, 1959 to June 30, 1961, inclusive	8 cents per pound
(*2*) For the period July 1, 1961 to September 30, 1972, inclusive	10 cents per pound
(*3*) On or after October 1, 1972	5 cents per pound
(*b*) Of the type used on other than highway vehicles	5 cents per pound
(*c*) Laminated tires:	
(*1*) For the period January 1, 1959 to May 31, 1960	5 cents per pound
(*2*) On or after June 1, 1960	1 cent per pound
(ii) *Inner tubes:*	
(*a*) For the period January 1, 1959 to June 30, 1961, inclusive	9 cents per pound
(*b*) For the period July 1, 1961 to September 30, 1972, inclusive	10 cents per pound
(*c*) On or after October 1, 1972	9 cents per pound
(iii) *Tread rubber:*	
(*a*) For the period January 1, 1959 to June 30, 1961, inclusive	3 cents per pound
(*b*) For the period July 1, 1961 to September 30, 1972, inclusive	5 cents per pound

PAR. 7. Section 48.4081 is amended to read as follows:

§ 48.4081 STATUTORY PROVISIONS; IMPOSITION OF TAX.

SEC. 4081. IMPOSITION OF TAX.

(a) IN GENERAL.—There is hereby imposed on gasoline sold by the producer or importer thereof, or by any producer of gasoline, a tax of 4 cents a gallon.

(b) RATE REDUCTION.—On and after October 1, 1972, the tax imposed by this section shall be 1½ cents a gallon.

[Sec. 4081 as amended and in effect Jan. 1, 1959, and as amended by sec. 201(a), Federal-Aid Highway Act 1959 (73 Stat. 613) [P.L. 86-342, C.B. 1959-2, 697]; sec. 201 (b), (c), and (d), Federal-Aid Highway Act 1961 (75 Stat. 123, 124) [P.L. 87-61, page 309, this Bulletin]]

PAR. 8. Paragraph (b) of § 48.4081-1 is amended to read as follows:

§ 48.4081-1 IMPOSITION AND RATES OF TAX.

* * * * * * *

(b) *Rate of tax.*—Tax is imposed on the sale of gasoline at the rate applicable on the date on which the gasoline is sold. Following are the rates in effect on or after January 1, 1959:

Gasoline sold	*Cents per gallon*
(1) January 1, 1959 to September 30, 1959, inclusive	3
(2) October 1, 1959 to September 30, 1972, inclusive	4
(3) On or after October 1, 1972	1½

PAR. 9. Paragraph (a)(1) of § 48.6421(a)–1 is amended by inserting "October 1, 1972" in lieu of "July 1, 1972" and, as so amended, reads as follows:

§ 48.6421(a)–1 PAYMENTS TO ULTIMATE PURCHASER OF GASOLINE USED FOR CERTAIN NONHIGHWAY PURPOSES.—(a) *In general.*—(1) Section 6421(a) provides that if gasoline is used otherwise than as a fuel in a highway vehicle—

(i) Which, at the time the gasoline is so used, is registered, or is required to be registered, for highway use under the laws of any State or foreign country, or

(ii) Which, in the case of a highway vehicle owned by the United States, is used on the highway,

payment (without interest) in respect of such gasoline shall be made to the ultimate purchaser thereof. The payment shall be in an amount equal to 1 cent for each gallon of gasoline so used on which tax was paid under section 4081 at the rate of 3 cents a gallon and 2 cents for each gallon of gasoline so used on which tax was paid under section 4081 at the rate of 4 cents a gallon. However, payment in respect of gasoline used as provided in section 6421(a) shall be made only as to gasoline purchased by an ultimate purchaser after June 30, 1956, and prior to October 1, 1972, and only if a properly executed claim is filed by the ultimate purchaser within the time prescribed in section 6421(c) (see § 48.6421(c)–1). For meaning of the term "gasoline", see paragraph (b) of § 48.4082–1, and for the definition of "State", see section 7701. For provisions relating to payments in respect of gasoline used on a farm for farming purposes, see section 6420 and the regulations thereunder.

PAR. 10. Paragraph (a)(1) of § 48.6421(b)–1 is amended by inserting "October 1, 1972" in lieu of "July 1, 1972" and, as so amended, reads as follows:

§ 48.6421(b)–1 PAYMENTS TO ULTIMATE PURCHASER OF GASOLINE USED BY LOCAL TRANSIT SYSTEMS.—(a) *In general.*—(1) Section 6421(b) provides that if gasoline is used during any calendar quarter in vehicles while engaged in furnishing scheduled common carrier public passenger land transportation service along regular routes, payment (without interest) in respect of such gasoline shall be made to the ultimate purchaser thereof provided the 60-percent passenger fare revenue test set forth in section 6421(b)(2) (see paragraph (b) of this section) is met for such calendar quarter. The payment in respect of gasoline so used in a particular calendar quarter is computed:

(i) By multiplying the number of gallons of gasoline so used in the calendar quarter on which tax was paid under section 4081 at the rate of 3 cents a gallon by 1 cent and by multiplying the number of gallons of gasoline so used in the calendar quarter on which tax was paid under section 4081 at the rate of 4 cents a gallon by 2 cents, and by multiplying the sum of these two products by

(ii) The percentage which the ultimate purchaser's tax-exempt passenger fare revenue derived from such scheduled service during such calendar quarter was of his total passenger fare revenue (not including the tax imposed by section 4261 on the amount paid for the transportation of persons) derived from such scheduled service during such quarter.

However, payment in respect of gasoline used as provided in section 6421(b)(1) shall be made only as to gasoline purchased by an ultimate purchaser after June 30, 1956, and prior to October 1, 1972, and only if a properly executed claim is filed by the ultimate purchaser within the time prescribed in section 6421(c) (see § 48.6421(c)–1). For meaning of the terms "gasoline" and "tax-exempt passenger fare revenue", see paragraph (b) of § 48.4082–1 and paragraph (b) of § 48.6421(d)–1, respectively.

PAR. 11. Section 48.6421(c)–1 is amended by revising paragraph (a)(1) to insert "October 1, 1972" in lieu of "July 1, 1972", and by revising paragraph (b)(2) to delete subdivisions (*i*)(*c*), (*ii*)(*h*), and item 8 in Table III in subdivision (iii). These amended provisions to read as follows:

§ 48.6421(c)-1 CLAIMS.—(a) *Period covered; time for filing.*—(1) *In general.*—Except as provided in subparagraph (2) of this paragraph and paragraph (d) of this section, a claim in respect of gasoline used for nonhighway purposes or by local transit systems shall cover a full one-year period beginning July 1 and ending June 30 of the following calendar year. A claim for a particular one-year period shall cover only gasoline purchased after June 30, 1956, and prior to October 1, 1972, and used during such one-year period for nonhighway purposes or by local transit systems. Therefore, gasoline on hand at the end of such one-year period (as, for example, in fuel supply tanks or in storage tanks and drums) must be excluded from a claim filed for such one-year period. On the other hand, gasoline used during such one-year period may be covered by a claim for such period although such gasoline has not been paid for at the time the claim is filed. A claim in respect of gasoline used for nonhighway purposes or by local transit systems during any one-year period ending June 30 shall not be allowed unless such claim is filed on or before September 30 of the calendar year in which the one-year period ends. See section 7502 for provisions relating to timely mailing treated as timely filing, and section 7503 for rules for filing claim when September 30 falls on Saturday, Sunday, or a legal holiday.

* * * * * * *

(b) *Form of claim.* * * *
(2) *Supporting evidence.*—(i) *Nonhighway uses.* * * *
(*c*) [deleted]

* * * * * * *

(ii) *Transit systems.* * * *
(*h*) [deleted]

* * * * * * *

(iii) *Example.* * * *
(8) [deleted]
(9) Income tax return for calendar year 1958 filed with District Director of Internal Revenue, Cleveland, Ohio.

PAR. 12. Section 48.6421(h) is amended by revising section 6421(h) and the historical note to read as follows:

§ 48.6421(h) STATUTORY PROVISIONS; GASOLINE USED FOR CERTAIN NONHIGHWAY PURPOSES OR BY LOCAL TRANSIT SYSTEMS; EFFECTIVE DATE.

SEC. 6421. GASOLINE USED FOR CERTAIN NONHIGHWAY PURPOSES OR BY LOCAL TRANSIT SYSTEMS. * * *

(h) EFFECTIVE DATE.—This section shall apply only with respect to gasoline purchased after June 30, 1956, and before October 1, 1972.

[Sec. 6421(h) as added and in effect Jan. 1, 1959, and as amended by sec. 201(e), Federal-Aid Highway Act 1961 (75 Stat. 124) [P.L. 87-61, page 309, this Bulletin]]

FACILITIES AND SERVICES EXCISE TAXES
(26 CFR Part 49)

PAR. 13. Section 49.4261 is amended by revising section 4261(a) (1) and (2), section 4261(b) (1) and (2), section 4261(c) (1) and (2), and the historical note, to read as follows:

§ 49.4261 STATUTORY PROVISIONS; IMPOSITION OF TAX; AMOUNTS PAID WITHIN THE UNITED STATES; AMOUNTS PAID OUTSIDE THE UNITED STATES; SEATS, BERTHS, ETC.; BY WHOM PAID.

SEC. 4261. IMPOSITION OF TAX.

(a) AMOUNTS PAID WITHIN THE UNITED STATES. * * *
(1) 10 percent of the amount so paid before July 1, 1962; or
(2) 5 percent of the amount so paid on or after July 1, 1962.

(b) AMOUNTS PAID OUTSIDE THE UNITED STATES. * * *
(1) 10 percent of the amount so paid before July 1, 1962; or
(2) 5 percent of the amount so paid on or after July 1, 1962.

(c) SEATS, BERTHS, ETC. * * *
(1) 10 percent of the amount so paid before July 1, 1962; or
(2) 5 percent of the amount so paid on or after July 1, 1962.

* * * * * * *

[Sec. 4261 as amended and in effect Jan. 1, 1959, and as further amended by sec. 4, Tax Rate Extension Act 1959 (73 Stat 158) [P.L. 86-75, C.B. 1959-2, 679]; sec. 202(a)(3), Public Debt and Tax Rate Extension Act 1960 (74 Stat. 290) [P.L. 86-564, C.B. 1960-2, 681]; sec. 3(a)(3), Tax Rate Extension Act 1961 (75 Stat. 193) [P.L. 87-72, page 317, this Bulletin]]

PAR. 14. Paragraph (a) of § 49.4261-2 is amended to read as follows:

§ 49.4261-2 RATE AND APPLICATIONS OF TAX.—(a) *Rate of tax.*—Tax is imposed under section 4261 upon the amount paid for taxable transportation at the rate applicable on the date on which payment for the transportation is made as specified below:

(1) With respect to amounts paid before July 1, 1962_____ 10 percent
(2) With respect to amounts paid on or after July 1, 1962_____ 5 percent

For purposes of determining the applicable rate of tax, it is immaterial that the taxable transportation begins or ends before, on, or after July 1, 1962. For the rate and application of tax with respect to amounts paid for seating and sleeping accommodations in connection with taxable transportation, see § 49.4261-9.

PAR. 15. Paragraph (b) of § 49.4261-9 is amended to read as follows:

§ 49.4261-9 SEATS AND BERTHS; RATE AND APPLICATION OF TAX.

* * * * * * *

(b) *Rate of tax.*—The tax is imposed under section 4261(c) upon the amount paid for taxable seating or sleeping accommodations at the rate applicable on the date on which payment for the accommodations is made as specified below:

(1) With respect to amounts paid before July 1, 1962_____ 10 percent
(2) With respect to amounts paid on or after July 1, 1962____ 5 percent

CERTAIN EXCISE TAX MATTERS UNDER THE EXCISE TAX TECHNICAL CHANGES ACT OF 1958

(26 CFR Part 148)

PAR. 16. Section 148.1-3 is amended by revising that portion of paragraph (b) preceding subparagraph (1) and by revising subparagraph (11) of paragraph (b), to read as follows:

§ 148.1-3 TEMPORARY PROCEDURES FOR TAX-FREE SALES AND PURCHASES.

* * * * * * *

(b) *Tax-free sales only if seller and purchaser are registered.*—Except as provided in paragraphs (c) and (i) of this section, an article subject to tax under chapter 32 may on or after January 1, 1959 (on or after May 1, 1960, in the case of a bicycle tire or tube to be used for the purpose prescribed in subparagraph (13) of this paragraph and on or after October 1, 1961, in the case of gasoline to be used for the purpose described in subparagraph (11)(ii) of this paragraph) be sold tax free by the manufacturer for the following uses (but only if the seller, first purchaser, and second purchaser, as the case may be, have registered as required by this section)—

* * * * * * *

(11) In the case of gasoline, (i) to a producer of gasoline, or (ii) for use by the purchaser, for nonfuel purposes, as a material in the manufacture or production of another article to be manufactured or produced by him;

Because this Treasury Decision merely (1) reflects the extension or increase in tax rates applicable to diesel fuel, special motor fuels, tires, inner tubes, tread rubber, gasoline, and transportation of persons in

accordance with the statutory changes made by sections 201 and 202 of the Federal-Aid Highway Act of 1961 [P.L. 87–61, page 309, this Bulletin] and section 3(a)(3) of the Tax Rate Extension Act of 1961 [P.L. 87–72, page 317, this Bulletin], (2) provides for registration of sellers and purchasers of gasoline to permit the tax-free sale of gasoline on or after October 1, 1961, under the amendment of section 4221(d)(6) made by section 205(a) of the Federal-Aid Highway Act of 1961, and (3) relaxes the reporting requirements for persons claiming payment of tax under section 6421 on account of the nonhighway or local transit use of gasoline, it is hereby found 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 section 7805 of the Internal Revenue Code of 1954 (68A Stat. 917; 26 U.S.C. 7805).)

MORTIMER M. CAPLIN,
Commissioner of Internal Revenue.

Approved October 6, 1961.

STANLEY S. SURREY,
Assistant Secretary of the Treasury.

(Filed by the Division of the Federal Register on October 10, 1961, 8:50 a.m., and published in the issue of the Federal Register for October 11, 1961, 26 F.R. 9575)

CHAPTER 32.—MANUFACTURERS EXCISE TAXES

SUBCHAPTER A.—AUTOMOTIVE AND RELATED ITEMS

PART I.—MOTOR VEHICLES

SECTION 4061.—IMPOSITION OF TAX

26 CFR 40.4061(a)–1: Imposition of tax. Rev. Rul. 61–159

"Detachable containers" which are produced with specially designed understructures for use with automobile truck chassis equipped with frames specially designed to accommodate the containers are considered to be taxable bodies for automobile trucks within the meaning of section 4061(a)(1) of the Code. Accordingly, the manufacturers excise tax imposed by that section applies to the manufacturer's sales of these containers.

Rev. Rul. 60–185, C.B. 1960–1, 412, distinguished.

Advice has been requested concerning the applicability of the manufacturers excise tax on motor vehicle articles to certain "detachable containers" sold for use in connection with automobile truck chassis.

A company manufactures and sells several different types and sizes of detachable containers, each of which is produced with the same type of specially designed understructure. Typical of the containers produced are those designed for use as refuse or scrap containers, tanks, portable tool boxes, flat platforms, cargo containers, cable reel carriers, or stakeside containers. These containers are at-

tached to and are initially transported only by a truck chassis equipped with a hydraulically operated tilting frame specially designed to accommodate the containers. Subsequently, the containers may be reloaded onto railroad flat cars for transporting, but the loading onto or unloading from a flat car can only be effectively accomplished by a truck equipped with the specially designed frame.

The detachable containers are said to be intended for use at material or cargo accumulation points, and while stationed there are used for storage and cargo accumulation purposes. When a container is filled, the truck frame mechanism picks up the container for attachment in carrying position on the specially designed frame of the truck chassis. Then, the container may be transported to and from a dumping or unloading point.

Section 4061(a)(1) of the Internal Revenue Code of 1954 imposes a tax upon the sale by the manufacturer, producer, or importer of various motor vehicle articles, including bodies for automobile trucks.

Revenue Ruling 60–185, C.B. 1960–1, 412, holds that so-called "cargo containers" which are designed for shipment of property by water, rail, and highway are not considered to constitute taxable bodies for trucks, truck trailers or semitrailers within the meaning of section 4061(a)(1) of the Code. These containers are designed to be handled by overhead cranes, fork lift trucks, or similar equipment, and are of special heavy construction so that they may be stacked up to five deep in the hold of a ship.

The basis for holding the "cargo containers" nontaxable is that they are considered to be articles designed or adapted by the manufacturer for purposes predominantly other than the transportation of property on the highway, even though incidental highway use may occur. In contrast, as described above, any movement of the detachable containers of the type here involved requires the utilization of the specially equipped truck chassis.

Upon the basis of the facts stated above, it is held that the detachable containers in question are primarily designed for use in the transportation of property on the highway. Under such circumstances, these containers are considered to be taxable bodies for automobile trucks within the meaning of section 4061(a)(1) of the Code. Accordingly, the manufacturers excise tax imposed by that section of the Code applies to the manufacturer's sales of these containers.

Revenue Ruling 60–185, C.B. 1960–1, 412, distinguished.

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26 CFR 40.4061(b)–1: Imposition of tax.

Whether certain sales by manufacturers of automobile seat covers come within the scope of the exemption from the manufacturers excise tax for articles sold for use in further manufacture. See Rev. Rul. 61–197, page 190.

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26 CFR 40.4061(b)–2: Definition of parts or accessories. Rev. Rul. 61–139

Certain flange gaskets and ring gaskets, which are produced, packaged, and sold for replacement use on taxable motor vehicle articles, are not excluded from the manufacturers excise tax on

automobile parts or accessories merely because the manufacturer produces and sells other similar gaskets for nonautomotive use. The tax imposed by section 4061(b) of the Internal Revenue Code of 1954 applies to the manufacturer's sales of those gaskets which are primarily designed for use on taxable motor vehicle articles.

Advice has been requested concerning the applicability of the manufacturers excise tax on automobile parts or accessories to certain flange and ring gaskets which are sold by the manufacturer for replacement use on taxable motor vehicle articles.

A manufacturer produces several types of flange gaskets and ring gaskets which are fabricated to meet the special needs and specifications of the manufacturer's customers. These gaskets are produced from various materials and are made in a variety of shapes and sizes.

Some of these gaskets are produced and sold to dealers and distributors for resale for use as replacement parts for automobiles, trucks, buses, trailers, and semitrailers. Each gasket which is produced and sold for this purpose is packaged in a container with a label indicating the make and model of the motor vehicle with which it is to be used. Also included on the label is a part number designated by the manufacturer of the gasket and a part number designated by the manufacturer of the motor vehicle.

On the other hand, certain similar gaskets are produced and sold for use in the manufacture of various articles not within the automotive field. When produced and sold for this purpose, they are fabricated to meet the special needs and specifications of the nonautomotive industrial customers. These gaskets may be sold in bulk or packaged in containers with labels indicating the part numbers and descriptions as designated by the various industrial customers.

It has been contended that, since articles in this broad category are produced and sold for use both in the automotive field and in the nonautomotive industrial field, the entire category should be excluded from the tax on automobile parts or accessories because they are "articles of a general use."

Section 4061(b) of the Internal Revenue Code of 1954 imposes a tax on sales by the manufacturer, producer, or importer of parts or accessories (other than tires and inner tubes and other than automobile radio and television receiving sets) for any of the motor vehicle articles enumerated in section 4061(a) of the Code.

Section 40.4061(b)-2 of the Manufacturers and Retailers Excise Tax Regulations defines parts or accessories, in pertinent part, as follows:

(a) *In general.*—The term "parts or accessories" includes (1) any article, the primary use of which is to improve, repair, replace, or serve as a component part of an automobile truck or bus chassis or body, or other automobile chassis or body, or taxable tractor, (2) any article designed to be attached to or used in connection with such chassis, body, or tractor to add to its utility or ornamentation, and (3) any article, the primary use of which is in connection with such chassis, body, or tractor, whether or not essential to its operation or use. However, the term does not include tires, inner tubes, or automobile radio or television receiving sets, since these articles are expressly excluded by section 4061(b) from the tax. The term "parts or accessories" does include tire valves designed for use on tires or tubes for articles taxable under section 4061(a). The term "parts or accessories" includes all articles which have reached such a stage of manufacture as to be commonly known as parts or

accessories whether or not fitting operations are required in connection with their installation.

(b) *Articles of a general use.*—The term "parts or accessories" does not include articles which are not used primarily in the manufacture of automobile trucks, other automobiles, or tractors, but have a general use in the manufacture of various articles. For example, commodities such as ball and roller bearings, bolts, nuts, washers, screws, nails, tacks, rivets, pins, studs, cotters, pipe fittings such as plugs, tees, ells, and elbows, drain cocks, grease cups, oilers, and similar articles are not of themselves parts or accessories. On the other hand, parts for automobile parts or accessories are in themselves taxable unless they are articles of a type not specifically designed for use primarily in the automobile field. For example, the tax applies to the sale of gears, flexible shafts, and flexible housings designed as replacement parts for automotive speedometers, as well as replacement parts for automobile engines, transmissions, differentials, steering mechanisms, timers, windshield wiper motors, and other automobile parts or accessories.

The fact that a manufacturer produces articles, some of which are designed and sold for use as replacement parts in the automotive field and some of which are designed and sold for use in the nonautomotive field, does not of itself serve to bring all of these articles within the meaning of the term "articles of a general use" as set forth in the regulations. The different articles within the category must be considered separately and upon the basis of the identity established for them by the manufacturer. Articles which are primarily designed for use with any of the motor vehicle articles enumerated in section 4061(a) of the Code are automobile parts or accessories within the meaning of section 4061(b) of the Code.

The fact that the flange gaskets and ring gaskets in the instant case are packaged and sold for use as replacement parts in the automotive field is indicative of the fact that they are primarily designed for use on taxable motor vehicle articles. Therefore, they are automobile parts or accessories rather than "articles of a general use." Accordingly, it is held that sales by the manufacturer of these particular flange and ring gaskets are subject to the manufacturers excise tax imposed by section 4061(b) of the Code.

Rev. Rul. 61–209

Facial tissue dispensers which are designed for use in automobiles are considered to be automobile parts or accessories within the meaning of section 4061(b) of the Internal Revenue Code of 1954, even though they may also be used in other places. Accordingly, the manufacturers excise tax imposed by that section applies to the manufacturer's sales of these articles.

Advice has been requested concerning the applicability of the manufacturers excise tax on automobile parts or accessories to sales of the articles described below.

A company manufactures and sells several types of tissue dispensers which are widely used in automobiles. Each of these plastic dispensers is designed to hold a box or a package of absorbent paper facial tissues. Some of the dispensers are designed to be attached to an automobile sun visor. Others are designed to be attached directly to some other part of an automobile. Some of them are designed with an extra compartment at the bottom for the disposal of used tissues.

Although these articles are sold primarily through automotive channels and it is generally recognized that they are used primarily in con-

nection with automobiles, they also are advertised for use in homes, offices, shops, or boats.

Section 4061(b) of the Internal Revenue Code of 1954 imposes a tax on the sale by the manufacturer, producer, or importer of parts or accessories (other than tires and inner tubes and other than automobile radio and television receiving sets) for any of the motor vehicle articles enumerated in section 4061(a) of the Code.

Section 40.4061(b)-2(a) of the Manufacturers and Retailers Excise Tax Regulations provides that, in general, the term "parts or accessories" includes (1) any article, the primary use of which is to improve, repair, replace, or serve as a component part of an automobile truck or bus chassis or body, or other automobile chassis or body, or taxable tractor, (2) any article designed to be attached to or used in connection with such chassis, body, or tractor to add to its utility or ornamentation, and (3) any article, the primary use of which is in connection with such chassis, body, or tractor, whether or not essential to its operation or use.

The tissue dispensers described above are designed for use in automobiles even though they may also be used in other places. Accordingly, the manufacturer's sales of these articles are subject to the manufacturers excise tax on parts and accessories imposed by section 4061(b) of the Code.

Pursuant to the authority contained in section 7805(b) of the Code, this ruling will be applied only to sales made on or after January 1, 1962.

PART II.—TIRES AND TUBES

SECTION 4071.—IMPOSITION OF TAX

26 CFR 48.4071: Statutory provisions; imposition of tax.

Tax rate increase on sales of tires of the type used on highway vehicles, inner tubes, and tread rubber for the period July 1, 1961, to September 30, 1972, inclusive. See T.D. 6574, page 162.

PART III.—PETROLEUM PRODUCTS

Subpart A.—Gasoline

SECTION 4081.—IMPOSITION OF TAX

26 CFR 48.4081: Statutory provisions; imposition of tax.

Extension to October 1, 1972, of the tax rate of four cents a gallon on the sale of gasoline. See T.D. 6574, page 162.

Subpart B.—Lubricating Oil

SECTION 4091.—IMPOSITION OF TAX

26 CFR 48.4091–2: Definitions. Rev. Rul. 61–148

A certain lubricant for jet engines, which is a synthetic material, is not considered to be a "lubricating oil" within the meaning of that term as defined in section 48.4091–2(a) of the Manufacturers and Retailers Excise Tax Regulations. Therefore, sales by the manufacturer of the lubricant are not subject to the manufacturers excise tax imposed by section 4091 of the Internal Revenue Code of 1954.

Advice has been requested whether a certain lubricant for jet engines is considered to be a lubricating oil for purposes of the manufacturers excise tax.

A company produces and sells a product which it refers to as a lubricant for jet engines. This product is synthetically produced from various chemicals in order to impart certain desirable properties. It has been established that the product is a synthetic material having the physical properties of oil, including lubricity.

Section 4091 of the Internal Revenue Code of 1954 imposes a tax on lubricating oils sold by the manufacturer or producer thereof.

Section 48.4091–2(a) of the Manufacturers and Retailers Excise Tax Regulations provides that the term "lubricating oils" includes all oils, regardless of origin, which are suitable for use as a lubricant, or sold for use as a lubricant. The term does not include synthetic materials which possess lubricating properties, nor does it ordinarily include products of the type commonly known as grease.

Since section 48.4091–2(a) of the regulations provides that the term "lubricating oils" does not include synthetic materials which possess lubricating properties, the product described above is not considered to be a lubricating oil within the meaning of that section.

Accordingly, it is held that the company's sales of this particular product are not subject to the manufacturers excise tax on lubricating oils imposed by section 4091 of the Code.

SUBCHAPTER B.—HOUSEHOLD TYPE EQUIPMENT, ETC.

PART II.—ELECTRIC, GAS, AND OIL APPLIANCES

SECTION 4121.—IMPOSITION OF TAX

26 CFR 48.4121–2: Definitions. Rev. Rul. 61–165

The fact that a portable kerosene cooking range is sold with a "sea rail" to facilitate its use aboard boats does not change the nature of the range from a household type appliance to a nonhousehold type appliance. Accordingly, sales of the range with sea rail by the manufacturer thereof are subject to the manufacturers excise tax on electric, gas, and oil appliances, imposed by section 4121 of the Internal Revenue Code of 1954.

Advice has been requested concerning the applicability of the manufacturers excise tax on electric, gas, and oil appliances of the household type to sales of the article described below.

A manufacturer produces and sells a portable two-burner kerosene cooking range, which is recognized as being subject to the manufacturers excise tax imposed by section 4121 of the Internal Revenue Code of 1954. However, the manufacturer sells some of these appliances with separate "sea rails" which facilitate their use aboard boats. After the sea rail has been fastened to some surface on the boat, the cooking range may be placed inside the sea rail, thereby preventing movement of the range as a result of the motion of the boat. The sea rail is equipped with an adjusting bar which may be used to keep utensils in place on the range.

When sold with a sea rail, the appliance is sometimes referred to as a "marine" or "yachting" range. The question is whether the manufacturer's sale of the appliance with a sea rail removes it from the scope of section 4121 of the Code.

Section 4121 of the Internal Revenue Code of 1954 imposes a tax upon the sale by the manufacturer, producer, or importer of certain "articles of the household type (including in each case parts or accessories therefor sold on or in connection with the sale thereof)." Included in the enumeration of articles subject to tax are "electric, gas, or oil appliances of the type used for cooking, warming, or keeping warm, food or beverages for consumption on the premises."

Section 48.4121–2(a) of the Manufacturers and Retailers Excise Tax Regulations provides that the term "articles of the household type" includes all articles enumerated in section 4121 of the Code which have an actual, practical, commercial fitness, or are specifically designed and constructed, for household use.

Section 48.4121–2(c) of the regulations provides that the term "electric, gas, or oil appliances of the type used for cooking, warming, or keeping warm, food or beverages for consumption on the premises" includes any type of appliance operated by, or for which the heat is generated by, electricity, gas, or oil, which is used to cook, warm, or keep warm, food or beverages for consumption on the premises.

The fact that the kerosene range described above is sold with a sea rail does not divest the article of its household characteristics or change its nature from a household type appliance to a non-household type appliance. Furthermore, the fact that the range with sea rail may be sold for use on a boat is immaterial. Therefore, it is held that the kerosene range with sea rail is a household type appliance within the meaning of section 4121 of the Code. Accordingly, sales thereof are subject to the manufacturers excise tax imposed by that section.

Under the authority contained in section 7805(b) of the Code, the conclusion of this Revenue Ruling will not be applied to sales made prior to November 1, 1961.

Rev. Rul. 61–202

For purposes of the manufacturers excise tax on oil water heaters of the household type, imposed by section 4121 of the Internal Revenue Code of 1954, oil water heaters of the pressure gun type which have either (1) a storage capacity of 50 gallons or less or (2) a recovery rate of 150 gallons or less per hour based on a 100 degree

Fahrenheit rise are considered to be of the household type, unless by reason of their design and construction they are primarily adapted for other than household use.

Advice has been requested concerning the applicability of the manufacturers excise tax on certain electric, gas, and oil appliances to sales by the manufacturer of the oil-fired water heaters described below.

(1) *An oil water heater of the pressure gun type with a storage capacity of 30 gallons and a recovery rate of 120 gallons per hour.* This oil water heater consists of a heavy steel glass-lined cylindrical tank, a pressure type oil burner, and a refractory combustion chamber. The overall measurements of the heater are approximately 58 inches in height and 22 inches in diameter. It has a storage capacity of 30 gallons of water, a recovery rate of 120 gallons per hour, and an input rating of 140,000 B.T.U.'s per hour.

(2). *An oil water heater of the pressure gun type with a storage capacity of 70 gallons and a recovery rate of 163 gallons per hour.* This oil water heater consists of a heavy steel glass-lined cylindrical tank, a pressure type oil burner, and a refractory combustion chamber. The overall measurements of the heater are approximately 72 inches in height and 26 inches in diameter. It has a storage capacity of 70 gallons of water, a recovery rate of 163 gallons per hour, and an input rating of 190,000 B.T.U.'s per hour.

Prior to November 1, 1951, the statute imposed a manufacturers excise tax upon all electric, gas, or oil water heaters. However, the Revenue Act of 1951 limited the applicability of the tax to those water heaters "of the household type."

This provision is now contained in section 4121 of the Internal Revenue Code of 1954, which imposes a tax upon the sale by the manufacturer, producer, or importer of numerous "articles of the household type," including "electric, gas, or oil water heaters."

In accordance with section 48.4121–2(a) of the Manufacturers and Retailers Excise Tax Regulations, the term "articles of the household type" includes all articles enumerated in section 4121 which have an actual, practical, commercial fitness, or are specifically designed and constructed, for household use.

In general, there are two basic types of oil-fired water heaters, which are distinguished by the different types of burners which are incorporated therein. One type has an "atmospheric pot" type burner, and the other has a "pressure gun" type burner.

In the atmospheric pot type heaters, gravity causes the oil to flow to the burner. In the pressure gun type heaters the oil is forced into the combustion chamber in an almost vaporized condition. The pressure gun type heaters produce much greater heat than do the atmospheric pot type heaters. Because of the differences in design, the pressure gun type heaters will heat water at a faster rate and, therefore, will produce greater quantities of hot water.

Since the amendment of the statute in 1951, it has been generally recognized that atmospheric pot type oil water heaters are of the household type. Therefore, they have been held to be subject to the manufacturers excise tax when sold by the manufacturer, producer, or importer.

On the other hand, at the time of the statutory amendment there was practically no household use of the pressure gun type heaters

because their greater heating capacity was considerably beyond the household demands for hot water. Therefore, these heaters have generally been considered to be not of the household type and, accordingly, not subject to the manufacturers excise tax.

In recent years, however, there has been a considerable increase in the household consumption of hot water. A recent survey of the industry indicates that, as a result of this increased consumption, there has been a trend toward the manufacture and sale of oil water heaters of the pressure gun type *specifically for household use.* Consequently, it now is recognized by the industry, as well as by the Internal Revenue Service, that some of the pressure gun type heaters have an actual, practical, commercial fitness for household use or are specifically designed and constructed for household use.

It has been found that the two factors which primarily distinguish between those heaters of the household type and those not of the household type are (i) the water *storage capacity* and (ii) the *recovery rate*, that is, the number of gallons of water in which the heaters will increase the temperature a designated number of degrees in a specified time. In order to promote uniformity in the application of the tax, it seems advisable to establish an administrative test of taxability based upon these two factors.

Accordingly, in view of the current situation in the industry, oil water heaters of the pressure gun type which have *either* (i) a storage capacity of 50 gallons or less *or* (ii) a recovery rate of 150 gallons or less per hour based on a 100-degree Fahrenheit rise are considered to be of the household type, *unless* by reason of their design and construction they are primarily adapted for other than household use.

In accordance with these criteria, the heater described in (1) above is subject to the manufacturers excise tax imposed by section 4121 of the Code, and the heater described in (2) above is not subject to the tax imposed by that section.

Under the authority contained in section 7805(b) of the Code, the criteria established by this Revenue Ruling will be applied only to sales made by manufacturers, producers, or importers on and after January 1, 1962.

SUBCHAPTER C.—ENTERTAINMENT EQUIPMENT

PART I.—RADIO AND TELEVISION SETS, PHONOGRAPHS AND RECORDS, ETC.

SECTION 4141.—IMPOSITION OF TAX

26 CFR 48.4141–1: Imposition and rate of tax. Rev. Rul. 61–160

The manufacturers excise tax imposed on radio receiving sets by section 4141 of the Internal Revenue Code of 1954 applies to kits containing components for radio receiving sets, including crystal or germanium diode receiving sets, which by reason of their design are suitable for receiving radio signals. It is immaterial whether they are basic (simple) or complex, whether they incorporate amplification stages, and whether they are intended for use by children or adults. However, the tax does not apply to toys which are incapable of receiving any radio signals.

Revenue Ruling 58–333, C.B. 1958–1, 413, revoked.

It has come to the attention of the Internal Revenue Service that some manufacturers of radio receiving sets have misinterpreted certain language used in Revenue Ruling 58–333, C.B. 1958–1, 413.

Revenue Ruling 58–333 holds that the manufacturers excise tax imposed by section 4141 of the Internal Revenue Code of 1954 does not apply to the "radio kits" which are described therein. Those kits contain all of the necessary parts for the assembly of so-called "radio receiving sets." The kits are designed, advertised, and sold as toys. It is stated that the kits are made up of substandard components (tuning coils, transistors, and diodes). They are capable of only a semblance of audio production and do not meet the performance standards characteristic of a commercial radio receiving set with respect to tone and volume.

Based upon all of the facts, Revenue Ruling 58–333 holds that the articles described are not radio receiving sets as contemplated by section 4141 of the Code. Instead, those articles merely simulate such sets. However, that ruling points out that the term "radio receiving sets" does apply to kits which are comprised of components which, when assembled, are suitable for use as radios of the conventional or commercial type, regardless of their price or quality.

The use of the terms "commercial radio receiving set," "radios of the conventional or commercial type," "substandard components," and "toy radio receiving set kits" in Revenue Ruling 58–333 has been misinterpreted by some manufacturers to mean that the tax does not apply to simple crystal or germanium diode radio receiving sets which are designed and sold for receiving radio signals.

A crystal or germanium diode set is considered to be a "conventional" type of basic but actual functioning radio receiving set even though its quality may not compare favorably with the more complex sets. See Revenue Ruling 167, C.B. 1953–2, 428, which holds that the tax applies to kits which contain the components for the assembly of a crystal radio receiving set or for the assembly of a one-tube radio receiving set.

The position of the Service, as intended to be set forth in Revenue Ruling 58–333, has been to exclude from the tax toys which are incapable of receiving any radio signals.

As a restatement of the position of the Service, it is held that the manufacturers excise tax imposed on radio receiving sets by section 4141 of the Code applies to kits containing components for radio receiving sets, including crystal or germanium diode radio receiving sets, which by reason of their design are suitable for receiving radio signals. It is immaterial whether they are basic (simple) or complex, whether they incorporate amplification stages, and whether they are intended for use by children or adults. The tax does not apply to toys which are incapable of receiving any radio signals.

Because of the misinterpretation of Revenue Ruling 58–333 which is mentioned above, that ruling is hereby revoked.

Rev. Rul. 61–168

The manufacturers excise tax on radio and television components, imposed by section 4141 of the Internal Revenue Code of 1954, does not apply to sales by manufacturers, producers, or importers of

certain described amplifiers designed for use on aircraft in responding to, and directing, signals for the operation of aircraft instruments.

The Internal Revenue Service has been asked advice concerning the applicability of the manufacturers excise tax on radio and television components to sales of the amplifiers described below which are specially designed for use on aircraft in responding to, and directing signals for the operation of aircraft instruments.

(1) *A throttle servo amplifier.*—This device is a dual channel electric and magnetic unit designed to respond to signals from a flight path computer. In response to these signals, the amplifier feeds power to the throttle servos which are geared to drive the throttle mechanism of an aircraft.

(2) *An amplifier and signal generator.*—This unit consists essentially of a signal generator section and an amplifier section. The signal generator section contains a vertical gyro transmitter which generates signals in proportion to the displacement of an aircraft in pitch and bank, a rate gyro transmitter which generates signals in proportion to the rate of turn, and an altitude control transmitter which generates signals in proportion to the displacement from a selected pressure altitude. The amplifier section contains the amplifiers for the compass system and the servo channels. It is designed to increase a small voltage into a voltage capable of controlling a large amount of power. The small voltage is an extremely sensitive and delicate automatic pilot signal, which is the resultant of a series of signals generated in the various components of the system. This signal is increased in the amplifier to a power level sufficient to control torque motors which actuate the aircraft control surfaces. In general, the amplifier and signal generator is the nerve center of the automatic pilot system, for it processes all displacement signals into command signals for operating the control surfaces of the aircraft in order to maintain it on a selected heading reference.

(3) *A servo amplifier.*—This unit is a single-channel amplifier used in conjunction with a transmitter and a servoed indicator to form a sensitive remote indicating system. It is intended for use in a multiple installation where two, three, or four amplifiers can be installed on one shock-mount base. It is also manufactured in a model designed for use where a single amplifier is required.

(4) *A power distribution amplifier.*—This amplifier is designed to increase the power of a magnetic direction signal and for generating excitation for a master direction indicator motor and compass transmitter. A direction signal amplifier strip within the amplifier delivers control signals to the master direction indicator for conversion to a proportional shaft rotation, which provides a compass reading and signals for automatic pilot control. This unit furnishes the power supply for the excitation of the primary winding of the transmitter and of the fixed phase of the master direction indicator motor. It is manufactured in two models, one of which is a self-contained, plug-in unit.

(5) *A compass signal power amplifier.*—This amplifier consists of a mechanism assembly, a rectifier, a voltage amplifier, a phase inverter, and an output stage. It is a general-purpose power amplifier used in

systems in which a direction signal must be amplified to a magnitude sufficient to operate a mechanical device. This amplifier may be used in various systems such as navigational aids, automatic pilots, radar, fire control, and numerous other computers requiring compass or ship's heading signals fed into their circuits. It is said that the compass signal amplifier offers a means of furnishing isolated multiple take-offs which will not cause undue loading of the compass circuits.

Section 4141 of the Internal Revenue Code of 1954 imposes a tax upon the sale by the manufacturer, producer, or importer of certain enumerated articles including radio and television receiving sets, phonographs, combinations thereof, radio and television components, and phonograph records. Section 4142 of the Code defines the term "radio and television components" to mean, among other articles, amplifiers which are suitable for use on or in connection with, or as component parts of, any of the articles enumerated in section 4141 of the Code, whether or not primarily adapted for such use.

Section 48.4142–1(c)(5) of the Manufacturers and Retailers Excise Tax Regulations provides that the term "amplifiers" includes all apparatus for the amplification of audio frequency or video frequency impulses which are suitable for use on or in connection with, or as component parts of, any radio or television receiving set, phonograph, or combination of any of the foregoing. In accordance with section 48.4142–1(b) of the regulations, an item is suitable for use, within the meaning of section 4142 of the Code, if it is commonly used with any of the articles enumerated in section 4141 of the Code or if it possesses actual, practical commercial fitness for such use. It is immaterial whether the item is primarily adapted for such use.

The amplifiers described above, which are designed for use on aircraft in responding to and directing signals for the operation of aircraft instruments, are not considered to be suitable for use on or in connection with, or as component parts of, radio or television receiving sets or phonographs. Accordingly, it is held that sales by manufacturers of such amplifiers are not subject to the manufacturers excise tax on radio and television components imposed by section 4141 of the Code.

SECTION 4142.—DEFINITION OF RADIO AND TELEVISION COMPONENTS

26 CFR 48.4142–1: Radio and television components. Rev. Rul. 61–183

> A multiplex adapter which is designed for use with a frequency modulation (FM) radio tuner for the reception of stereophonic FM radio broadcasts and which contains an FM detector is a chassis within the meaning of section 4142 of the Internal Revenue Code of 1954. Accordingly, sales of such multiplex adapters are subject to the manufacturers excise tax on radio and television components, imposed by section 4141 of the Code.

Advice has been requested whether the manufacturers excise tax on radio and television components, imposed by section 4141 of the Internal Revenue Code of 1954, applies to sales of the multiplex adapters described below.

A manufacturer produces and sells multiplex adapters which are designed for use with frequency modulation (FM) radio tuners for the reception of stereophonic FM radio broadcasts utilizing the so-called "compatible" multiplex system. The multiplex adapter includes an FM detector and can be connected to any FM radio tuner that is equipped with a multiplex jack.

Generally, stereophonic programs which are broadcast under the "compatible" multiplex system are transmitted simultaneously by the same FM radio station on a primary or main channel and on a subchannel. For purposes of sound reproduction, a monophonic FM radio tuner can detect only the signals which are transmitted on the primary or main channel of the multiplex system. The second channel or sub-carrier signal is delivered by the tuner but at such frequencies as to be unusable by an audio amplifier.

The function of a multiplex adapter when used with an FM radio tuner is to detect or demodulate the sub-carrier signal and to deliver such signal in a form which is suitable for sound reproduction when transmitted to an audio amplifier. The combined output of the FM radio tuner and the multiplex adapter is fed into the audio stereophonic amplifier and then into speakers for stereophonic reproduction of the broadcast.

Section 4141 of the Code imposes a tax upon the sale by the manufacturer, producer, or importer of radio receiving sets, automobile radio receiving sets, television receiving sets, automobile television receiving sets, phonographs, combinations of any of the foregoing, radio and television components, and phonograph records (including in each case parts or accessories therefor sold on or in connection with the sale thereof).

Section 4142 of the Code provides that the term "radio and television components," as used in section 4141 of the Code, means, among other things, "chassis" which are suitable for use on or in connection with, or as component parts of, any of the articles enumerated in section 4141 of the Code, whether or not primarily adapted for such use.

Section 48.4142–1(c)(1) of the Manufacturers and Retailers Excise Tax Regulations provides that the term "chassis" includes any assembly of parts into circuits for the reception and conversion of radio or television signals into impulses suitable for the reproduction of (i) sound by a radio receiving set, or (ii) a picture, either with or without its associated sound, by a television receiving set.

A device falling within the foregoing tests is taxable without regard to what it may be called, *i.e.*, detector, adapter, converter, tuner, or by any other name. Thus, where an article is considered a "chassis" for purposes of the Code and regulations, it is not necessary that the article be functional without other equipment to be taxable.

The multiplex adapter described above contains an FM detector the function of which is to demodulate or convert the second carrier signal delivered by the FM tuner into impulses suitable for the reproduction of sound when such impulses are transmitted to the input of a stereophonic amplifier and thence to the speakers. Therefore, such a multiplex adapter is considered to be a chassis within the meaning of section 4142 of the Code.

Accordingly, it is held that sales of these multiplex adapters by the manufacturer, producer, or importer thereof are subject to the manufacturers excise tax on radio and television components imposed by section 4141 of the Code.

PART II.—MUSICAL INSTRUMENTS

SECTION 4151.—IMPOSITION OF TAX

26 CFR 48.4151–1: Imposition and rate of tax. Rev. Rul. 61–179

X corporation was organized for the purpose of importing electric chord organs into the United States. To this end, it entered into an agreement with a foreign supplier. Then, *Y* company was formed for the purpose of distributing all organs imported by *X*. Under a separate agreement between *X* and *Y*, the importation of the organs is financed by *Y*. *Y* determines the number of organs to be imported, and all right, title, and interest in and to the organs pass to *Y* prior to the time they are imported into this country. *Held*, *Y* is the importer of the organs for purposes of the manufacturers excise tax on musical instruments, imposed by section 4151 of the Internal Revenue Code of 1954, and is liable for the tax imposed by that section on its sales of the organs.

The Internal Revenue Service has been asked to determine whether *X* or *Y* is the importer of electric chord organs, for purposes of the manufacturers excise tax, under the circumstances described below.

X corporation was organized for the purpose of importing electric chord organs into the United States. To this end, an agreement was entered into with a foreign supplier. Among other things, the agreement provided that letters of credit would be established in favor of the foreign supplier's bank and that payment for the organs would be made upon the foreign supplier's presentation of shipping documents to the bank.

Subsequently, the organizing stockholders sold all of their *X* corporation stock to an unrelated individual and formed *Y* company for the purpose of selling the imported organs to local distributors.

Pursuant to this transaction, *X* and *Y* entered into an agreement which provided that *Y* would purchase all of the organs which would be imported under the agreement between *X* and the foreign supplier; that *Y* would determine the number of organs to be ordered each month; and that *Y* would advance to *X* such sums of money as would be required by *X* to support the letters of credit in connection with the purchase of the organs from the foreign supplier. To secure these advances, *X* assigned to *Y* all its right, title, and interest in and to the letters of credit and in and to all organs sold to *X* by the foreign supplier.

The agreement also provided that *Y* would pay to *X* for each organ an amount equal to the cost of the organ plus three percent of that cost. The establishment of that price was influenced by the fact that *Y* advanced funds to *X*. The organs are distributed under the trade name of *Y*.

Although the organs are shipped to *X* by the foreign supplier, they are delivered to the premises of *Y*. Consequently, *X* does not maintain any inventory of the organs, has no employees, and has no busi-

ness premises except desk space at which one of the officers keeps the necessary records of the corporation's transactions pursuant to its separate agreements with the foreign supplier and with *Y*.

Section 4151 of the Internal Revenue Code of 1954 imposes a tax upon the sale of musical instruments by the manufacturer, producer, or importer thereof.

In determining who is an importer for purposes of the manufacturers excise taxes, consideration must be given to the substance of the transaction. In the instant case, *X* corporation maintains no inventories, the importation of the organs is financed by *Y* company, and *Y* determines how many organs will be imported. All right, title, and interest in and to the organs pass to *Y* prior to the time they are imported into this country, and the organs are delivered to the premises of *Y*. Consequently, *Y* company, in effect, controls the importation.

Therefore, it is held that *Y* company is the importer of the organs for purposes of the manufacturers excise tax imposed by section 4151 of the Code and is liable for the tax imposed by that section on its sales of the organs.

SUBCHAPTER D.—RECREATIONAL EQUIPMENT

PART I.—SPORTING GOODS

SECTION 4161.—IMPOSITION OF TAX

26 CFR 48.4161–1: Imposition and rate of tax. Rev. Rul. 61–188

A company which purchases artificial fishing lures in a finished condition, imprints its trade name thereon, and attaches them to display cards, has not further manufactured the lures. Therefore, sales of such lures by the company are not subject to the manufacturers excise tax on sporting goods imposed by section 4161 of the Internal Revenue Code of 1954. However, where the company purchases lures in an unfinished condition, paints them, and adds feathers to them, the company has further manufactured the lures, and sales of such lures by the company are subject to the tax imposed by that section.

The Internal Revenue Service has been requested to determine, for purposes of the manufacturers excise tax on sporting goods, who is the manufacturer of the articles produced under the circumstances described below.

Among the articles sold by a company engaged in the business of selling fishing equipment are artificial lures. The company completely manufactures some of these lures in its own plant, but it also purchases both finished and unfinished lures from other suppliers.

In those instances in which the lures are purchased in a finished condition, the company imprints its trade name on the articles and attaches them to display cards also bearing its name. In instances in which the lures are purchased in an unfinished condition, the company paints them and adds feathers to them, before imprinting its trade name on the articles and attaching them to display cards also bearing its name.

Section 4161 of the Internal Revenue Code of 1954 imposes a tax upon the sale by the manufacturer, producer, or importer of certain enumerated articles of sporting goods (including in each case parts or accessories of such articles sold on or in connection therewith, or with the sale thereof). Included in the articles enumerated are "artificial lures, baits and flies."

Section 316.4(a) of Regulations 46, made applicable to the 1954 Code by Treasury Decision 6091, C.B. 1954–2, 47, defines the term "manufacturer" to include a person who produces a taxable article from scrap, salvage, or junk material, as well as from new or raw material, (1) by processing, manipulating, or changing the form of an article, or (2) by combining or assembling two or more articles.

In the situation described above wherein the company purchases artificial fishing lures in a finished condition and merely imprints its trade name on the lures and attaches them to display cards for resale in the same form, it is held that the company has not further manufactured the lures. Therefore, the company does not incur liability for the manufacturers excise tax on sporting goods imposed by section 4161 of the Code on its sales of such lures. The manufacturer who is subject to tax in this instance is the one who produced and sold the lures which were purchased by the company.

On the other hand, when the company purchases lures in an unfinished condition, paints them and adds feathers to them, it is held that the company has further manufactured the lures. Accordingly, the company incurs liability for the manufacturers excise tax imposed by section 4161 of the Code on its sales of such lures.

Rev. Rul. 61–189

A company which combines in a kit the components required for the assembling of artificial flies, is considered to be a manufacturer of artificial flies in a knockdown condition. The company's sales of these "fly-tying kits" are subject to the manufacturers excise tax on sporting goods imposed by section 4161 of the Internal Revenue Code of 1954. Where such kits are sold containing tools, the sales are considered to be combination sales of taxable artificial flies and nontaxable tools.

Advice has been requested concerning the applicability of the manufacturers excise tax on sporting goods to sales of so-called "fly-tying kits."

A company assembles and sells fly-tying kits for use by fishermen who wish to tie their own artificial flies. The kits vary in their contents, but generally they include such items as a vise, a paint brush, nylon winding thread, fly head cement, hooks, silk floss, wool yarn, wax, tinsel, turkey tails, duck quills, bucktail, neck hackles, peacock and other fancy feathers, and a supply of chenille. All of the kits contain sufficient components for assembling finished flies.

Section 4161 of the Internal Revenue Code of 1954 imposes a tax upon the sale by the manufacturer, producer, or importer of certain enumerated articles of sporting goods (including in each case parts or accessories of such articles sold on or in connection therewith, or with the sale thereof). Included in the articles enumerated are "artificial lures, baits and flies."

Section 316.4 of Regulations 46, made applicable to the 1954 Code by Treasury Decision 6091, C.B. 1954–2, 47, provides that the term "manufacturer" includes a person who produces a taxable article by combining or assembling two or more articles. That section 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.

Since the fly-tying kits described above contain the components required for assembling artificial flies, it is considered that the kits contain complete artificial flies in a knockdown condition. Therefore, the person who produces such kits is a manufacturer of artificial flies within the meaning of section 4161 of the Code.

Accordingly, it is held that sales of these kits by the manufacturer thereof are subject to the manufacturers excise tax on sporting goods imposed by section 4161 of the Code. However, the sales of kits containing tools, such as a vise and a paint brush which are used in assembling the flies, are combination sales of artificial flies in a knockdown condition and nontaxable tools, and the tax does not apply to that portion of the sales price which is attributable to the sales of the nontaxable tools.

The manufacturers excise tax on combination sales should be computed in accordance with the methods which are outlined in Revenue Ruling 59–16, C.B. 1959–1, 340, among other Revenue Rulings.

Rev. Rul. 61–190

A company which supplies tools and materials to fabricators for the production of artificial flies and acquires the completed flies from such fabricators is considered to be the manufacturer of the flies for purposes of the manufacturers excise tax on sporting goods imposed by section 4161 of the Internal Revenue Code of 1954, even though there is no written agreement requiring the fabricators to deliver the completed flies to the company.

The Internal Revenue Service has been requested to determine, for purposes of the manufacturers excise tax on sporting goods, who is the manufacturer of artificial flies which are manufactured under the circumstances described below.

A company, which manufactures and sells fishing equipment, acquires certain artificial flies from fabricators who produce the flies in their own homes. All tools and materials used in producing the flies are furnished by the company without charge to the fabricators. All the finished flies are acquired from the fabricators by the company.

There is no written agreement under which the fabricators are required to deliver the finished flies to the company. The consideration for which the flies are transferred to the company reflect the reduced costs incurred by the fabricators by reason of the fact that the tools and materials are supplied by the company.

Section 4161 of the Internal Revenue Code of 1954 imposes a tax upon the sale by the manufacturer, producer, or importer of certain enumerated articles of sporting goods (including in each case parts or accessories of such articles sold on or in connection therewith, or with the sale thereof). Included in the articles enumerated are "artificial lures, baits and flies."

Section 316.4(b) of Regulations 46, made applicable to the 1954 Code by Treasury Decision 6091, C.B. 1954–2, 47, provides that under certain circumstances, as where a person manufactures or produces a taxable article for a person who furnishes materials and retains title thereto, the person for whom the taxable article is manufactured or produced, and not the person who actually manufactures or produces it, will be considered the manufacturer.

Revenue Ruling 60–42, C.B. 1960–1, 474, holds, in part, that among the factors to be considered in determining whether a fabricator or his vendee is liable for the manufacturers excise tax are (1) the ownership of the raw materials used in producing the articles and (2) who has the right to control the production and sale of the article.

In the ordinary course of trade, materials and tools are not furnished to a fabricator without a requirement for some consideration, expressed or implied. The facts in this case clearly indicate that there is an implied agreement that the materials are furnished with the understanding that the finished flies will be delivered by the fabricators to the company at a price dictated by the company. The only apparent constraint the company may bring to bear to compel the fabricators to deliver the finished flies to the company is the threat of discontinuance of the arrangement under which the tools and materials are furnished by the company. Nevertheless, this constraint is real and effective, and it is considered sufficient to warrant the conclusion that the company controls the production and sale of the flies it obtains from the fabricators. Furthermore, by furnishing in the manner stated the materials from which the flies are produced, the company retains a property right therein during the entire period of fabrication and until the flies are sold.

Accordingly, it is held that the company is the manufacturer of the artificial flies within the meaning of section 4161 of the Code, and its sales of the flies produced by the fabricators are subject to the manufacturers excise tax on sporting goods imposed by that section.

SUBCHAPTER E.—OTHER ITEMS

PART I.—BUSINESS MACHINES

SECTION 4191.—IMPOSITION OF TAX

26 CFR 48.4191–1: Imposition and rate of tax. Rev. Rul. 61–169

A device which is designed for use by telephone installation men for printing or stamping numbers on the discs which are inserted in the center of telephone instrument dials is a "numbering machine" for purposes of the manufacturers excise tax imposed by section 4191 of the Internal Revenue Code of 1954.

The Internal Revenue Service has been asked whether the number printing or stamping device which is described below is a "numbering machine" for purposes of the manufacturers excise tax imposed by section 4191 of the Internal Revenue Code of 1954.

The portable, manually operated device is designed for use by telephone instrument installation men for printing or stamping numbers on the card-type discs which are inserted in the center of telephone

instrument dials. It is designed to print numbers containing up to seven digits in a single line.

The device consists of a base, an inverted "U" shaped frame, a figure-wheel mechanism, a plunger which extends through the top of the frame and is connected to the wheel mechanism, and a built-in ink pad which automatically inks the numbering surface after each imprint. When the plunger is depressed, the wheel mechanism moves downward and prints a predetermined number on the disc which has been placed under the device.

The figure-wheel mechanism includes seven independently operated metal wheels, each containing the digits "0" through "9" and a blank space for use when printing numbers of less than seven digits. In addition, the first wheel contains the letter "E," the second wheel contains the letter "X," and the third wheel contains the letter "T." Thus, in addition to its use for printing numbers containing up to seven digits, the device may be used for printing the abbreviation for "extension" along with numbers containing up to four digits.

The device does not have a mechanism for automatically advancing the wheel settings, since relatively few numbers are printed in advancing order in the particular use for which the device is designed. Instead, an outside knob, or dial, is connected to each of the last five wheels, permitting the quick selection of the numbers to be printed by those five wheels. Since the setting of the first two wheels is changed infrequently in normal use, those wheels are reset by using a stylus. Once the device is set for printing a particular number (or the combination of "EXT" and a number), it may be used without resetting for printing that number as many times as desired.

Section 4191 of the Code imposes a tax upon the sale by the manufacturer, producer, or importer of certain enumerated articles or any combination thereof (including in each case parts or accessories of such articles sold on or in connection therewith, or with the sale thereof). Included among the enumerated articles are "numbering machines."

The primary issue in this case is whether a device is considered to be outside the scope of the term "numbering machines" because of the fact that it is not equipped to automatically advance the wheel settings so as to print numbers in consecutive order. Although many "numbering machines" are equipped to automatically print numbers in consecutive order, in duplicate, in triplicate, etc., the absence of that feature from a device, such as the one described in the instant case, is not an adequate basis for concluding that it is nontaxable. Basically, the device is a machine which is designed to perform a numbering function.

Accordingly, it is held that the device described in the instant case is a "numbering machine" which is subject to the manufacturers excise tax imposed by section 4191 of the Code when sold by the manufacturer, producer, or importer.

Rev. Rul. 61–176

A stencil dispensing machine which is used to dispense so-called "tab-on" stencils is not subject to the manufacturers excise tax on business machines imposed by section 4191 of the Internal Revenue Code of 1954.

Advice has been requested whether the manufacturers excise tax on certain business machines, imposed by section 4191 of the Internal

Revenue Code of 1954, applies to sales by the manufacturer of the stencil dispensing machine described below.

The stencil dispensing machine is similiar to a tape dispensing machine in design and operation. It is used to dispense a so-called "tab-on" stencil, which is a combination of tape and stencil material with a carbon backing. This material is contained in the machine in roll form. By manually pressing a lever, the machine feeds out a predetermined length of tape and stencil material and cuts it to the desired length. The material is then tabbed onto a business form, such as a bill of lading or shipping order, over the "ship to" address area to permit the user to cut the stencil as a by-product of the form writing operation. The machine is primarily used in the shipping operations and shipping departments of industries that require multiple addressing on their individual shipments.

Section 4191 of the Code imposes a tax upon the sale by the manufacturer, producer, or importer of certain enumerated business machines.

Stencil dispensing machines are not specifically included in the list of business machines enumerated in section 4191 of the Code, nor do they come within the general classification of any of the articles which are enumerated in that section. Accordingly, it is held that sales by the manufacturer, producer, or importer of the stencil dispensing machine described above are not subject to the manufacturers excise tax imposed by section 4191 of the Code.

Applicability of the manufacturers excise tax on business machines to a "one-time charge" made by a manufacturer for making alterations or additions to a taxable business machine at the time the machine is originally leased. See Rev. Rul. 61–155, below.

SUBCHAPTER F.—SPECIAL PROVISIONS APPLICABLE TO MANUFACTURERS TAX

SECTION 4216.—DEFINITION OF PRICE

(Also Sections 4191, 4217; 26 CFR 48.4191–1.) Rev. Rul. 61–155

A manufacturer of taxable business machines leases those machines to various customers. The manufacturer does not make any sales of the machines. Upon originally leasing a machine, a customer requests the manufacturer to make certain changes or additions to the basic machine so that it will perform certain special operations for that customer. Although there is no increase in the monthly lease payments for the altered machine, the manufacturer bills the customer a "one-time charge" for the alterations. This charge includes costs attributable to material, labor, overhead, and a margin of profit. *Held*, under the provisions of section 4217(a) and section 4216(c) of the Internal Revenue Code of 1954, the manufacturers excise tax on business machines, imposed by section 4191 of the Code, applies to the

full amount of the "one-time charge" made by the manufacturer for the special changes or additions to the machine, as well as to the monthly payments under the lease.

SECTION 4217.—LEASES

Whether, for purposes of the exemption from the manufacturers excise tax on certain leases of business machines directly to the United States, provided by the Secretary's Authorization effective January 1, 1959, C.B. 1959–1, 769, the manufacturer-lessor must be engaged at the time of making the lease in the business of selling in arm's length transactions the same type and model of business machine. See Rev. Rul. 61–144, page 202.

Applicability of the manufacturers excise tax on business machines to a "one-time charge" made by a manufacturer for making alterations or additions to a taxable business machine at the time the machine is originally leased. See Rev. Rul. 61–155, page 189.

SUBCHAPTER G.—EXEMPTIONS, REGISTRATION, ETC.

SECTION 4221.—CERTAIN TAX-FREE SALES

(Also Section 4061; 26 CFR 40.4061(b)–1.) Rev. Rul. 61–197

The exemption from the manufacturers excise tax provided by section 4221(a)(1) of the Internal Revenue Code of 1954 does not apply to sales by manufacturers of automobile seat covers (1) to automobile dealers for resale by them with new or used automobiles, (2) to operators of automobile service stations for resale by them to their customers, (3) to fleet owners or other persons for use by them in their business automobiles, or (4) to automobile owners for use in the replacement of upholstery damaged by fire or collision.

Advice has been requested whether the transactions described in the situations set forth below, with respect to automobile seat covers, come within the scope of the exemption from the manufacturers excise tax on taxable articles sold for use in further manufacture, provided by section 4221(a)(1) of the Internal Revenue Code of 1954.

Situation (1). Manufacture and sale of seat covers to automobile dealers for resale by them with new or used automobiles.

Situation (2). Manufacture and sale of seat covers to operators of automobile service stations for resale by them to their customers.

Situation (3). Manufacture and sale of seat covers to fleet owners or other persons for use in their business automobiles.

Situation (4). Manufacture and sale of seat covers to automobile owners for use in the replacement of upholstery damaged by fire or collision.

Section 4061(b) of the Code imposes a tax on the sale by the manufacturer, producer, or importer of automobile parts or accessories, with certain exceptions not here material. Automobile seat

covers come within the classification of taxable parts or accessories. See S.T. 944, C.B. 1952–2, 225, as clarified by Revenue Ruling 54–330, C.B. 1954–2, 409.

Section 4220 of the Code, prior to its amendment by Public Law 367, C.B. 1955–2, 768, provided, in part, an exemption from the manufacturers excise tax with respect to the sale of any article (1) for use by the vendee as material in the manufacture or production of, or as a component part of, *an article subject to the manufacturers excise tax*, or (2) for resale by the vendee for such use by his vendee, if such article was in due course so resold. Public Law 367, effective September 1, 1955, amended section 4220 of the Code to extend the exemption to sales of certain articles, including automobile parts or accessories, sold for use as material in the manufacture of *any article*, irrespective of whether the end article is taxable.

The Excise Tax Technical Changes Act of 1958, Public Law 85–859, C.B. 1958–3, 92, effective January 1, 1959, amended section 4220 and redesignated it as part of section 4221 of the Code. Section 4221(a)(1) of the Code provides that, under regulations prescribed by the Secretary of the Treasury or his delegate, no manufacturers excise tax shall be imposed on the sale by the manufacturer of an article for use by the purchaser for further manufacture, or for resale by the purchaser to a second purchaser for use by such second purchaser in further manufacture, but only if such use is to occur before any other use. Section 4221(d)(6)(B) of the Code provides, in part, that an article shall be treated as sold for use in further manufacture if, in the case of a part or accessory taxable under section 4061(b), such article is sold for use by the purchaser as material in the manufacture or production of, or as a component part of, another article to be manufactured or produced by him.

Senate Report No. 1162, 84th Congress, C.B. 1955–2, 884, relating to H.R. 7024 which became Public Law 367, indicates that Congress intended to adopt a single rule exempting parts or accessories only where they are sold or resold to manufacturers for incorporation in other end articles, whether or not such end articles are taxable. It was not intended, however, that the exemption should be extended to articles sold for repair and replacement use or sold for any other use which does not constitute further manufacture.

None of the purchasers involved here are manufacturers. Accordingly, it is held that the transactions referred to above are not covered by the exemption provided by section 4221(a)(1) of the Code.

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26 CFR 40.4220–1: Exemption for sales or resales for further manufacture. Rev. Rul. 61–171

A manufacturer of marine type outboard motors equipped with electric starting devices advertises and sells to its dealers complete motors including automotive type storage batteries. It purchases the batteries from a battery manufacturer but does not include them in shipments to its dealers. Instead, each shipment of an outboard motor includes a form of certificate which authorizes any of the battery manufacturer's warehouses to deliver a battery to the dealer on behalf of the outboard motor manufacturer. The reason for this

procedure is to provide the ultimate purchaser of the motor with a fresh battery. *Held*, a manufacturer of automotive batteries may sell batteries tax-free for use by outboard motor manufacturers as material in the manufacture or production of, or as a component part of outboard motors, when sold and delivered in the manner and under the circumstances outlined above. Such sales may be made tax-free only when the parties to the sales meet the registration and procedural requirements of section 148.1–3 of the temporary rules relating to registration requirements for certain tax-free sales. These rules were published as Treasury Decision 6344, C.B. 1959–1, 776, and were amended by Treasury Decision 6463, C.B. 1960–1, 872.

SECTION 4222.—REGISTRATION

26 CFR 148.1–3: Temporary procedures for tax-free sales and purchases.

Registration requirements in the case of gasoline sold for use by the purchaser for nonfuel purposes as a material in the manufacture of other articles. See T.D. 6574, page 162.

SECTION 4226.—FLOOR STOCKS TAXES

26 CFR 48.4226: Statutory provisions; floor stocks taxes. T. D. 6569 [1]

TITLE 26—INTERNAL REVENUE.—CHAPTER I, SUBCHAPTER D, PART 48.—MANUFACTURERS AND RETAILERS EXCISE TAXES

Regulations under section 4226 of the Internal Revenue Code of 1954, relating to 1961 floor stocks taxes on certain tires, inner tubes, and tread rubber.

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

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

Section 206 (a) and (b) of the Federal-Aid Highway Act of 1961 (75 Stat. 127) [P.L. 87–61, page 309, this Bulletin], amended section 4226 of the Internal Revenue Code of 1954 to impose floor stocks taxes on tires, inner tubes, and tread rubber held on July 1, 1961, by dealers and certain other persons. The following regulations amending the Manufacturers and Retailers Excise Tax Regulations (26 CFR Part 48) are hereby prescribed relating to such floor stocks taxes:

PARAGRAPH 1. Section 48.4226, relating to floor stocks taxes, is amended by adding after paragraph (5) of section 4226(a) new paragraphs (6) and (7) and by revising subsection (d) of section 4226 and the historical note. Section 48.4226, as so amended and revised, reads as follows:

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[1] 26 F.R. 7771.

§ 48.4226 STATUTORY PROVISIONS; FLOOR STOCKS TAXES.

SEC. 4226. FLOOR STOCKS TAXES.

(a) IN GENERAL.—

* * * * * * *

(5) 1959 TAX ON GASOLINE.—On gasoline subject to tax under section 4081 which, on October 1, 1959, is held by a dealer for sale, there is hereby imposed a floor stocks tax at the rate of 1 cent a gallon. The tax imposed by this paragraph shall not apply to gasoline in retail stocks held at the place where intended to be sold at retail, nor to gasoline held for sale by a producer or importer of gasoline.

(6) 1961 TAXES ON CERTAIN TIRES AND INNER TUBES.—On tires subject to tax under section 4071(a)(1), and on inner tubes subject to tax under section 4071(a)(3), which, on July 1, 1961, are held—

(A) By a dealer for sale,

(B) For sale on, or in connection with, other articles held by the manufacturer, producer, or importer of such other articles, or

(C) For use in the manufacture or production of other articles,

there is hereby imposed a floor stocks tax at the rate of 2 cents a pound in the case of such tires, and a floor stocks tax at the rate of 1 cent a pound in the case of such inner tubes. The taxes imposed by this paragraph shall not apply to any tire or inner tube which is held for sale by the manufacturer, producer, or importer of such tire or tube, or which will be subject under section 4218(b) or 4219 to the manufacturers excise tax on tires or inner tubes. The tax on inner tubes imposed by this paragraph shall not apply to inner tubes for bicycle tires (as defined in section 4221(e)(4)(B)).

(7) 1961 TAX ON TREAD RUBBER.—On tread rubber subject to tax under section 4071(a)(4) which, on July 1, 1961, is held by a dealer, there is hereby imposed a floor stocks tax at the rate of 2 cents a pound. The tax imposed by this paragraph shall not apply in the case of any person if such person establishes, to the satisfaction of the Secretary or his delegate, that all tread rubber held by him on July 1, 1961, will be used otherwise than in the recapping or retreading of tires of the type used on highway vehicles (as defined in section 4072(c)).

(b) OVERPAYMENT OF FLOOR STOCKS TAXES.—Section 6416 shall apply in respect of the floor stocks taxes imposed by this section, so as to entitle, subject to all provisions of section 6416, any person paying such floor stocks taxes to a credit or refund thereof for any of the reasons specified in section 6416.

(c) MEANING OF TERMS.—For purposes of subsection (a), the terms "dealer" and "held by a dealer" have the meaning assigned to them by section 6412(a)(4).

(d) DUE DATE OF TAXES.—The taxes imposed by subsection (a) shall be paid at such time after September 30, 1956, as may be prescribed by the Secretary or his delegate; except that the tax imposed by paragraph (5) shall be paid at such time after December 31, 1959, as may be prescribed by the Secretary or his delegate, and except that the taxes imposed by paragraphs (6) and (7) shall be paid at such time after September 30, 1961, as may be prescribed by the Secretary or his delegate.

[Sec. 4226 as added and in effect Jan. 1, 1959, and as amended by sec. 201(c) (1), (2) and (3) of the Federal-Aid Highway Act of 1959 (73 Stat. 614) [P.L. 86-342, C.B. 1959-2, 697]: by sec. 206 (a) and (b) of the Federal-Aid Highway Act of 1961 (75 Stat. 127) [P.L. 87-61, page 309, this Bulletin].]

PAR. 2. The following section is added immediately after § 48.4226-8:

§ 48.4226-9 1961 FLOOR STOCKS TAXES ON TIRES, INNER TUBES, AND TREAD RUBBER.—(a) *Scope of tax.*—(1) *In general.*—A floor stocks tax is imposed on any article subject to tax under the following sections of the Internal Revenue Code which is held for sale or other specific disposition at the first moment of July 1, 1961, by a dealer or certain other persons (see paragraph (b) of this section):

(i) Section 4071(a)(1) (relating to tires of the type used on highway vehicles),

(ii) Section 4071(a)(3) (relating to inner tubes for tires), and

(iii) Section 4071(a)(4) (relating to tread rubber).

The taxes are imposed on articles held in inventory for sale or other specified disposition, without regard to their sale or other disposition. The taxes do not apply to articles held by the manufacturer, producer, or importer of such articles.

(2) *Dealer.*—A dealer for purposes of the floor stocks taxes on tires and inner tubes includes a wholesaler, jobber, distributor, or retailer. In the case of tread rubber, a dealer includes any person (other than the manufacturer, producer, or importer thereof) who holds such tread rubber for sale or use.

(3) *Held by a dealer.*—(i) An article subject to floor stocks tax is regarded as held by a dealer if title to the article has passed to the dealer (whether or not delivery has been made), and if, for purposes of consumption, title to or possession of such article has not at any time been transferred to any person other than a dealer. For example, the tax applies to tires in inventory which have been pledged as security for a loan by the dealer even though he has transferred title or possession to the lender as of July 1, 1961.

(ii) If the dealer has title to an article, the article is considered to be held by him even though it is in transit, in storage, or at a distribution point. Where title does not pass until delivery, articles in transit at the first moment of July 1, 1961, are regarded as held by the shipper at that time.

(b) *Application of tax.*—(1) *Highway tires and certain inner tubes.*—(i) The floor stocks tax applies to tires of the type used on highway vehicles which are highway motor vehicles, such as automobiles, trucks, buses, highway tractors, and motorcycles, and on vehicles such as trailers (including house trailers) and semitrailers of the type used in connection with highway motor vehicles. For the purpose of the regulations under this section, the term "highway tires" means "tires of the type used on highway vehicles" as defined in section 4072(c). The floor stocks tax applies to inner tubes for any type of tire, except a bicycle tire (as defined in section 4221(e)(4)(B)). It is immaterial whether the tire with which the inner tube may be used is or is not of the highway type. Highway tires and inner tubes are subject to the tax if held at the first moment of July 1, 1961, (*a*) by a dealer for sale; (*b*) by a manufacturer, producer, or importer for sale on, or in connection with, other articles manufactured, produced, or imported by him and held by him; or (*c*) for use in the manufacture or production of other articles. Thus, a manufacturer, producer, or importer of vehicles incurs liability for the floor stocks tax on highway tires and inner tubes which are mounted on vehicles held by him for sale or which are held by him in inventory for use in the manufacture or production of vehicles.

(ii) The tax does not apply to tires and inner tubes which at the first moment of July 1, 1961, are actually mounted on a vehicle held for sale by a person who is not the manufacturer, producer, or importer of the vehicle. The tax does not apply to used tires or inner tubes as such or to recapped tires, unless the recapping has been from bead to bead so that the original tire has lost its identity. The tax does not apply to tires which are neither of the type used on highway motor vehicles nor of the type used on vehicles of the type used in connection with highway motor vehicles. The tax does not apply to bicycle tires. The tax does not apply to tires and inner tubes held for sale by the manufacturer, producer, or importer of such tires and inner tubes. Further, the floor stocks tax does not apply to any tires or inner tubes which will be subject under section 4218(b) or 4219 to the manufacturers excise tax on tires or inner tubes.

(iii) The tax applies to tires and inner tubes which are made wholly or in part of rubber, including synthetic or substitute rubber.

(iv) The tax is computed on the total weight of the tire or the inner tube, including fractional parts of a pound, but excluding metal rims or rim bases in the case of tires.

(v) Any person liable for the floor stocks tax on tires and inner tubes may be guided by schedules furnished by the manufacturer, producer, or importer of such tires and inner tubes as to the taxable weight of the tires and inner tubes which are subject to floor stocks tax provided such schedules are based upon the latest method of determination of weight of tires and inner tubes as approved by the Commissioner. This schedule may also be used as a guide to determine the tires of the highway type subject to floor stocks tax.

(2) *Tread rubber.*—(i) The floor stocks tax applies to tread rubber held at the first moment of July 1, 1961, by any person (other than the manufacturer, producer, or importer of tread rubber) for either sale or use.

(ii) The term "tread rubber" means any material (a) which is commonly or commercially known as tread rubber or camelback, or (b) which is a substitute for any material commonly or commercially known as tread rubber or camelback and is of a type used in recapping or retreading tires. The term includes, for example, strips of material, wholly or partially of rubber, natural or synthetic, intended to be vulcanized or otherwise affixed to a tire casing to form the outside perimeter of the tire, smooth or treaded. It further includes treading material produced by reprocessing scrap, salvage, or junk rubber. Tread rubber loses its identity as such when it has been used in the recapping or retreading of a tire.

(iii) Any person (other than the manufacturer, producer, or importer of the tread rubber) who holds tread rubber for sale or use at the first moment of July 1, 1961, incurs liability for the tax on such tread rubber and must report and pay the tax thereon unless he establishes that all the tread rubber held by him at such time will be used for a purpose other than the recapping or retreading of highway tires. If any of the tread rubber held by such person is to be used in the recapping or retreading of highway tires, the tax applies to all the tread rubber held by him at the first moment of July 1, 1961. However, credit or refund of the tax may be claimed, as provided in sections 4226(b) and 6416 of the Code, by the person paying the tax

with respect to tread rubber which is used or resold for use other than in the recapping or retreading of highway tires. See paragraph (g) of this section relating to credit or refund of floor stocks tax.

(c) *Rates of tax.*—The rates of the floor stocks taxes are:

(1) *Highway tires and inner tubes.*—Two cents per pound on the total weight of the highway tire and 1 cent per pound on the total weight of the inner tube. See paragraph (b)(1) (iv) and (v) of this section for determining the weight on which tax is computed.

(2) *Tread rubber.*—Two cents per pound on the total weight of the tread rubber.

(d) *Inventory.*—(1) Every person liable for the floor stocks tax on highways tires, inner tubes, or tread rubber shall prepare an inventory of such articles held at the first moment of July 1, 1961, and shall retain such inventory at his principal place of business. Persons holding articles subject to the tax at more than one location shall prepare a separate inventory, in duplicate, for each location. One copy of the separate inventory shall be retained at such location and one copy shall be kept at the principal place of business of the taxpayer. Each inventory shall show the name of the taxpayer, the location of the particular premises for which the inventory is made, and the address shown on the tax return. The inventories shall not be filed with the return but shall be retained by the taxpayer.

(2) The inventory shall consist of the following information with respect to articles subject to tax:

(i) The trade name, grade, size, number of plies, and weight of highway tires.

(ii) The trade name, grade, size, and weight of inner tubes.

(iii) The crown width, gauge, and weight of tread rubber.

(e) *Requirements with respect to return.*—(1) *Form.*—Every person liable for the floor stocks taxes on highway tires, inner tubes, or tread rubber shall make a return of such tax on Form 3174.

(2) *Place for filing returns by persons other than corporations.*—The return of a person other than a corporation shall be filed with the district director of internal revenue for the district in which is located the principal place of business or legal residence of such person. If such person has no principal place of business or legal residence in any internal revenue district, the return shall be filed with the District Director at Baltimore, Maryland, except as provided in subparagraph (4) of this paragraph.

(3) *Place for filing returns by corporations.*—The return of a corporation shall be filed with the district director for the district in which is located the principal place of business or principal office or agency of the corporation, except as provided in subparagraph (4) of this paragraph.

(4) *Returns of taxpayers outside the United States.*—The return of a person (other than a corporation) outside the United States having no legal residence or principal place of business in any internal revenue district, or the return of a corporation outside the United States having no principal place of business or principal office or agency in any internal revenue district, shall be filed with the Director, Office of International Operations, Internal Revenue Service, Washington 25, D.C.

(f) *Time for filing return and paying tax.*—The return, with remittance of the tax due, shall be filed on or before October 15, 1961. The tax is due and payable without assessment or notice. For additions to the tax for failure to file a return within the prescribed time, see section 6651 and § 301.6651–1 of this chapter (Regulations on Procedure and Administration).

(g) *Credit or refund.*—A claim on Form 843 for credit or refund may be filed by any person who makes an overpayment of the floor stocks tax. Any person who has paid a floor stocks tax may be entitled to a credit or refund of the tax for any of the reasons specified in section 6416 and subject to all the conditions provided in such section. Thus, for example, credit or refund may be allowed, subject to the conditions provided in section 6416(a), where the highway tire, inner tube, or tread rubber is used or sold for use for certain purposes specified (1) in section 6416(b)(2)(A), relating to exportation; (2) in section 6416(b)(2)(C), relating to exclusive use of a State or local government; (3) in section 6416(b)(2)(D), relating to exclusive use of a nonprofit educational organization; (4) in section 6416(b)(2)(F) or 6416(b)(3)(C), relating to a tire or inner tube resold for use or used on or in connection with the exportation or exempt sale of another article; or (5) in section 6416(b)(2)(L), relating to use or resale for use of tread rubber otherwise than in the recapping or retreading of highway tires as defined in paragraph (b) of this section.

(h) *Records.*—(1) *Inventories.*—Every person liable for floor stocks taxes shall maintain records of the separate inventories required by paragraph (d) of this section.

(2) *Copies of returns and other relevant papers and material.*—Every person liable for floor stocks taxes shall keep a duplicate copy of the return, together with other relevant papers and material.

(3) *Records of claimants.*—Any person claiming refund, credit or abatement of the tax, interest, additional amount, addition to the tax or assessable penalty, shall keep a complete and detailed record with respect to the claim.

(4) *Place and period for keeping records.*—(i) All records required by the regulations in this section shall be kept, by the person required to keep them, at a convenient and safe location within the United States which is accessible to internal revenue officers. Such records shall at all times be available for inspection by such officers. If such person has a principal place of business in the United States, the records shall be kept at such place of business.

(ii) Records required by subparagraphs (1) and (2) of this paragraph shall be maintained for a period of at least 3 years after the date the tax becomes due or the date the tax is paid, whichever is the later. Records required by subparagraph (3) of this paragraph (including any record required by subparagraph (1) or (2) of this paragraph which relates to the claim) shall be maintained for a period of at least 3 years after the date the claim is filed.

Because this Treasury Decision relates to floor stocks taxes imposed on highway tires, inner tubes, and tread rubber held at the first moment of July 1, 1961, 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 such Act.

MORTIMER M. CAPLIN,
Commissioner of Internal Revenue.

Approved August 15, 1961.

STANLEY S. SURREY,
Assistant Secretary of the Treasury.

(Filed by the Division of the Federal Register on August 18, 1961, 8:47 a.m., and published in the issue of the Federal Register for August 19, 1961, 26 F.R. 7771)

CHAPTER 33.—FACILITIES AND SERVICES

SUBCHAPTER C.—TRANSPORTATION OF PERSONS

SECTION 4261.—IMPOSITION OF TAX

26 CFR 49.4261: Statutory provisions; imposition of tax.

Postponement from July 1, 1961 to July 1, 1962, of the scheduled reduction in the rate tax on amounts paid for the transportation of persons. See T.D. 6574, page 162.

26 CFR 49.4261–2: Rate and application of tax. Rev. Rul. 61–140

> Where a helicopter rental company furnishes helicopters with pilots to an oil exploration company for the transportation of its employees and charges a per diem charge plus a fixed hourly charge for actual flying time, and the helicopter is flown with passengers only a part of the time covered by the per diem charge, the excise tax on the transportation of persons, imposed by section 4261 of the Internal Revenue Code of 1954, applies to that portion of the per diem charge and the hourly charge which is allocable to time spent flying passengers.

Advice has been requested concerning the application of the excise tax on the transportation of persons to payments made to a helicopter rental company under the circumstances described below.

A helicopter rental company furnishes helicopters with pilots to an oil exploration company for the transportation of employees to and from oil well sites. The contract stipulates a per diem charge over the duration of the contract period plus an additional fixed hourly charge for actual flying time. The contract also stipulates that the flying period shall be restricted to daylight flying. A record of the exact flying time (which is tabulated by a clocking device in each helicopter) is retained by the helicopter company. The company bills its customer monthly for two amounts, one for the fixed per diem charge and the other for the actual time in flight.

Section 4261 of the Internal Revenue Code of 1954 imposes a tax of 10 percent upon the amount paid within the United States for taxable transportation of any person by rail, motor vehicle, water, or air.

Section 49.4261–2(d) of the Facilities and Services Excise Tax Regulations provides that where a payment covers charges for nontransportation services as well as for transportation of a person, the charges for the nontransportation services may be excluded in computing the tax payable with respect to such payment, provided such charges are separable and are shown in the exact amounts thereof in the records pertaining to the transportation charge. If the charges for nontransportation services are not separable from the charge for transportation of the person, the tax must be computed upon the full amount of the payment.

Where a helicopter rental company furnishes a helicopter with pilot under a contract which includes a per diem charge and a fixed hourly charge for actual flying time, and the helicopter is flown with passengers during the entire period covered by the per diem charge, the total per diem payment and the additional hourly payment constitute amounts paid for taxable transportation. However, if the helicopter is flown with passengers for only a portion of the time covered by the per diem charge, a transportation service is being furnished during that portion of the time only. Therefore, only that portion of the total payment allocable to transporting passengers constitutes an amount paid for taxable transportation.

Accordingly, in the instant case, it is held that the tax on the transportation of persons applies to that portion of the per diem charge and the fixed hourly charge which is allocable to the flying of passengers, provided such allocation is made on a fair and reasonable basis and can be supported by proper records. If no allocation is made, the tax applies to the total payment made to the helicopter company. See Rev. Rul. 60–311, C.B. 1960–2, 341.

This conclusion may be illustrated by an example in which the helicopter company bills its customer for a 30-day month at a per diem rate of $100, or a total per diem charge of $3,000. During this month the actual flying time was 100 hours. At the rate of $75 per hour, the total hourly charge for the month is $7,500. However, the records of the company show that only 60 hours flying time was spent in flying passengers. During this month the daily daylight flying period, under the terms of the contract, was approximately 13 hours; therefore, the per diem charge may be allocated at the rate of $7.69 per hour ($100 divided by 13 hours). The amount of the tax on transportation of persons should be computed as follows:

Per diem charge—30 days @ $100 per day	$3,000.00
Additional hourly charge—100 hours total flight time @ $75 per hour	7,500.00
Total charge (exclusive of tax)	10,500.00
Portion of per diem charge attributable to the transportation of persons—60 hours flight time transporting persons @ $7.69 per hour	461.40
Hourly charge for flight time transporting persons—60 hours @ $75 per hour	4,500.00
Total per diem and hourly charge allocable to the transportation of persons	4,961.40
Tax—10 percent of $4,961.40	496.14

It should be noted, however, that section 4263(f) of the Code provides an exemption from the tax on the transportation of persons for certain small aircraft when operated on nonestablished lines.

Rev. Rul. 61–172

Under the terms of a contract between a boat owner and an oil company, the boat owner furnished boats with crews to transport the oil company's employees to and from offshore oil well sites. The boats were in a "stand-by" or "waiting" status during a portion of the time covered by a specified daily charge for each boat. In addition to this basic daily charge, the oil company furnished the fuel and oil supplies necessary to operate the boats. *Held,* for purposes of the excise tax on the transportation of persons, the oil company's cash payments of the specified daily charges may be allocated between transportation services and nontransportation services. However, the value of the fuel and oil supplies furnished is attributable only to the transportation services.

Advice has been requested concerning the application of the excise tax on the transportation of persons to payments made under the circumstances described below.

Under the terms of a contract between a boat owner and an oil company, the boat owner furnished boats with crews and transported the oil company's employees to and from offshore oil well sites. Although it was known that there would be varying portions of each day during which the boats would be in a "stand-by" or "waiting" status rather than in use in transporting employees, the contract provided for a specified daily charge for each boat. This daily charge was determined by the size of the boat and was not affected by the portion of the time during which the boat might be in a "stand-by" or "waiting" status. In addition to this daily charge, the contract further provided that the oil company would furnish the fuel and oil supplies necessary to operate the boats.

The boat owner submitted to the oil company periodic statements covering only the specified daily charges referred to above. These amounts were paid in cash to the boat owner by the oil company. The statements contained no allocation of the charges between transportation services and nontransportation services. Likewise, they contained no billing of the excise tax on transportation of persons The oil company kept a record of the value of the fuel and oil supplies furnished for the operation of the boats.

The question presented is whether, based upon the circumstances described below, a portion of the amounts paid by the oil company may be considered nontaxable on the basis of having been attributable to nontransportation services.

An analysis of the boat owner's log records relating to the boats used indicates the percentage of the total time during which the boats were in "stand-by" or "waiting" status. It has been proposed that this percentage be applied to the total payments made by the oil company (including both the cash payments made in response to the periodic billing and the value of the fuel and oil supplies furnished) and that the resulting portion of the total payments be considered as having been paid for nontransportation services.

Section 4261(a) of the Internal Revenue Code of 1954 imposes a tax upon the amount paid within the United States for taxable transportion of any person by rail, motor vehicle, water, or air.

Section 49.4261–2(d) of the Facilities and Services Excise Tax Regulations provides that where a payment covers charges for nontransportation services as well as for transportation of a person, the charges for the nontransportation services may be excluded in computing the tax payable with respect to such payment, provided such charges are separable and are shown in the exact amounts thereof in the records pertaining to the transportation charge. If the charges for nontransportation services are not separable from the charge for transportation of the person, the tax must be computed upon the full amount of the payment.

Among several examples of payments not subject to the tax, section 49.4261–8(f)(5) of the regulations includes charges in connection with the charter of a land, water, or air conveyance for the transportation of persons, such as for parking, icing, sanitation, "layover" or "waiting time," movement of equipment in deadhead service, dockage, wharfage, etc.

Under the circumstances of the instant case, charges for "stand-by" or "waiting" time are considered to be charges for nontransportation services within the meaning of the regulations. See Revenue Ruling 61–140, page 198, this Bulletin, which holds that the tax applies only to that portion of the charges for a helicopter transportation service which is allocable to the time spent in flying passengers.

Generally, any allocation of charges between transportation services and nontransportation services should be made prior to rendering statements to the person who is to pay for the transportation services, in order that the proper amount of tax may be computed and paid at the prescribed time. However, in determining the application of the tax to the amounts which already have been paid under the circumstances of this case, allocation may be made on the basis of acceptable records which clearly show the portion of the total payments allocable to nontransportation services. Assuming that there is no question regarding the authenticity of the log records from which the percentage of "stand-by" or "waiting" time has been determined, it will be acceptable to apply that percentage to those payments which are properly allocable. Under the circumstances outlined above, the oil company's cash payments of the specified daily charges are properly allocable to the transportation of the employees and to "stand-by" or "waiting" time.

However, none of the value of the fuel and oil supplies is allocable to "stand-by" or "waiting" time. This is because the nature of those supplies and the agreement pertaining thereto indicate that they are attributable to the time during which the boats are performing a transportation function rather than to the time during which the boats are in a "stand-by" or "waiting" status.

Accordingly, under the circumstances of this case, it is held that the cash payments by the oil company may be allocated between transportation services and nontransportation services but that the value of fuel and oil supplies furnished by the oil company is attributable in its entirety to transportation services.

SUBCHAPTER E.—SPECIAL PROVISIONS APPLICABLE TO SERVICES AND FACILITIES TAXES

SECTION 4293.—EXEMPTION FOR UNITED STATES AND POSSESSIONS

(Also Section 4217.) Rev. Rul. 61–144

Pursuant to the authority granted by section 4293 of the Internal Revenue Code of 1954, the Secretary of the Treasury has authorized exemption from the manufacturers excise tax imposed by section 4191 of the Code on any payment made under leases of business machines directly to the United States for its exclusive use to which section 4217(b) of the Code is applicable. See Secretary's Authorization which is effective as of January 1, 1959, C.B. 1959–1, 769.

Section 4217(b) of the Code provides certain limitations upon the amount of tax to be paid in the case of any lease by the manufacturer, producer, or importer of an article which is subject to the manufacturers excise tax. However, section 4217(d)(1) of the Code provides that subsection (b) shall not apply to any lease of an article unless at the time of making the lease, or any prior lease of such article to which subsection (b) applies, the person making the lease or prior lease was also engaged in the business of selling in arm's length transactions the same type and model of article.

Held, the exemption provided by the Secretary's Authorization does not apply to payments made with respect to a taxable business machine leased to the United States unless, at the time of making the lease or prior lease, the manufacturer-lessor was also engaged in the business of selling in arm's length transactions the same type and model of business machine. Where the exemption does not apply under these circumstances, the tax is to be computed under the provisions of section 4216(c) of the Code.

CHAPTER 34.—DOCUMENTARY STAMP TAXES

SUBCHAPTER A.—ISSUANCE OF CAPITAL STOCK AND CERTIFICATES OF INDEBTEDNESS BY A CORPORATION

PART I.—ISSUANCE OF CAPITAL STOCK AND SIMILAR INTERESTS

SECTION 4303.—EXEMPTIONS

Rev. Rul. 61–184

The exemption from the documentary stamp tax provided by section 4303(c) of the Internal Revenue Code of 1954 applies to the issuance of "periodic payment plan" certificates of beneficial interest for the accumulation of shares of stock of a mutual investment fund, even though, upon completion or earlier termination of the plan, the investor has an option to receive cash in lieu of the shares purchased for his account. However, the exemption does not apply to the issuance of certificates under a single-payment "fully paid plan."

Advice has been requested whether the exemption from the documentary stamp tax provided by section 4303(c) of the Internal Revenue Code of 1954 applies to the issuance of "periodic payment plan" certificates of beneficial interest for the accumulation of shares of stock of a mutual investment fund corporation under the circumstances described below.

A company, referred to here as the "Sponsor," under the terms of an agreement with another company, the "Custodian," offers certain investment plans whereby the investors' payments are used for the accumulation of shares of stock of a designated mutual investment fund, referred to here as the "Fund." The plan certificates of beneficial interest are considered to be "shares or certificates issued by a corporation" for purposes of the documentary stamp tax.

Under a "periodic payment" plan, the investor makes an initial payment along with an application for an investment program in a certain amount. Upon acceptance by the Sponsor, a plan certificate is issued in the face amount of the program chosen in the application. Under the terms set forth in the certificate, the investor agrees to pay to the Custodian a specified amount periodically (usually monthly) during the term of the plan (10 to 15 years), the total investment to equal the face amount of the certificate. The certificate provides that the net amount of the investor's payments (after certain deductions for distribution costs and management fees) are to be invested by the Custodian in shares of the Fund for the account of the investor. All dividends or distributions (less authorized charges) with respect to Fund shares held for the account of the investor are to be applied to the purchase of additional Fund shares for the investor's account unless the investor elects to receive such dividends or distributions in cash. The investor may complete his payments in less than the full term of the plan by making advance payments.

The investor may terminate the plan at any time by surrendering his certificate to the Custodian. Upon completion or earlier termination of the plan, the investor has a right to receive the Fund shares held for his account or to instruct the Custodian to sell his Fund shares and to remit to him the net proceeds less authorized deductions. In the absence of such instructions, the Custodian will deliver the Fund shares to the investor. Therefore, the receipt of cash rather than shares is at the discretion of the investor and not the Sponsor or the Custodian. However, where Fund shares are to be delivered to the investor, the Custodian may sell sufficient shares to pay authorized deductions and may remit cash to the investor in lieu of fractional shares.

The specific question with respect to the above-described periodic payment plan is whether the fact that the investor has an option to receive cash in lieu of shares precludes the applicability of the exemption provided by section 4303(c) of the Code.

In addition to this periodic payment plan, the Sponsor offers a single-payment "fully paid" plan, under which the investor makes a single payment in an amount equal to the face amount of the certificate applied for. No further payments by the investor are required under this plan. Otherwise, the provisions of the fully paid plan are

the same as the provisions of the periodic payment plan. The specific question with respect to the fully paid plan is whether the fact that dividends or distributions (less authorized charges) with respect to Fund shares may, at the investor's option, be applied to the purchase of additional shares for the investor's account is sufficient to characterize the plan as "an installment purchase agreement."

Section 4301 of the Code, as amended by the Excise Tax Technical Changes Act of 1958, Public Law 85–859, C.B. 1958–3, 92, effective January 1, 1959, and by Public Law 86–416, C.B. 1960–1, 786, effective April 9, 1960, imposes, on each original issue of shares or certificates of stock issued by a corporation, a tax at the rate of ten cents on each $100 (or major fraction thereof) of the actual value of the certificates (or of the shares where no certificates are issued), except that such rate shall be four cents instead of ten cents in the case of shares or certificates issued by a corporation to which subchapter M of chapter 1 applies for the taxable year during which such share or certificate is issued. The tax imposed by this section is computed on the basis of all certificates (or shares) so issued by the corporation on each day.

Section 4303(c) of the Code, as added by the Excise Tax Technical Changes Act of 1958, provides that the tax imposed by section 4301 shall not apply to shares or certificates issued by a corporation pursuant to an installment purchase agreement which provides that (1) the periodic payments by the purchaser will be applied (as received by the corporation) solely to the acquisition of shares or certificates in specified other corporations (and in specified percentages), and (2) the corporation will transfer to the purchaser, on or before the termination of the agreement, all shares or certificates in other corporations acquired by it for the purchaser.

The exemption provided by section 4303(c) of the Code would not apply to a situation of the type described if the Sponsor or the Custodian, under the terms of the agreement with the investor, had an option to distribute cash in lieu of the shares of stock purchased for the account of the investor. However, where the Sponsor and the Custodian are obligated, as in this case, to deliver the Fund shares to the investor unless the investor chooses to receive cash, the applicability of the exemption is not precluded by the fact that the investor may exercise his discretion to receive cash in lieu of the shares Furthermore, the discretionary authority of the investor is not changed by the fact that the Custodian may sell sufficient shares to pay authorized deductions and may remit cash to the investor in lieu of fractional shares.

Accordingly, it is held that, under the circumstances described, the exemption provided by section 4303(c) of the Code applies to the issuance of certificates under the periodic payment plan.

On the other hand, the fully paid plan is not considered to be an installment purchase agreement merely because the dividends or distributions may, at the investor's option, be applied to the purchase of additional shares for the investor's account. Therefore, it is further held that the fully paid plan certificates do not come within the scope of the exemption provided by section 4303(c) of the Code.

PART II.—ISSUANCE OF CERTIFICATES OF INDEBTEDNESS

SECTION 4311.—IMPOSITION OF TAX

26 CFR 43.4311–1: Imposition of tax on issuance of certificates of indebtedness. Rev. Rul. 61–212

A change in the obligor of outstanding bonds, effected by a reorganization agreement and a supplemental indenture, constitutes such a material change in the obligations as to create a new issue subject to the documentary stamp tax under section 4311 of the Internal Revenue Code of 1954.

Advice has been requested whether a change in the obligor of outstanding bonds, under the circumstances described below, constitutes such a material change in the obligations as to create a new issue which is subject to the documentary stamp tax imposed by section 4311 of the Internal Revenue Code of 1954.

Corporations *X*, *Y*, and *Z* entered into an agreement and plan of reorganization pursuant to which the properties, assets, and businesses of *Y* and *Z* were acquired by corporation *M*, a newly-formed wholly-owned subsidiary of *X*. *M* became liable for the obligations of *Y* and *Z*, including certain outstanding long-term mortgage bonds issued by *Y*. Accordingly, under the terms of a supplemental indenture, *M* agreed to pay the principal and interest with respect to the mortgage bonds on substantially the same terms as under the original indenture. By express exoneration, the supplemental indenture relieves *Y*, its shareholders, officers and employees from liability under the bonds. The former assets of *Y* continue to be subject to the mortgage securing the bonds; however, the holder of the bonds has agreed, and the supplemental indenture provides, that none of the former assets of *Z* are subject to the operation of the indenture.

Section 4311 of the Code provides that a tax shall be imposed on all certificates of indebtedness issued by a corporation.

The applicability of the documentary stamp tax in the instant case depends upon whether the transaction constitutes such a material change in the obligation under the bonds as to create a new issue. Revenue Ruling 54–60, C.B. 1954–1, 241, holds that a change in the interest rate of outstanding bonds, effected by a consolidation agreement, constitutes such a material change as to create a new issue. On the other hand, Revenue Ruling 58–49, C.B. 1958–1, 457, holds that a mere agreement to change a mortgage bond arrangement so as to make payments on a first and a second mortgage on the same date does not constitute such a material change in the mortgage bond as to make it taxable as a new issue.

In the instant case, a new entity becomes obligated under the terms of the supplemental indenture, the former obligor being no longer liable. The original debt is discharged, and there is a new and different promise to pay. The original creditor-debtor relationship no longer exists, since that relationship is now between the lender and a new and different party. The effect of this transaction is the same as if a new bond had been issued by *M* corporation.

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Accordingly, it is held that the change in the obligor of outstanding bonds, in the manner described above, constitutes such a material change in the obligations as to create a new issue which is subject to the documentary stamp tax imposed by section 4311 of the Code.

CHAPTER 36.—CERTAIN OTHER EXCISE TAXES

SUBCHAPTER B.—OCCUPATIONAL TAX ON COIN-OPERATED DEVICES

SECTION 4462.—DEFINITION OF COIN-OPERATED AMUSEMENT OR GAMING DEVICE

26 CFR 45.4462–1: Definition of coin-operated amusement or gaming devices. Rev. Rul. 61–130

One-ball pinball machines are considered to be gaming devices subject to the $250.00 annual occupational tax imposed by section 4461(a)(2) of the Internal Revenue Code of 1954, whether or not evidence exists as to actual payoffs.

Advice has been requested whether one-ball pinball machines are "amusement devices" or "gaming devices" for purposes of the occupational tax on coin-operated devices.

Upon insertion of a coin in a device of this type, one ball is released to the player who propels it, by means of a plunger, across the playing surface. As the ball hits various bumpers located on the playing surface, the score is registered on the backboard. Many of these machines have been altered by the removal of the push button and meter, or the provision for multiple coin insertion for increasing the odds, and it is contended, therefore, that they do not fall within the scope of either Revenue Ruling 59–294, C.B. 1959–2, 340, or Revenue Ruling 60–102, C.B. 1960–1, 555.

Section 4461(a) of the Internal Revenue Code of 1954 imposes a special tax to be paid by every person who maintains for use or permits the use of, on any place or premises occupied by him, a coin-operated amusement or gaming device. This tax is imposed at the rate of $10.00 a year in the case of a device defined in paragraph (1) of section 4462(a), and at the rate of $250.00 a year in the case of a device defined in paragraph (2) of section 4462(a).

As defined in paragraph (1) of section 4462(a) of the Code, the term "coin-operated amusement device" includes any machine which is an amusement machine operated by the insertion of a coin, token, or similar object, but not including any device defined in paragraph (2) of that section. As defined in paragraph (2) of that section, the term "coin-operated gaming device" includes any machine which is a so-called "slot" machine which operates by means of the insertion of a coin, token, or similar object and which, by application of the element of chance, may deliver, or entitle a person playing or operating the machine to receive, cash, premiums, merchandise, or tokens.

Section 45.4462–1(b)(2) of the Miscellaneous Stamp Tax Regulations lists several examples of machines or devices coming within the scope of section 4462(a)(2) of the Code, including the following:

(i) A machine which is operated by means of the insertion of a coin, token, or similar object and which, even though it does not dispense cash or tokens, has the features and characteristics of a gaming device whether or not evidence exists as to actual payoffs.

The question whether a particular coin-operated device is a coin-operated gaming device is to be determined from the features, characteristics, and functioning of the device, and when it is peculiarly adaptable to use for gambling purposes, it is a coin-operated gaming device notwithstanding the fact that evidence fails to disclose its actual use for gambling purposes.

Operation of one-ball pinball machines is considered to be essentially comparable with that of slot machines of the lever type, which come within the purview of the above-mentioned section 45.4462–1(b)(2) of the regulations as coin-operated gaming devices. Generally speaking, the profitable operation of such slot machines depends upon the appeal to the player's desire to risk the element of chance in order to win something of value, as distinguished from the mere satisfaction and pleasure that might come from watching the reels of the machines spin. Therefore, such machines are, by their very nature, peculiarly adapted for gambling purposes. Pulling the handle, which causes the spinning of the reels in a slot machine, is comparable to shooting a single ball across the playing surface of a one-ball pinball machine.

Accordingly, since one-ball pinball machines have the features and characteristics of a gaming device, they are held to be coin-operated gaming devices within the meaning of section 4462(a)(2) of the Code, whether or not evidence exists as to actual payoffs. Any person who maintains for use, or permits the use of, such a machine on premises occupied by him is liable for the $250 special tax on coin-operated gaming devices.

SUBCHAPTER D.—TAX ON USE OF CERTAIN VEHICLES

SECTION 4482.—DEFINITIONS

26 CFR 41.4482(c)–1: Definition of State, year, and use. Rev. Rul. 61–173

Section 4481(a) of the Internal Revenue Code of 1954 imposes a tax on the use of certain highway motor vehicles. Section 4482(c)(3) of the Code defines the term "use" to mean use in the United States on the public highways. Section 41.4482(c)–1(c) of the Highway Motor Vehicle Use Tax Regulations further defines the term "use" to mean the operation of the vehicle, by means of its own motor, on any roadway (whether a Federal highway, State highway, city street, or otherwise) in the United States which is not a private roadway. *Held*, the use of a water truck by a highway construction contractor in the construction of a new freeway on land which has not been used as a public roadway does not constitute a taxable "use" for purposes of the highway motor vehicle use tax. However, the movement of the water truck, by means of its own motor, over any public roadway, such as from one construction site to another, does constitute a taxable "use" of the vehicle.

CHAPTER 37.—SUGAR, COCONUT AND PALM OIL

SUBCHAPTER A.—SUGAR

SECTION 4501—IMPOSITION OF TAX

26 CFR 46.4501: Statutory provisions; imposition of tax.
(Also Section 6412; 46.6412(d).)

T.D. 6578[1]

TITLE 26—INTERNAL REVENUE.—CHAPTER I. SUBCHAPTER D. PART 46.—REGULATIONS RELATING TO MISCELLANEOUS EXCISE TAXES PAYABLE BY RETURN

Amendments to excise tax regulations relating to the tax on sugar.

DEPARTMENT OF THE TREASURY,
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 the Regulations Relating to Miscellaneous Excise Taxes Payable by Return (26 CFR Part 46) to the appropriate sections of the Act of March 31, 1961 (Public Law 87–15, 75 Stat. 40 C.B. 1961–1, 855), such regulations are amended as follows:

PARAGRAPH 1. Section 46.4501 is amended by revising section 4501(c), and the historical note, to read as follows:

§ 46.4501 STATUTORY PROVISIONS; IMPOSITION OF TAX.

SEC. 4501. IMPOSITION OF TAX * * *

(c) TERMINATION OF TAX.—No tax shall be imposed under this subchapter on the manufacture, use, or importation of sugar or articles composed in chief value of sugar after December 31, 1962. Notwithstanding the provisions of subsections (a) or (b), no tax shall be imposed under this subchapter with respect to unsold sugar held by a manufacturer on December 31, 1962, or with respect to sugar or articles composed in chief value of sugar held in customs custody or control on such date.

[Sec. 4501 as amended by sec. 19, Act of May 29, 1956 (Pub. Law 545, 84th Cong., 70 Stat. 221 [C.B. 1956–1, 887]); sec. 162(b), Excise Tax Technical Changes Act 1958 (72 Stat. 1306 [C.B. 1958–3, 124]); sec. 2, Act of July 6, 1960 (Pub. Law 86–592, 74 Stat. 330 [C.B. 1960–2, 685]); sec. 2(a), Act of March 31, 1961 (Pub. Law 87–15, 75 Stat. 40 [C.B. 1961–1, 855])]

PAR. 2. Section 46.6412(d) is amended by revising section 6412(d), and the historical note, to read as follows:

§ 46.6412(d) STATUTORY PROVISIONS; FLOOR STOCK REFUNDS.

SEC. 6412. FLOOR STOCKS REFUNDS * * *

(d) SUGAR.—With respect to any sugar or articles composed in chief value of sugar upon which tax imposed under section 4501(b) has been paid and which, on December 31, 1962, are held by the importer and intended for sale or other disposition, there shall be refunded (without interest) to such importer, subject to such regulations as may be prescribed by the Secretary or his delegate, an amount equal to the tax paid with respect to such sugar or articles, composed in chief value of sugar, if claim for such refund is filed with the Secretary or his delegate on or before March 31, 1963.

[1] 26 F.R. 10128.

[Sec. 6412(d) as amended by sec. 19, Act of May 29, 1956 (Pub. Law 545, 84th Cong., 70 Stat. 221); sec. 162(a), Excise Tax Technical Changes Act 1958 (72 Stat. 1306); sec. 2, Act of July 6, 1960 (Pub. Law 86-592, 74 Stat. 330); sec. 2(b), Act of March 31, 1961 (Pub. Law 87-15, 75 Stat. 40)]

Because this Treasury Decision makes only the necessary technical changes in the statutory provisions to reflect the amendments to the Internal Revenue Code contained in the Act of March 31, 1961, it is hereby found 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 section 7805 of the Internal Revenue Code of 1954 (68A Stat. 917; 26 U.S.C. 7805).)

WILLIAM H. LOEB,
Acting Commissioner of Internal Revenue.

Approved October 24, 1961.

STANLEY S. SURREY,
Assistant Secretary of the Treasury.

(Filed by the Division of the Federal Register on October 27, 1961, 8:47 a.m., and published in the issue of the Federal Register for October 28, 1961, 26 F.R. 10128)

CHAPTER 39.—REGULATORY TAXES

SUBCHAPTER A.—NARCOTIC DRUGS AND MARIHUANA

PART I.—NARCOTIC DRUGS

Subpart A.—Tax on Opium, Isonipecaine, Opiates, and Coca Leaves

SECTION 4702.—EXEMPTIONS

REGULATIONS 5, 26 CFR 151.428: Pharmaceutical preparations designated as Class "X" products.

TITLE 26—INTERNAL REVENUE.—CHAPTER I, PART 151.—REGULATORY TAXES ON NARCOTIC DRUGS

Excepted narcotic pharmaceutical preparations

On June 6, 1961, a notice was published in the Federal Register (26 F.R. 5016) stating that the Commissioner of Narcotics, pursuant to the provisions of section 4702(a) of the Internal Revenue Code of 1954, as amended by section 4(c) of the Narcotics Manufacturing Act of 1960 (74 Stat. 58) [P.L. 86-429, C.B. 1960-1, 789], proposed that pharmaceutical preparations in liquid form containing not more than 2.5 mgs. diphenoxylate and not less than 25 micrograms atropine sulfate per dosage unit be designated as Class "X" products.

After due notice and opportunity for public hearing, and after consideration of all relevant matters, it is hereby found that pharmaceutical preparations in liquid form containing not more than 2.5 mgs. diphenoxylate and not less 25 micrograms atropine sulfate per

dosage unit do not possess an addiction-forming or addiction-sustaining liability sufficient to warrant imposition of all the requirements of the Federal narcotic laws and do not permit recovery of a narcotic drug having an addiction-forming or addiction-sustaining liability, with such relative technical simplicity and degree of yield as to create a risk of improper use. Such preparations are hereby designated as Class "X" products subject to such requirements as are indicated for Class "X" products in 26 CFR 151.421–151.428.

Subparagraph (6) of § 151.428(a) is amended by adding the words "or liquid" following the word "solid" and as so amended, reads as follows:

§ 151.428 EXEMPT NARCOTIC PHARMACEUTICAL PREPARATIONS.—(a) *Pharmaceutical preparations designated as Class "X" products.* * * *

(6) Pharmaceutical preparations in solid or liquid form containing not more than 2.5 mgs. diphenoxylate and not less than 25 micrograms atropine sulfate per dosage unit. (26 U.S.C. 4702(a), as amended by sec. 4(c), Pub. Law 86-429 (74 Stat. 58) [C.B. 1960–1, 789], sec. 17, Pub. Law 86-429 (74 Stat. 67).)

[SEAL] HENRY L. GIORDANO,
Acting Commissioner of Narcotics.

Approved July 18, 1961.

A. GILMORE FLUES,
Assistant Secretary of the Treasury.

(Filed by the Division of the Federal Register on July 24, 1961, 8:50 a.m., and published in the issue of the Federal Register for July 25, 1961, 26 F.R. 6619)

Subpart D.—General Provisions Relating to Narcotic Drugs

SECTION 4731.—DEFINITIONS

21 CFR 305.2: Chronological list of findings. T. D. 62 (Narcotics) [1]

TITLE 21—FOOD AND DRUGS.—CHAPTER II, BUREAU OF NARCOTICS, DEPARTMENT OF THE TREASURY, PART 305.—OPIATES

Finding of certain drugs to be opiates

On July 4, 1961, a notice was published in the Federal Register (26 F.R. 6001) stating that the Commissioner of Narcotics pursuant to the provisions of section 4731(g) of the Internal Revenue Code of 1954 (26 U.S.C. 4731(g)), as amended by section 4(b) of the Narcotics Manufacturing Act of 1960 (74 Stat. 57), and pursuant to 21 CFR 305.1, proposed that a finding be made that certain drugs possess an addiction-forming or addiction-sustaining liability similar to morphine or are capable of conversion into drugs having an addiction-forming or addiction-sustaining liability similar to morphine with relative technical simplicity and degree of yield as to create a risk of improper use, and are opiates.

After due notice and opportunity for public hearing and after consideration of all relevant matters presented, the substances referred to in the proposed findings as so published are hereby proclaimed as opiates.

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[1] 26 F.R. 7760.

PARAGRAPH 1. Part 305 is amended by adding a new § 305.2 *Chronological list of findings*, for the purpose of listing chronologically the substances proclaimed by the Commissioner of Narcotics as opiates, as follows:

§ 305.2 CHRONOLOGICAL LIST OF FINDINGS.

August 8, 1961

Betamethadol (B-4,4-diphenyl-6-dimethylamino-3-heptanol or B-6-dimethylamino-4,4-diphenyl-3-heptanol).
Etoxeridine (1-[2-(2-hydroxyethoxy)-ethyl]-4-phenylpiperidine-4-carboxylic acid ethyl ester) (Atenorax, Atenos, Carbetidine).
Levomoramide (1-3-methyl-2,2-diphenyl-4-morpholino-butyryl-pyrrolidine).
Racemoramide (d,l-3-methyl-2,2-diphenyl-4-morpholino-butyryl-pyrrolidine).
Trimeperidine (1,2,5-trimethyl-4-phenyl-4-propionoxypiperidine) (Promedol).
Phenoperidine (1-(3-hydroxy-3-phenylpropyl)-4-phenylpiperidine-4-carboxylic acid ethyl ester).

Because the addition of § 305.2 is merely for the purpose of listing the substances proclaimed by the Commissioner of Narcotics as opiates, 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.

EFFECTIVE DATE.—This Treasury Decision shall become effective upon its filing for publication in the Federal Register.

(26 U.S.C. 4731(g), as amended by sec. 4(b), Pub. Law 86-429 (74 Stat. 57) [C.B. 1960-1, 789]; sec. 17, Pub. Law 86-429 (74 Stat. 67).)

[SEAL] HENRY L. GIORDANO,
Acting Commissioner of Narcotics.

Approved August 14, 1961.

A. GILMORE FLUES,
Assistant Secretary of the Treasury.

(Filed by the Division of the Federal Register on August 18, 1961, 8:47 a.m., and published in the issue of the Federal Register for August 19, 1961, 26 F.R. 7760)

T. D. 64 (Narcotics)[1]

TITLE 21—FOOD AND DRUGS.—CHAPTER II, BUREAU OF NARCOTICS, DEPARTMENT OF THE TREASURY, PART 305.—OPIATES

Noracymethadol found to be an opiate

On September 2, 1961, a notice was published in the Federal Register (26 F.R. 8322) stating that the Commissioner of Narcotics pursuant to the provisions of section 4731(g) of the Internal Revenue Code of 1954 (26 U.S.C. 4731(g)), as amended by section 4(b) of the Narcotics Manufacturing Act of 1960 (74 Stat. 57), and pursuant to 21 CFR 305.1, proposed that a finding be made that the drug known as Noracymethadol (α-dl-3-acetoxy-6-methylamino-4,4-diphenyl heptane) possesses an addiction-forming or addiction-sustaining liability similar to morphine or is capable of conversion into a drug having an addiction-forming or addiction-sustaining liability similar to morphine with relative technical simplicity and degree of yield as to create a risk of improper use and is an opiate.

[1] 26 F.R. 9715.

After due notice and opportunity for public hearing and after consideration of all relevant matters presented, Noracymethadol (α-dl-3-acetoxy-6-methylamino-4,4-diphenyl heptane) is hereby proclaimed an opiate.

Section 305.2 is amended by adding a new drug to the chronological list of findings, as follows:

§ 305.2 CHRONOLOGICAL LIST OF FINDINGS.

October 5, 1961

Noracymethadol (α-dl-3-acetoxy-6-methylamino-4,4-diphenyl heptane)

Because the amendment of § 305.2 is merely for the purpose of listing the substance proclaimed by the Commissioner of Narcotics as an opiate, 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.

Effective date.—This Treasury Decision shall become effective upon its filing for publication in the Federal Register.

(26 U.S.C. 4731(g), as amended by sec. 4(b), Public Law 86-429 (74 Stat. 57) [C.B. 1960-1,789]; sec. 17, Public Law 86-429 (74 Stat. 67))

[SEAL] WAYLAND L. SPEER,
Acting Commissioner of Narcotics.

Approved October 11, 1961.

A. GILMORE FLUES,
Assistant Secretary of the Treasury.

(Filed by the Division of the Federal Register on October 13, 1961, 8:50 a.m., and published in the issue of the Federal Register for October 13, 1961, 26 F.R. 9715)

CHAPTER 52.—TOBACCO, CIGARS, CIGARETTES, AND CIGARETTE PAPERS AND TUBES

SUBCHAPTER A.—DEFINITIONS; RATE AND PAYMENT OF TAX; EXEMPTION FROM TAX; AND REFUND AND DRAWBACK OF TAX

SECTION 5704.—EXEMPTION FROM TAX

26 CFR 280.121: Tobacco materials released from customs custody. T.D. 6571[1]

TITLE 26—INTERNAL REVENUE.—CHAPTER I, SUBCHAPTER E, PART 280.—DEALERS IN TOBACCO MATERIALS

Importation procedures

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

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

On June 7, 1961, a notice of proposed rule making to amend 26 CFR Part 280 was published in the Federal Register (26 F.R. 5070).

[1] 26 F.R. 8198.

The purposes of the proposal were to delete provisions relating to the release of imported tobacco materials from customs custody, without payment of tax, for delivery to dealers in tobacco materials, since improved procedures concerning such operations are being concurrently incorporated in proposed regulations in 26 CFR Part 275, and also to make certain editorial and conforming changes.

No data, views, or arguments pertaining to these regulations were received during the period of 30 days from the date of publication of the notice of proposed rule making. Accordingly, the regulations so published are hereby adopted without change.

§ 280.12 [Deletion]

1. Section 280.12 is deleted.

§ 280.13 [Deletion]

2. Section 280.13 is deleted.

§ 280.15 [Deletion]

3. Section 280.15 is deleted.

§ 280.21 [Deletion]

4. Section 280.21 is deleted.

§ 280.24 [Deletion]

5. Section 280.24 is deleted.

§ 280.29 [Deletion]

6. Section 280.29 is deleted.

§ 280.30 [Deletion]

7. Section 280.30 is deleted.

§ 280.32 [Deletion]

8. Section 280.32 is deleted.

9. Section 280.33 is amended to read:

§ 280.33 TOBACCO MATERIALS.—"Tobacco materials" shall mean tobacco other than manufactured tobacco, cigars, and cigarettes, and includes tobacco in process, Perique, Black Fat, leaf tobacco, and tobacco scraps, cuttings, clippings, siftings, stems, and waste. Tobacco materials are categorized:

(a) *Unstemmed leaf tobacco.*—Leaf tobacco from which the stem or midrib has not been removed.

(b) *Other tobacco materials.*—Tobacco materials other than unstemmed leaf tobacco.

10. Section 280.43 and the heading are amended to read as follows:

§ 280.43 ALTERNATE METHODS OR PROCEDURES.—A dealer in tobacco materials, on specific approval by the Director as provided in this section, may use an alternate method or procedure in lieu of a method or procedure specifically prescribed in this part. The Director may approve an alternate method or procedure, subject to stated conditions, when he finds that—

(a) good cause has been shown for the use of the alternate method or procedure,

(b) the alternate method or procedure is within the purpose of, and consistent with the effect intended by, the specifically prescribed method or procedure, and affords equivalent security to the revenue, and

(c) the alternate method or procedure will not be contrary to any provision of law, and will not result in an increase in cost to the Government or hinder the effective administration of this part.

No alternate method or procedure relating to the giving of any bond, or to the assessment, payment, or collection of tax, shall be authorized under this section. Where a dealer desires to employ an alternate method or procedure, he shall submit a written application to do so, in triplicate, to the assistant regional commissioner for transmittal to the Director. The application shall specifically

describe the proposed alternate method or procedure, and shall set forth the reasons therefor. Alternate methods or procedures shall not be employed until the application has been approved by the Director. The dealer shall, during the period of authorization of an alternate method or procedure, comply with the terms of the approved application. Authorization for any alternate method or procedure may be withdrawn whenever in the judgment of the Director the revenue is jeopardized or the effective administration of this part is hindered. The dealer shall retain, as part of his records, any authorization of the Director under this section.

11. A new section designated, § 280.43a is added, to read:

§ 280.43a EMERGENCY VARIATIONS FROM REQUIREMENTS.—The Director may approve methods of operation other than as specified in this part, where he finds that an emergency exists and the proposed variations from the specified requirements are necessary, and the proposed variations—

(a) will afford the security and protection to the revenue intended by the prescribed specifications,

(b) will not hinder the effective administration of this part, and

(c) will not be contrary to any provision of law.

Variations from requirements granted under this section are conditioned on compliance with the procedures, conditions, and limitations set forth in the approval of the application. Failure to comply in good faith with such procedures, conditions, and limitations shall automatically terminate the authority for such variations and the dealer thereupon shall fully comply with the prescribed requirements of regulations from which the variations were authorized. Authority for any variations may be withdrawn whenever in the judgment of the Director the revenue is jeopardized or the effective administration of this part is hindered by the continuation of such variation. Where a dealer desires to employ such variation, he shall submit a written application to do so, in triplicate, to the assistant regional commissioner for transmittal to the Director. The application shall describe the proposed variations and set forth the reasons therefor. Variations shall not be employed until the application has been approved. The dealer shall retain, as part of his records, any authorization of the Director under this section.

12. Section 280.101 and the heading are amended to read:

§ 280.101 DEPOSIT OF SECURITIES IN LIEU OF CORPORATE SURETY.—In lieu of corporate surety the dealer in tobacco materials may pledge and deposit, as security for his bond, securities which are transferable and are guaranteed as to both interest and principal by the United States, in accordance with the provisions of 31 CFR Part 225. (61 Stat. 650, 72 Stat. 1421; 6 U.S.C. 15, 26 U.S.C. 5711.)

13. Section 280.108 and the heading are amended to read:

§ 280.108 RELEASE OF PLEDGED SECURITIES.—Securities of the United States pledged and deposited as provided in § 280.101 shall be released only in accordance with the provisions of 31 CFR Part 225. Such securities will not be released by the assistant regional commissioner until liability under the bond for which they were pledged has been terminated. When the assistant regional commissioner is satisfied that they may be released, he shall fix the date or dates on which a part or all of such securities may be released. At any time prior to the release of such securities, the assistant regional commissioner may extend the date of release for such additional length of time as he deems necessary. (61 Stat. 650, 72 Stat. 1421; 6 U.S.C. 15, 26 U.S.C. 5711.)

14. Section 280.121 is amended to read:

§ 280.121 TOBACCO MATERIALS RELEASED FROM CUSTOMS CUSTODY.—The release of tobacco materials from customs custody, without payment of tax, for delivery to a dealer in tobacco materials, shall be in accordance with the provisions of Part 275 of this chapter. (72 Stat. 1418; 26 U.S.C. 5704.)

This Treasury Decision shall be effective on the first day of the first month which begins not less than 30 days following the date of publication in the Federal Register.

(This Treasury Decision is issued under the authority contained in section 7805 of the Internal Revenue Code of 1954 (68A Stat. 917; 26 U.S.C. 7805).)

MORTIMER M. CAPLIN,
Commissioner of Internal Revenue.

Approved August 28, 1961.

STANLEY S. SURREY,
Asst. Secretary of the Treasury.

(Filed by the Division of the Federal Register on August 30, 1961, 8:55 a. m., and published in the issue of the Federal Register for August 31, 1961, 26 F.R. 8198)

SECTION 5705.—REFUND OR ALLOWANCE OF TAX

26 CFR 285.172: Allowance. T. D. 6572 [1]

TITLE 26—INTERNAL REVENUE.—CHAPTER I, SUBCHAPTER E, PART 285.—MANUFACTURE OF CIGARETTE PAPERS AND TUBES

Deletion of provisions relating to importations and miscellaneous amendments.

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

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

On June 7, 1961, a notice of proposed rulemaking to amend 26 CFR Part 285 was published in the Federal Register (26 F.R. 5071). The purpose of the proposal was (1) to remove from these regulations all provisions relating to the importation of cigarette papers and tubes, which are being incorporated in the new 26 CFR Part 275 "Importation of Tobacco Materials, Tobacco Products, and Cigarette Papers and Tubes," (2) to prescribe the use of certain forms in connection with claims, and (3) to make conforming, clarifying, and editorial changes.

No comments or suggestions pertaining to these regulations were received during the period of 30 days from the date of publication of the notice of proposed rulemaking. However, it has been determined administratively necessary to make an editorial change in section 285.31 to provide a retention period for authorizations required to be kept under proposed sections 285.34a and 285.35. Accordingly, the following regulations are hereby adopted.

1. The title of this part is amended to read "Manufacture of Cigarette Papers and Tubes".

2. Section 285.1 and the heading are amended to read as follows:

§ 285.1 MANUFACTURE OF CIGARETTE PAPERS AND TUBES.—This part contains the regulations relating to the manufacture of cigarette papers and tubes; the payment of internal revenue taxes imposed by Chapter 52 of the Internal Revenue Code; and the qualification of and operations by manufacturers of cigarette papers and tubes.

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[1] The publication of this Treasury Decision in 26 F.R. 8199, dated August 31, 1961, contains (1) instructions for modifying the notice of proposed rulemaking published in 26 F.R. 5071, dated June 7, 1961, and (2) the full context of the regulations with such modifications. As here published, the Treasury Decision reflects the context of such regulations with modifications. The individual instructions have been omitted.

3. A new section, designated § 285.3, is added immediately following § 285.2.

§ 285.3 TERRITORIAL EXTENT.—The provisions of the regulations in this part shall apply in the several States of the United States and the District of Columbia.

§ 285.11 [Amendment]

4. Section 285.11 is amended as follows:

(A) By deleting the definition entitled "Importer".

(B) By striking, in the definition entitled "Internal revenue officer", the words "Treasury Department" and inserting, in lieu thereof, the words "Internal Revenue Service".

(C) By deleting the definitions entitled "Manufacturer of cigarettes" and "Manufacturer of tobacco".

(D) By adding, immediately following the definition entitled "Manufacturer of cigarette papers and tubes", a new definition to read:

MANUFACTURER OF TOBACCO PRODUCTS.—Any person who manufactures cigars or cigarettes, or who prepares, processes, manipulates, or packages, for removal, or merely removes, tobacco (other than cigars and cigarettes) for consumption by smoking or for use in the mouth or nose, or who sells or delivers any tobacco (other than cigars and cigarettes) contrary to the provisions of Chapter 52, I.R.C., or regulations thereunder. The term "manufacturer of tobacco products" shall not include (a) a person who in any manner prepares tobacco, or produces cigars or cigarettes, solely for his own personal consumption or use; (b) a proprietor of a customs bonded manufacturing warehouse with respect to the operation of such warehouse; (c) a farmer or grower of tobacco with respect to the sale of leaf tobacco of his own growth or raising, if it is in the condition as cured on the farm; or (d) a bona fide association of farmers or growers of tobacco with respect to sales of leaf tobacco grown by farmer or grower members, if the tobacco so sold is in the condition as cured on the farm, and if the association maintains records of all leaf tobacco, acquired or received and sold or otherwise disposed of, in accordance with Part 280 of this chapter.

5. Section 285.23 is amended to read as follows:

§ 285.23 PERSONS LIABLE FOR TAX.—The manufacturer of cigarette papers and tubes shall be liable for the taxes imposed on such articles by section 5701, I.R.C: *Provided*, That when cigarette papers and tubes are transferred, without payment of tax, pursuant to section 5704, I.R.C., to the bonded premises of another such manufacturer, a manufacturer of tobacco products, or an export warehouse proprietor, the transferee shall become liable for the tax upon receipt by him of such papers and tubes and the transferor shall thereupon be relieved of his liability for the tax. When cigarette papers and tubes are released in bond from customs custody for transfer to the bonded premises of a manufacturer of such papers and tubes or a manufacturer of tobacco products, the transferee shall become liable for the tax on the papers and tubes upon release from customs custody. Any person who possesses cigarette papers and tubes in violation of section 5751(a)(1) or (2), I.R.C., shall be liable for a tax equal to the tax on such articles. (72 Stat. 1417, 1424; 26 U.S.C. 5703, 5751.)

§ 285.25 [Amendment]

6. Section 285.25 is amended by changing the period at the end of the second sentence to a colon and adding "*Provided*, That where the manufacturer so requests by letter, in duplicate, and the assistant regional commissioner grants specific authorization, the manufacturer need not, during the term of such authorization, file a tax return for any month for which tax is not due or payable."

§ 285.26 [Amendment]

7. Section 285.26 is amended by changing the period at the end of the fourth sentence to a comma and adding the clause "both subject to the period of limitations prescribed in section 6511, I.R.C."

§ 285.27 [Deletion]

8. Section 285.27 is deleted.

9. Section 285.31 and the heading are amended to read as follows:

§ 285.31 RETENTION OF RECORDS.—All records required to be kept under this part, including copies of authorizations, inventories, reports, and returns, shall be retained by the manufacturer for three years following the close of the calendar year in which filed or made, or in the case of an authorization, for three years following the close of the calendar year in which the operation under such authorization is concluded. Such records shall be made available for inspection by any internal revenue officer upon his request. (72 Stat. 1423; 26 U.S.C. 5741.)

10. A new section, designated § 285.34a, is added immediately following § 285.34.

§ 285.34a ALTERNATE METHODS OR PROCEDURES.—A manufacturer of cigarette papers and tubes, on specific approval by the Director as provided in this section, may use an alternate method or procedure in lieu of a method or procedure specifically prescribed in this part. The Director may approve an alternate method or procedure, subject to stated conditions, when he finds that—

(a) good cause has been shown for the use of the alternate method or procedure,

(b) the alternate method or procedure is within the purpose of, and consistent with the effect intended by, the specifically prescribed method or procedure, and affords equivalent security to the revenue, and

(c) the alternate method or procedure will not be contrary to any provision of law, and will not result in an increase in cost to the Government or hinder the effective administration of this part.

No alternate method or procedure relating to the giving of any bond or to the assessment, payment, or collection of tax, shall be authorized under this section. Where a manufacturer desires to employ an alternate method or procedure, he shall submit a written application to do so, in triplicate, to the assistant regional commissioner for transmittal to the Director. The application shall specifically describe the proposed alternate method or procedure, and shall set forth the reasons therefor. Alternate methods or procedures shall not be employed until the application has been approved by the Director. The manufacturer shall, during the period of authorization of an alternate method or procedure, comply with the terms of the approved application. Authorization for any alternate method or procedure may be withdrawn whenever in the judgment of the Director the revenue is jeopardized or the effective administration of this part is hindered. The manufacturer shall retain, as part of his records, any authorization of the Director under this section.

11. Section 285.35 and the heading are amended to read as follows:

§ 285.35 EMERGENCY VARIATIONS FROM REQUIREMENTS.—The Director may approve methods of operation other than as specified in this part, where he finds that an emergency exists and the proposed variations from the specified requirements are necessary, and the proposed variations—

(a) will afford the security and protection to the revenue intended by the prescribed specifications,

(b) will not hinder the effective administration of this part, and

(c) will not be contrary to any provision of law.

Variations from requirements granted under this section are conditioned on compliance with the procedures, conditions, and limitations set forth in the approval of the application. Failure to comply in good faith with such procedures, conditions, and limitations shall automatically terminate the authority

for such variations and the manufacturer thereupon shall fully comply with the prescribed requirements of regulations from which the variations were authorized. Authority for any variations may be withdrawn whenever in the judgment of the Director the revenue is jeopardized or the effective administration of this part is hindered by the continuation of such variation. Where a manufacturer desires to employ such variation, he shall submit a written application to do so, in triplicate, to the assistant regional commissioner for transmittal to the Director. The application shall describe the proposed variations and set forth the reasons therefor. Variations shall not be employed until the application has been approved. The manufacturer shall retain, as part of his records, any authorization of the Director under this section.

12. Section 285.72 and the heading are amended to read as follows:

§ 285.72 DEPOSIT OF SECURITIES IN LIEU OF CORPORATE SURETY.—In lieu of corporate surety, the manufacturer of cigarette papers and tubes may pledge and deposit, as security for his bond, securities which are transferable and are guaranteed as to both interest and principal by the United States, in accordance with the provisions of 31 CFR Part 225. (61 Stat. 650, 72 Stat. 1421; 6 U.S.C. 15, 26 U.S.C. 5711.)

13. Section 285.79 and the heading are amended to read as follows:

§ 285.79 RELEASE OF PLEDGED SECURITIES.—Securities of the United States pledged and deposited as provided in § 285.72 shall be released only in accordance with the provisions of 31 CFR Part 225. Such securities will not be released by the assistant regional commissioner until liability under the bond for which they were pledged has been terminated. When the assistant regional commissioner is satisfied that they may be released, he shall fix the date or dates on which a part or all of such securities may be released. At any time prior to the release of such securities, the assistant regional commissioner may extend the date of release for such additional length of time as he deems necessary. (61 Stat. 650, 72 Stat. 1421; 6 U.S.C. 15, 26 U.S.C. 5711.)

14. Section 285.131 is amended to read as follows:

§ 285.131 TRANSFER IN BOND.—A manufacturer of cigarette papers and tubes may transfer such papers and tubes, under his bond, without payment of tax, to the bonded premises of any manufacturer of cigarette papers and tubes, or to the bonded premises of any manufacturer of tobacco products solely for use in the manufacture of cigarettes, or, in the case of cigarette papers only, to be put up by him in units of not more than 25 papers each for distribution with packages of manufactured tobacco. The transfer of cigarette papers and tubes, without payment of tax, to the bonded premises of an export warehouse proprietor shall be in accordance with the provisions of Part 290 of this chapter. (72 Stat. 1418; 26 U.S.C. 5704.)

15. Section 285.132 is amended to read as follows:

§ 285.132 RELEASE FROM CUSTOMS CUSTODY.—The release of cigarette papers and tubes from customs custody, without payment of tax, for transfer to the premises of a cigarette papers and tubes factory or a tobacco products factory, shall be in accordance with the provisions of Part 275 of this chapter. (72 Stat. 1418; 26 U.S.C. 5704.)

16. Section 285.134 and the heading are amended to read as follows:

§ 285.134 REMOVAL FOR EXPORT PURPOSES.—The removal of cigarette papers and tubes, without payment of tax, for shipment to a foreign country, Puerto Rico, the Virgin Islands, or a possession of the United States, or for consumption beyond the jurisdiction of the internal revenue laws of the United States, shall be in accordance with the provisions of Part 290 of this chapter. (72 Stat. 1418; 26 U.S.C. 5704.)

17. Subpart J.—Operations by Importers, consisting of §§ 285.151, 285.161, and 285.162, is deleted.

18. Section 285.172 is amended to read as follows:

§ 285.172 ALLOWANCE.—Relief from the payment of tax on cigarette papers and tubes may be extended to a manufacturer by allowance of the tax, where the cigarette papers and tubes, after removal from the factory upon determination of tax and prior to the payment of such tax, are lost (otherwise than by theft) or destroyed, by fire, casualty, or act of God, while in the possession or ownership of the manufacturer who removed such articles, or are withdrawn by him from the market. Any claim for allowance under this section shall be filed on Form 2635, in triplicate, with the assistant regional commissioner for the region in which the articles were removed, shall be executed under penalties of perjury and shall show the date the cigarette papers and tubes were removed from the factory. A claim relating to articles lost or destroyed shall be supported as prescribed in § 285.181. In the case of a claim relating to cigarette papers and tubes withdrawn from the market, the schedule, as provided in § 285.191, shall be filed with the assistant regional commissioner for the region in which the articles are assembled. The manufacturer may not anticipate allowance of his claim by making the adjusting entry in a tax return pending consideration and action on the claim. Cigarette papers and tubes to which such a claim relates must be shown to have been removed on determination of tax on the return covering the period during which such papers and tubes were so removed. Upon action on the claim by the assistant regional commissioner he will return a copy of the Form 2635 to the manufacturer as notice of such action, which copy, with the copy of any verified supporting schedules, shall be retained by the manufacturer. When such notification of allowance of the claim or any part thereof is received prior to the time the return covering the tax on the cigarette papers and tubes to which the claim relates is to be filed, the manufacturer may make an adjusting entry and explanatory statement in that tax return. Where the notice of allowance is received subsequent to the filing of the return and taxpayment of the cigarette papers and tubes to which the claim relates, the manufacturer may make an adjusting entry and explanatory statement on the next subsequent tax return(s) to the extent necessary to take credit in the amount of the allowance. (72 Stat. 1419; 26 U.S.C. 5705.)

§ 285.173 [Amendment]

19. Section 285.173 is amended by striking in the first sentence the words "or importer" wherever they appear.

20. Section 285.174 is amended to read as follows:

§ 285.174 REMISSION.—Remission of the tax liability on cigarette papers and tubes may be extended to the manufacturer liable for the tax where cigarette papers and tubes, before removal or after removal for tax-exempt purposes (including transfers in bond), are lost (otherwise than by theft) or destroyed, by fire, casualty, or act of God, while in the possession or ownership of such manufacturer. Where cigarette papers and tubes are so lost or destroyed, the manufacturer shall report promptly such fact, and the circumstances, to the assistant regional commissioner for the region in which the factory is located, and shall prepare a claim on Form 2635, in triplicate, setting forth the nature, date, place, and extent of the loss or destruction. All copies of the claim, accompanied by such evidence as is necessary to establish to the satisfaction of the assistant regional commissioner that the claim is valid, shall be filed with the assistant regional commissioner for the region in which the factory is located. Upon action on the claim by the assistant regional commissioner he will return a copy of the Form 2635 to the manufacturer as notice of such action. (72 Stat. 1419; 26 U.S.C. 5705.)

§ 285.175 [Amendment]

21. Section 285.175 is amended by striking the words "or importer".

§ 285.181 [Amendment]

22. Section 285.181 is amended by striking from the first sentence the words "or importer".

23. Section 285.191 is amended to read as follows:

§ 285.191 ACTION BY CLAIMANT.—Where cigarette papers and tubes are withdrawn from the market and the manufacturer desires to file claim under the provisions of § 285.172 or § 285.173, he shall assemble the articles in or adjacent to a factory if they are to be retained in or received into such factory, or at any suitable place if they are to be destroyed. The manufacturer shall group the articles according to the rate of tax applicable thereto, and shall prepare a schedule of the articles on Form 3069, in triplicate. All copies of the schedule shall be forwarded to the assistant regional commissioner for the region in which the articles are assembled. (72 Stat. 1419; 26 U.S.C. 5705.)

24. Section 285.192 is amended to read as follows:

§ 285.192 ACTION BY ASSISTANT REGIONAL COMMISSIONER.—Upon receipt of a schedule of cigarette papers and tubes withdrawn from the market, the assistant regional commissioner may assign an internal revenue officer to verify the schedule and supervise disposition of the cigarette papers and tubes, or he may authorize the manufacturer to dispose of the articles without supervision by so stating on the original and one copy of the schedule returned to the manufacturer. (72 Stat. 1419; 26 U.S.C. 5705.)

25. Section 285.193 and the heading are amended to read as follows:

§ 285.193 DISPOSITION OF CIGARETTE PAPERS AND TUBES AND SCHEDULE.—When so authorized, as evidenced by the assistant regional commissioner's statement on the schedule, the manufacturer shall dispose of the cigarette papers and tubes as specified in the schedule. After the manufacturer has disposed of the articles, he shall execute a certificate on both copies of the schedule returned to him by the assistant regional commissioner, to show the disposition and the date of disposition of the articles. In connection with a claim for allowance, the manufacturer then shall return the original of the schedule to the assistant regional commissioner who authorized such disposition, who will cause such schedule to be associated with the claim, Form 2635. In connection with a claim for refund, the manufacturer shall attach the original of the schedule to his claim, Form 843, filed under § 285.173. When an internal revenue officer is assigned to verify the schedule and supervise disposition of the cigarette papers and tubes, such officer shall, upon completion of his assignment, execute a certificate on all copies of the schedule to show the disposition and the date of disposition of the articles. In connection with a claim for allowance, the officer shall return one copy of the schedule to the manufacturer for his records, and in connection with a claim for refund, the officer shall return the original and one copy of the schedule to the manufacturer, the original of which the manufacturer shall attach to his claim, Form 843, filed under § 285.173. (72 Stat. 1419; 26 U.S.C. 5705.)

Effective date.—This Treasury Decision shall be effective on the first day of the first month which begins not less than 30 days following the date of publication in the Federal Register.

(This Treasury Decision is issued under the authority contained in section 7805 of the Internal Revenue Code of 1954 (68A Stat. 917; 26 U.S.C. 7805).)

MORTIMER M. CAPLIN,
Commissioner of Internal Revenue.

Approved August 28, 1961.

STANLEY S. SURREY,
Assistant Secretary of the Treasury.

(Filed by the Division of the Federal Register on August 30, 1961, 8:55 a.m., and published in the issue of the Federal Register for August 31, 1961, 26 F.R. 8199)

SUBCHAPTER F.—GENERAL PROVISIONS

SECTION 5751.—PURCHASE, RECEIPT, POSSESSION, OR SALE OF TOBACCO PRODUCTS AND CIGARETTE PAPERS AND TUBES AFTER REMOVAL

26 CFR 296.161: Scope of subpart. T.D. 6573 [1]

TITLE 26—INTERNAL REVENUE.—CHAPTER I, SUBCHAPTER E, PART 296.—MISCELLANEOUS REGULATIONS RELATING TO TOBACCO MATERIALS, TOBACCO PRODUCTS, AND CIGARETTE PAPERS AND TUBES

Provisions relating to dealers in tobacco products

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

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

On June 7, 1961, a notice of proposed rule making to amend 26 CFR Part 296 was published in the Federal Register (26 F.R. 5073). The purposes of the proposal were to make conforming amendments in Subparts A, B, and C of 26 CFR Part 296, and to revise and incorporate in one subpart, designated as Subpart G of the regulations in 26 CFR Part 296, the provisions relating to dealers in tobacco products which were formerly contained in 26 CFR Parts 270 and 275.

No comments or suggestions pertaining to these regulations were received during the period of 30 days from the date of publication of the notice of proposed rule making. Accordingly, with the exception of an editorial change striking ", labels," from section 296.167, the regulations so published are hereby adopted.

§ 296.11 [Amendment]

1. Section 296.11 of Subpart A is amended by striking, in the first sentence, the words "Form 356—Revised" and inserting, in lieu *thereof, the words* "Circular No. 570, as revised".

§ 296.51 [Amendment]

2. Section 296.51 of Subpart B is amended, in the definition of the United States, by striking ", the Territories of Alaska and Hawaii,".

§ 296.72 [Amendment]

3. Section 296.72 of Subpart C is amended, in the definition of the United States, by striking ", the Territory of Hawaii,".

4. A new Subpart G is added to read as follows:

Subpart G.—Dealers in Tobacco Products

Preamble.—The regulations in this subpart shall not affect any act done, or any liability or right accruing or accrued, or any suit or proceeding had or commenced, before the effective date of the regulations in this subpart.

[1] 26 F.R. 8202.

Section
296.161 Scope of subpart.
296.162 Territorial extent.
296.163 Meaning of terms.
296.164 Authority of internal revenue officers to enter premises.
296.165 Interference with administration.
296.166 Dealing in tobacco products.
296.167 Liability to tax.
296.168 Liability to penalties and forfeitures.

AUTHORITY. §§ 296.161 to 296.168 are issued under section 7805, 68A Stat. 917; 26 U.S.C. 7805. Additional authority is cited in parentheses following the sections affected.

§ 296.161 SCOPE OF SUBPART.—The regulations in this subpart relate to the purchase, receipt, possession, offering for sale, or sale or other disposition of tobacco products by dealers in such products.

§ 296.162 TERRITORIAL EXTENT.—The provisions of the regulations in this subpart shall apply in the several States of the United States and the District of Columbia.

§ 296.163 MEANING OF TERMS.—When used in this subpart, where not otherwise distinctly expressed or manifestly incompatible with the intent thereof, each of the following terms shall have the meaning ascribed in this section. Words in the plural form shall include the singular, words in the singular form shall include the plural, and words importing the masculine gender shall include the feminine. The terms "includes" and "including" do not exclude things not enumerated which are in the same general class.

Dealer.—Any person who sells, or offers for sale, at wholesale or retail levels, any tobacco products after removal.

Internal revenue officer.—An officer or employee of the Internal Revenue Service duly authorized to perform any function relating to the administration or enforcement of this subpart.

I.R.C.—The Internal Revenue Code of 1954, as amended.

Manufacturer of tobacco products.—Any person who manufactures cigars or cigarettes, or who prepares, processes, manipulates, or packages, for removal, or merely removes, tobacco (other than cigars and cigarettes) for consumption by smoking or for use in the mouth or nose, or who sells or delivers any tobacco (other than cigars and cigarettes) contrary to the provisions of Chapter 52, I.R.C., or regulations thereunder. The term "manufacturer of tobacco products" shall not include (a) a person who in any manner prepares tobacco, or produces cigars or cigarettes, solely for his own personal consumption or use; (b) a proprietor of a customs bonded manufacturing warehouse with respect to the operation of such warehouse; (c) a farmer or grower of tobacco with respect to the sale of leaf tobacco of his own growth or raising, if it is in the condition as cured on the farm; or (d) a bona fide association of farmers or growers of tobacco with respect to sales of leaf tobacco grown by farmer or grower members, if the tobacco so sold is in the condition as cured on the farm, and if the association maintains records of all leaf tobacco, acquired or received and sold or otherwise disposed of, in accordance with Part 280 of this chapter.

Package.—The container in which tobacco products are put up by the manufacturer or the importer and offered for sale or delivery to the consumer.

Person.—An individual, partnership, association, company, corporation, estate, or trust.

Removal or remove.—The removal of tobacco products from the factory or release from customs custody, including the smuggling or other unlawful importation of such articles into the United States.

Tobacco products.—Manufactured tobacco, cigars, and cigarettes.

U.S.C.—The United States Code.

§ 296.164 AUTHORITY OF INTERNAL REVENUE OFFICERS TO ENTER PREMISES.—Any internal revenue officer may enter in the daytime any premises where tobacco products are kept or stored, so far as it may be necessary for the purpose of examining such products. When such premises are open at night, any internal revenue officer may enter them, while so open, in the performance of his official duties. The owner of such premises, or person having the superintendence of the same, who refuses to admit any internal revenue officer or permit him to examine such products shall be liable to the penalties prescribed by law for the offense. Operators of vending machines shall make the tobacco products in their machines available for inspection upon the request of any internal revenue officer. (68A Stat. 872, 903; 26 U.S.C. 7342, 7606.)

§ 296.165 INTERFERENCE WITH ADMINISTRATION.—Whoever, corruptly or by force or threats of force, endeavors to hinder or obstruct the administration of this subpart, or endeavors to intimidate or impede any internal revenue officer acting in his official capacity, or forcibly rescues or attempts to rescue or causes to be rescued any property, after it has been duly seized for forfeiture to the United States in connection with a violation of the internal revenue laws, shall be liable to the penalties prescribed by law. (68A Stat. 855; 26 U.S.C. 7212.)

§ 296.166 DEALING IN TOBACCO PRODUCTS.—All tobacco products purchased, received, possessed, offered for sale, sold or otherwise disposed of, by any dealer must be in proper packages which bear the mark and notice as prescribed in Parts 270 and 275 of this chapter. Tobacco products may be sold, or offered for sale, at retail *from* such packages, provided the products remain in the packages until removed by the customer or in the presence of the customer. Where a vending machine is used, tobacco products must similarly be vended in proper packages or *directly from* such packages. (72 Stat. 1424; 26 U.S.C. 5751.)

§ 296.167 LIABILITY TO TAX.—Any dealer who, with intent to defraud the United States, possesses tobacco products (1) upon which the tax has not been paid or determined in the manner and at the time prescribed in Parts 270 and 275 of this chapter or (2) which, after removal without payment of tax pursuant to section 5704, I.R.C., and regulations issued thereunder, have been diverted from the applicable purpose or use specified in that section or (3) which are not put up in packages prescribed in Parts 270 and 275 of this chapter or are put up in packages not bearing the marks, and notices prescribed in such regulations shall be liable for a tax equal to the tax on such products. (72 Stat. 1424; 26 U.S.C. 5751.)

§ 296.168 LIABILITY TO PENALTIES AND FORFEITURES.—Any dealer who fails to comply with the provisions of this subpart becomes liable to the civil and criminal penalties, and forfeitures, provided by law. (72 Stat. 1425, 1426; 26 U.S.C. 5761, 5762, and 5763.)

Effective date.—This Treasury Decision shall be effective on the first day of the first month which begins not less than 30 days following the date of publication in the Federal Register.

(This Treasury Decision is issued under the authority contained in section 7805 of the Internal Revenue Code of 1954 (68A Stat. 917; 26 U.S.C. 7805).)

MORTIMER M. CAPLIN,
Commissioner of Internal Revenue.

Approved August 28, 1961.

STANLEY S. SURREY,
Asst. Secretary of the Treasury.

(Filed by the Division of the Federal Register on August 30, 1961, 8:55 a.m., and published in the issue of the Federal Register for August 31, 1961, 26 F.R. 8202)

CHAPTER 53.—MACHINE GUNS AND CERTAIN OTHER FIREARMS

SUBCHAPTER B.—GENERAL PROVISIONS

SECTION 5848.—DEFINITIONS

26 CFR 179.20: Firearm. Rev. Rul. 61-203

A hand gun of the Luger or semi-automatic Mauser type, as well as the Fiala Arms and Equipment Company, Inc., .22 caliber pistol, with a barrel of less than 16 inches in length is a "firearm," if it has an attached or attachable shoulder stock.

However, where a hand gun of this type has a barrel of 16 inches or more in length, it is not a "firearm" even though such weapon has an attached or attachable shoulder stock.

Advice has been requested whether semi-automatic hand guns, such as Luger and Mauser pistols, and single shot .22 caliber pistols made by the Fiala Arms and Equipment Company, Inc., with attached or attachable shoulder stocks are "firearms" as defined in section 5848(1) of the National Firearms Act (Chapter 53 of the Internal Revenue Code of 1954).

Basically, such types of weapons were originally designed as pistols. However, they are also designed to function as rifles when shoulder stocks are attached.

Section 5848(1) of the National Firearms Act defines the term "firearm" as follows:

The term "firearm" means a shotgun having a barrel or barrels of less than 18 inches in length, or a rifle having a barrel or barrels of less than 16 inches in length, or any weapon made from a rifle or shotgun (whether by alteration, modification, or otherwise) if such weapon as modified has an overall length of less than 26 inches, or 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, or a machine gun, and includes a muffler or silencer for any firearm whether or not such firearm is included within the foregoing definition.

Accordingly, a hand gun of the Luger or semi-automatic Mauser type, as well as the Fiala Arms and Equipment Company, Inc., .22 caliber pistol, with a barrel of less than 16 inches in length, is held to be a "firearm," as that term is defined in section 5848(1) of the Act, if such weapon has an attached or attachable shoulder stock. See also Rev. Rul. 61-45, C.B. 1961-1, 663.

Conversely, where one of the above described pistols has a barrel of 16 inches or more in length, it is held not to be a "firearm," within the definition of section 5848(1) of the Act, even though such weapon has an attached or attachable shoulder stock. With the shoulder stock attached, such weapon is a rifle. When the shoulder stock is detached, such weapon is a pistol and is deemed not to have been made from a rifle.

On the other hand, certain types of weapons are not designed to function as pistols. This category includes semi-automatic weapons with folding shoulder stocks such as the U.S. Carbine, caliber 30,

model MI A1, and the Marble Game Getter Gun. These weapons were originally designed to be fired from the shoulder.

Therefore, any such weapon with a folding shoulder stock is held not to be a "firearm," as that term is defined in section 5848(1) of the Act, if it has either a rifled barrel of 16 inches or more in length or a combination of a rifled bore and smooth bore barrels of 18 inches or more in length. However, if the shoulder stock is removed from such a weapon it will be classified as a "firearm," as that term is defined in section 5848(1) of the Act, if its overall length is less than 26 inches.

SUBTITLE F.—PROCEDURE AND ADMINISTRATION

CHAPTER 61.—INFORMATION AND RETURNS

SUBCHAPTER A.—RETURNS AND RECORDS

PART I.—RECORDS, STATEMENTS, AND SPECIAL RETURNS

SECTION 6001.—NOTICE OR REGULATIONS REQUIRING RECORDS, STATEMENTS, AND SPECIAL RETURNS

26 CFR 1.6001–1: Records.

Reproduction of certain Federal tax return forms and schedules. See Rev. Proc. 61–31, page 569.

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26 CFR 44.6001–1: Record requirements. T. D. 6568 [1]

TITLE 26—INTERNAL REVENUE.—CHAPTER I, SUBCHAPTER D, PART 44.—TAXES ON WAGERING

Amendment to paragraph (e) of § 44.6001–1, relating to period for retaining records.

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

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

Paragraph (e) of § 44.6001–1 of the Wagering Tax Regulations (26 CFR Part 44), relating to the retention of records, is amended to provide a period for the retention of the daily record required by § 44.4403–1 of such Regulations. As amended, such paragraph (e) reads as follows:

§ 44.6001–1 RECORD REQUIREMENTS.

* * * * * * *

(e) *Period for retaining records.*—All records required by the regulations in this part shall at all times be available for inspection by internal revenue officers. Records required by § 44.4403–1 and by paragraph (a) of this section shall be maintained for a period of at least three years from the date the tax became

[1] 26 F.R. 7568.

due. Records required by paragraph (b) of this section shall be maintained for a period of at least three years from the date the wager was received. Records required by paragraph (c) of this section shall be maintained for a period of at least three years from the date any credit is taken or refund is claimed.

Because this Treasury Decision merely prescribes the period for which certain records are to be maintained, it is found 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 is issued under the authority contained in section 7805 of the Internal Revenue Code of 1954 (68A Stat. 917; 26 U.S.C. 7805).)

MORTIMER M. CAPLIN,
Commissioner of Internal Revenue.

Approved August 9, 1961.

STANLEY S. SURREY,
Assistant Secretary of the Treasury.

(Filed by the Division of the Federal Register on August 14, 1961, 8:49 a.m., and published in the issue of the Federal Register for August 15, 1961, 26 F.R. 7568)

SECTION 6011.—GENERAL REQUIREMENT OF RETURN, STATEMENT OR LIST

26 CFR 1.6011–1: General requirement of return, statement, or list.

Reproduction of certain Federal tax return forms and schedules. See Rev. Proc. 61–31, page 569.

Subpart C.—Estate and Gift Tax Returns

SECTION 6018.—ESTATE TAX RETURNS

26 CFR 20.6018–1: Returns.

Reproduction of certain Federal tax return forms and schedules. See Rev. Proc. 61–31, page 569.

SECTION 6019.—GIFT TAX RETURNS

26 CFR 25.6019–1: Persons required to file returns.

Reproduction of certain Federal tax return forms and schedules. See Rev. Proc. 61–31, page 569.

PART III.—INFORMATION RETURNS

Subpart C.—Information Regarding Wages Paid Employees

SECTION 6051.—RECEIPTS FOR EMPLOYEES

26 CFR 31.6051–1: Statements for employees.

Printing of substitutes for Form W–2, Withholding Tax Statement—1962. See Rev. Proc. 61–29, page 566.

SUBCHAPTER B.—MISCELLANEOUS PROVISIONS

SECTION 6103.—PUBLICITY OF RETURNS AND LISTS OF TAXPAYERS

26 CFR 301.6103(a)–1: Inspection of returns by certain classes of persons and State and Federal government establishments pursuant to Executive order. E. O. 10954

Amendment of Executive Order No. 10906, authorizing inspection of certain tax returns.

By virtue of the authority vested in me by sections 6103(a) and 6106 of the Internal Revenue Code of 1954 (68A Stat. 753, 756; 26 U.S.C. 6103(a), 6106), it is hereby ordered that the last paragraph of Executive Order No. 10906 of January 17, 1961 [C.B. 1961–1, 681], entitled "Inspection by Certain Classes of Persons and State and Federal Government Establishments of Returns Made in Respect of Certain Taxes Imposed by the Internal Revenue Code of 1954", be, and it is hereby, amended to read as follows:

This order shall become effective upon its filing for publication in the Federal Register, and shall on that date supersede Executive Order No. 10738 of November 15, 1957 [C.B. 1957–2, 844], to the extent that such order is applicable to inspection by State tax officials after the effective date of this order of estate and gift tax returns made under the Internal Revenue Code of 1954.

This order shall be effective as of January 18, 1961.

JOHN F. KENNEDY.

THE WHITE HOUSE,
July 26, 1961.

(Filed by the Division of the Federal Register on July 26, 1961, 4:33 p.m., and published in the issue of the Federal Register for July 28, 1961, 26 F.R. 6759)

26 CFR 301.6103(a)–101: Inspection of returns by committees of Congress other than those enumerated in section 6103(d). (Also Part II, Section 55; 458.324.) E.O. 10947

Inspection of income, excess-profits, estate, and gift tax returns by the House Committee on Public Works.

By virtue of the authority vested in me by section 55(a) of the Internal Revenue Code of 1939, as amended (53 Stat. 29, 54 Stat.

1008; 26 U.S.C. (1952 Ed) 55(a)), and by section 6103(a) of the Internal Revenue Code of 1954 (68A Stat. 753; 26 U.S.C. 6103(a)), it is hereby ordered that any income, excess-profits, estate, or gift tax return for the years 1950 to 1961, inclusive, shall, during the Eighty-seventh Congress, be open to inspection by the Committee on Public Works, House of Representatives, or any duly authorized subcommittee thereof, in connection with its investigation of the policies, procedures and practices involved in the administration of the Federal-Aid Highway Program, pursuant to House Resolution 23, 87th Congress, agreed to February 6, 1961, such inspection to be in accordance and upon compliance with the rules and regulations prescribed by the Secretary of the Treasury in Treasury Decisions 6132 [C.B. 1955–1, 142] and 6133 [C.B. 1955–1, 335], relating to the inspection of returns by committees of the Congress, approved by the President on May 3, 1955.

This order shall be effective upon its filing for publication in the Federal Register.

JOHN F. KENNEDY.

THE WHITE HOUSE,
June 12, 1961.

(Filed by the Division of the Federal Register on June 13, 1961, 11:12 a.m., and published in the issue of the Federal Register for June 14, 1961, 26 F.R. 5283)

(Also Part II, Section 55; 458.324.) E. O. 10966

Inspection of income, excess-profits, estate, and gift tax returns by the Committee on Government Operations, House of Representatives.

By virtue of the authority vested in me by section 55(a) of the Internal Revenue Code of 1939, as amended (53 Stat. 29, 54 Stat. 1008; 26 U.S.C. (1952 Ed.) 55(a)), and by section 6103(a) of the Internal Revenue Code of 1954 (68A Stat. 753; 26 U.S.C. 6103(a)), it is hereby ordered that any income, excess-profits, estate, or gift tax return for the years 1947 to 1961, inclusive, shall, during the Eighty-seventh Congress, be open to inspection by the Committee on Government Operations, House of Representatives, or any duly authorized subcommittee thereof, in connection with its studies of the operation of Government activities at all levels with a view to determining the economy and efficiency of the Government, such inspection to be in accordance and upon compliance with the rules and regulations prescribed by the Secretary of the Treasury in Treasury Decisions 6132 [C.B. 1955–1,142] and 6133 [C.B. 1955–1,335], relating to the inspection of tax returns by committees of the Congress, approved by the President on May 3, 1955.

This order shall become effective upon its filing for publication in the Federal Register.

JOHN F. KENNEDY.

THE WHITE HOUSE,
October 10, 1961.

(Filed by the Division of the Federal Register on October 11, 1961, 4:47 p.m., and published in the issue of the Federal Register for October 13, 1961, 26 F.R. 9667)

26 CFR 301.6103(a)-103: Inspection of returns by the Advisory Commission on Intergovernmental Relations. E. O. 10962
(Also Part II, Section 55; 458.326.)

Inspection of returns by Advisory Commission on Intergovernmental Relations.

By virtue of the authority vested in me by sections 55(a), as amended, 1204, and 1604(c) of the Internal Revenue Code of 1939 (53 Stat. 29, 171, 186; 54 Stat. 1008; 55 Stat. 722; 26 U.S.C. (1952 Ed.) 55(a), 1204, and 1604(c)) and by sections 6103(a) and 6106 of the Internal Revenue Code of 1954 (68A Stat. 753, 756; 26 U.S.C. 6103(a), 6106), it is hereby ordered that returns made in respect of taxes imposed by chapter 1, subchapters A, B, D, and E of chapter 2, subchapter B of chapter 3, chapters 4, 6, and 7, subchapter C of chapter 9, chapters 12 and 21, subchapter A of chapter 29, and chapter 30 of the Internal Revenue Code of 1939 and returns made in respect of taxes imposed by chapters 1, 2, 3, 5, 6, 11, 12, 23, and 32, subchapters B, C, and D of chapter 33, and subchapter B of chapter 37 of the Internal Revenue Code of 1954 shall be open to inspection by the Advisory Commission on Intergovernmental Relations for the purpose of making studies and investigations in connection with the performance of its function of recommending methods of coordinating and simplifying tax laws and administrative practices to achieve a more orderly and less competitive fiscal relationship between the levels of government and to reduce the burden of compliance for taxpayers. Such inspection shall be in accordance and upon compliance with the rules prescribed by the Secretary of the Treasury in the Treasury Decision approved by me this date, relating to the inspection of such returns by the Advisory Commission on Intergovernmental Relations.

This Executive Order shall be effective upon its filing for publication in the Federal Register.

JOHN F. KENNEDY.

THE WHITE HOUSE,
August 23, 1961.

(Filed by the Divison of the Federal Register on August 24, 1961, 3:12 p.m., and published in the issue of the Federal Register for August 26, 1961, 26 F.R. 8001)

(Also Part II, Section 55; 458.326.) T. D. 6570[1]

TITLE 26—INTERNAL REVENUE.—CHAPTER I

SUBCHAPTER E, PART 458.—INSPECTION OF RETURNS

SUBCHAPTER F, PART 301.—PROCEDURE AND ADMINISTRATION

Regulations governing inspection of returns by the Advisory Commission on Intergovernmental Relations.

[1] 26 F.R. 8009.

DEPARTMENT OF THE TREASURY,
Washington 25, D.C.

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

PARAGRAPH 1. Section 458.326 is inserted immediately after § 458.325 to read as follows:

§ 458.326 INSPECTION OF RETURNS BY THE ADVISORY COMMISSION ON INTERGOVERNMENTAL RELATIONS.—(a) Pursuant to the provisions of sections 55(a), as amended, 1204, and 1604(c) of the Internal Revenue Code of 1939 (53 Stat. 29, 171, 186; 54 Stat. 1008; 55 Stat. 722; 26 U.S.C. (1952 ed.) 55(a), 1204, and 1604(c)) and of the Executive order issued under section 55(a) of such Code, any return with respect to income tax, excess-profits tax, declared value excess-profits tax, unjust enrichment tax, estate tax, gift tax, capital stock tax, tax on transfers to avoid income tax, unemployment tax, tax on safe deposit boxes, tax on coconut and other vegetable oils, manufacturers' excise taxes, communications tax, or transportation taxes imposed by such Code shall be open to inspection by the Advisory Commission on Intergovernmental Relations for the purpose of making studies and investigations in connection with the performance of its function of recommending methods of coordinating and simplifying tax laws and administrative practices to achieve a more orderly and less competitive fiscal relationship between the levels of government and to reduce the burden of compliance for taxpayers. The inspection of returns herein authorized may be made by any member or employee of the Commission duly authorized by the Chairman of the Commission to make such inspection. Upon written notice by the Chairman to the Secretary of the Treasury stating the kinds of returns which it is desired to inspect, the Secretary of the Treasury, or any officer or employee of the Department of the Treasury with the approval of the Secretary, may furnish the Commission with any data on such returns or may make the returns available for inspection and the taking of such data as the Chairman may designate. Such data shall be furnished, or such returns shall be made available for inspection, in the office of the Commissioner of Internal Revenue. Any information thus obtained shall be held confidential except that it may be published or disclosed in statistical form provided such publication does not disclose, directly or indirectly, the name or address of any taxpayer.

(b) This section shall be effective upon its filing for publication in the Federal Register.

PAR. 2. Section 301.6103(a)–103 is inserted immediately after § 301.6103(a)–102 to read as follows:

§ 301.6103(a)–103 INSPECTION OF RETURNS BY THE ADVISORY COMMISSION ON INTERGOVERNMENTAL RELATIONS.—(a) Pursuant to the provisions of sections 6103(a) and 6106 of the Internal Revenue Code of 1954 (68A Stat. 753, 756; 26 U.S.C. 6103(a), 6106) and of the Executive order issued thereunder, any return with respect to income tax, tax on transfers to avoid income tax, estate tax, gift tax, unemployment tax, manufacturers excise taxes, communications tax, transportation taxes, tax on safe deposit boxes, or tax on coconut and palm oil imposed by such Code shall be open to inspection by the Advisory Commission on Intergovernmental Relations for the purpose of making studies and investigations in connection with the performance of its function of recommending methods of coordinating and simplifying tax laws and administrative practices to achieve a more orderly and less competitive fiscal relationship between the levels of government and to reduce the burden of compliance for taxpayers. The inspection of returns herein authorized may be made by any member or employee of the Commission duly authorized by the Chairman of the Commission to make such inspection. Upon written notice by the Chairman to the Secretary of the Treasury stating the kinds of returns which it is desired to inspect, the Secretary of the Treasury, or any officer or employee of the Department of the Treasury with the approval of the Secretary, may furnish the Commission with any data on such returns or may make the returns available for inspection and the taking of such data as the Chairman may designate. Such data shall be furnished, or such returns shall be made available for inspection, in the office of the Commissioner of Internal Revenue. Any information thus obtained shall

be held confidential except that it may be published or disclosed in statistical form provided such publication does not disclose, directly or indirectly, the name or address of any taxpayer.

(b) This section shall be effective upon its filing for publication in the Federal Register.

DOUGLAS DILLON,
Secretary of the Treasury.

Approved August 23, 1961.

JOHN F. KENNEDY,
The White House.

(Filed by the Division of the Federal Register on August 24, 1961, 3:12 p.m., and published in the issue of the Federal Register for August 26, 1961, 26 F.R. 8009)

SECTION 6104.—PUBLICITY OF INFORMATION REQUIRED FROM CERTAIN EXEMPT ORGANIZATIONS AND CERTAIN TRUSTS

26 CFR 301.6104–1: Public inspection of applications for tax exemption. T. D. 6565[1]

TITLE 26—INTERNAL REVENUE.—CHAPTER I. SUBCHAPTER F, PART 301.—PROCEDURE AND ADMINISTRATION

Amendment of regulations under section 6104 of the Internal Revenue Code of 1954, relating to publicity of information required from certain exempt organizations and certain trusts, to permit the furnishing of copies of certain documents.

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

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

The regulations under section 6104 of the Internal Revenue Code of 1954, relating to publicity of information required from certain exempt organizations and certain trusts, are hereby amended as follows:

PARAGRAPH 1. Paragraph (e)(3) of § 301.6104–1 is revised to read as follows:

§ 301.6104–1 PUBLIC INSPECTION OF APPLICATIONS FOR TAX EXEMPTION.

* * * * * * *

(e) *Procedure for public inspection of applications for exemption.* * * *

(3) *Copies.*—Notes may be taken of the material opened for inspection under this section, and copies may be made manually but not photographically. Copies of such material will be furnished by the Internal Revenue Service to any person making request therefor. Requests for such copies shall be made in the same manner as requests for inspection (see subparagraph (1) of this paragraph) to the office of the Internal Revenue Service in which such material is available for inspection as provided in paragraph (d) of this section. If made at the time of inspection, the request for copies need not be in writing. Any copies furnished will be certified upon request. The Commissioner may prescribe a reasonable fee for furnishing copies of applications and supporting documents pursuant to this section.

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[1] 26 F.R. 6970.

PAR. 2. Paragraph (b) of § 301.6104–2 is revised to read as follows:

§ 301.6104–2 PUBLICITY OF INFORMATION ON CERTAIN INFORMATION RETURNS.

* * * * * * *

(b) *Copies.*—Notes may be taken of the material opened for inspection under this section, and copies may be made manually but not photographically. Copies of such material will be furnished by the Internal Revenue Service to any person making request therefor. The request shall adequately identify the return and shall be addressed to the district director in whose office the return is available for inspection. The request shall be in writing unless it is made at the time of inspection. Any copies furnished will be certified upon request. The Commissioner may prescribe a reasonable fee for furnishing copies of material available for inspection pursuant to this section.

Because this Treasury Decision makes only procedural changes, 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 Decison is issued under the authority contained in section 7805 of the Internal Revenue Code of 1954 (68A Stat. 917; 26 U.S.C. 7805).)

JOHN W. S. LITTLETON,
Acting Commissioner of Internal Revenue.

Approved July 28, 1961.

DOUGLAS DILLON,
Secretary of the Treasury.

(Filed by the Division of the Federal Register for August 2, 1961, 8:49 a.m., and published in the issue of the Federal Register for August 3, 1961, 26 F.R. 6970)

CHAPTER 63.—ASSESSMENT

SUBCHAPTER B.—DEFICIENCY PROCEDURES IN THE CASE OF INCOME, ESTATE, AND GIFT TAXES

SECTION 6212.—NOTICE OF DEFICIENCY

26 CFR 301.6212–1: Notice of deficiency.

Practice to regard the address of the taxpayer's duly authorized representative as constituting the last known address of the taxpayer. See Rev. Proc. 61–18, page 550.

CHAPTER 65.—ABATEMENTS, CREDITS, AND REFUNDS

SUBCHAPTER B.—RULES OF SPECIAL APPLICATION

SECTION 6412.—FLOOR STOCKS REFUNDS

26 CFR 46.6412(d): Statutory provisions; floor stocks refunds.

Extension to March 31, 1963, of the time for filing claims for refund of tax paid on floor stocks of imported sugar. See T.D. 6578, page 208.

SECTION 6421.—GASOLINE USED FOR CERTAIN NONHIGHWAY PURPOSES OR BY LOCAL TRANSIT SYSTEMS

26 CFR 48.6421(c)-1: Claims.

Reporting requirements for persons claiming payment of tax on account of the nonhighway or local transit use of gasoline with respect to gasoline purchased after June 30, 1956, and before October 1, 1972. See T.D. 6574, page 162.

CHAPTER 75.—CRIMES, OTHER OFFENSES, AND FORFEITURES

SUBCHAPTER A.—CRIMES

PART I.—GENERAL PROVISIONS

SECTION 7201.—ATTEMPT TO EVADE OR DEFEAT TAX

Exclusion of embezzled funds from gross income. See Ct. D. 1863, page 9.

CHAPTER 79.—DEFINITIONS

SECTION 7701.—DEFINITIONS

26 CFR 301.7701-4: Trusts.

Investment trust established by grantor-beneficiary banks where each bank is the owner of its respective portion of trust corpus and income therefrom. See Rev. Rul. 61-175, page 128.

PART II

RULINGS AND DECISIONS UNDER THE INTERNAL REVENUE CODE OF 1939, THE FEDERAL FIREARMS ACT, AND OTHER PUBLIC LAWS

SUBPART A.—RULINGS AND DECISIONS UNDER THE INTERNAL REVENUE CODE OF 1939

Rulings and decisions published in Part II, Subpart A, of the Internal Revenue Bulletin are based on the applications of provisions of the Internal Revenue Code of 1939 and unless otherwise noted therein are published without consideration to any application of the provisions of the Internal Revenue Code of 1954, the Federal Firearms Act, or other public laws.

SUBTITLE A.—TAXES SUBJECT TO THE JURISDICTION OF THE BOARD OF TAX APPEALS

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.

Whether embezzled funds are to be included in the gross income of the embezzler. See Ct. D. 1863, page 9.

Whether the refunded portion of contested real property taxes is income in the year recovered. See Ct. D. 1864, page 236.

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

REGULATIONS 111, SECTION 29.22(b)(1)-1:
Life insurance; amounts paid by reason of the death of the insured.

Proceeds of insurance on the life of an officer of a closely held corporation paid directly to shareholders of the corporation. See Rev. Rul. 61-134, page 250.

REGULATIONS 118, SECTION 39.22(b)(1)-1:
Life insurance; amounts paid by reason of the death of the insured.

Proceeds of insurance on the life of an officer of a closely held corporation paid directly to shareholders of the corporation. See Rev. Rul. 61-134, page 250.

SECTION 22(k).—GROSS INCOME: ALIMONY, ETC., INCOME

REGULATIONS 111, SECTION 29.22(k)-1:
Alimony and separate maintenance payments; income to former wife.

Treatment of alimony payments and payments for support of children. See Ct. D. 1862, page 241.

REGULATIONS 118, SECTION 39.22(k)-1:
Alimony and separate maintenance payments; income to former wife.

Treatment of alimony payments and payments for support of children. See Ct. D. 1862, page 241.

SECTION 23(c).—DEDUCTIONS FROM GROSS INCOME: TAXES GENERALLY

REGULATIONS 118, SECTION 39.23(c)-1: Taxes. Ct. D. 1864
(Also Sections 22(a), 43; Regulations 118, Sections 39.22(a)-1, 39.43-1.)

INCOME TAX—INTERNAL REVENUE CODE OF 1939—DECISION OF COURT

1. DEDUCTIONS FROM GROSS INCOME—ACCRUAL DATE OF CONTESTED REAL PROPERTY TAXES.

The contested portion of real property taxes did not accrue in the year in which remittance was made in order to avoid seizure and sale of the property but in the year in which the contest was finally determined, since it was not until the latter year that "all events" occurred which fixed the taxpayer's liability. The amount of the tax for which the taxpayer was held not liable and which was refunded to it was not income in the year recovered since such tax was not a proper deduction in any prior tax year.

2. JUDGMENT AFFIRMED.

Judgment of the United States Court of Appeals for the Second Circuit, 279 Fed. (2d) 152, affirmed.

SUPREME COURT OF THE UNITED STATES

United States, petitioner v. *Consolidated Edison Company of New York, Inc.*

On writ of certiorari to the United States Court of Appeals for the Second Circuit

[May 22, 1961]

MR. JUSTICE WHITTAKER delivered the opinion of the Court.

Respondent brought this action in the United States District Court for the Southern District of New York to recover a claimed overpayment of federal income taxes for the year 1951. It keeps its books and files its returns on a calendar year-accrual basis. The case turns on the correct determination of the proper year of accrual and deduction of certain contested real estate taxes. Specifically, the question is whether the contested part of a real estate tax *accrued* (1) in the year it was assessed and, for the purpose—and as the only mode recognized by the local law—of avoiding seizure and sale of the property for the contested tax while the contest was pending, was "paid" by the taxpayer, or (2) in the year the contest was finally determined.

The District Court, following the holding of the Court of Claims in *Consolidated Edison Co.* v. *United States*, 133 Ct. Cl. 376, that such a "payment" of the tax "accrues the item even though payment is made under protest and even though litigation is started within the taxable year to obtain repayment," *id.*, at 383–384, held, without opinion, that the contested part of the tax accrued in the year of the "payment." On appeal, the Court of Appeals, by a divided court, held that the contested part of the tax accrued in the year the contest was finally determined, and reversed the judgment. 279 F. 2d 152. It reasoned that inasmuch as respondent was "keeping its books on the accrual basis," the contested part of the tax accrued "only when all events [had] occurred which determine[d] the fact and amount of the tax liability." *Id.*, at 155. To resolve the conflict between the decision below and *Consolidated Edison Co.* v. *United States*, *supra*, we granted certiorari. 364 U.S. 890.

During the years involved—1946 through 1950—respondent owned numerous tracts of real estate in New York City which were subject to annual local property taxes. Under the New York law, the City Council annually fixes the tax rate, and the City Tax Commission annually fixes the property valuations. Thus the amount of the tax on each tract is determined by multiplying the valuation by the tax rate. The tax rate is not contestable, but a timely application (commonly called a "protest") may be made to the City Tax Commission to correct an erroneous valuation. Among other things, the protest must state the amount which the taxpayer "consider[s] was the full value of the property on January 25 [of the current] year" thus to establish the amount of the tax that is not contested. Upon exhaustion of this administrative procedure, a review of the Commission's determination may be had by a judicial proceeding, commonly called a certiorari proceeding, in the State Supreme Court, which is the taxpayer's sole and exclusive remedy. But the institution of such a suit does not stay or suspend the maturity of the tax bill, the accrual of 7% interest on it, nor the seizure and sale of the property to satisfy the tax lien. Thus, to obtain review, the taxpayer must either "pay" the tax or suffer the interest penalty and run the risk of seizure and sale of its property.[1]

Though taxes for each of five years on hundreds of tracts are involved and the aggregate amount is very substantial, the parties very commendably stipulated in the District Court that the facts are sufficiently reflected, for the purposes of this suit, in the following simplified example:

In each of the years 1946 through 1950, respondent was notified of a tentative valuation which, at the established tax rate, would produce a tax of $100. Respondent then timely filed a *bona fide* protest (in respect of many, but not nearly all, of its tracts) stating a valuation which, at the established tax rate, would produce a tax of $85, and asking that the balance of the proposed valuation be stricken as excessive. After hearing, the Commission rejected the protest, and an assessment in the amount of $100 was made. Thereupon respondent, under protest and for the honestly stated purpose of avoiding the interest penalty and the seizure and sale of its property while it was contesting the Commission's valuation by certiorari proceedings in the state court, remitted to the city cash

[1] The procedures allowed by the laws of New York for the contest of real property taxes are more fully set forth in *Consolidated Edison Co.* v. *United States*, 133 Ct. Cl. 376, 378.

in an amount equal to the tax of $100, and immediately thereafter commenced a certiorari proceeding in the proper court, in which it again admitted liability for a tax in the amount of $85, but denied all liability for any tax in excess of that amount. In December 1951, the court, upon the consent of the parties to the action, entered its order in (each of) the certiorari proceedings fixing respondent's tax liability at $95, and thereupon the city forthwith returned $5 to respondent.

Although it was then engaged in a contest with the Commissioner in the Court of Claims over an identical question, namely, the proper income tax treatment to be accorded the $15 for each of the years 1938, 1939 and 1941—which issue was decided by the Court of Claims in December 1955 in favor of the Government, *Consolidated Edison Co.* v. *United States, supra*—respondent, in terms of the illustrative example, accrued on its books and deducted on its federal income tax returns, for each of the years 1946 through 1950, the full $100; and in its return for the year 1951—in which year the real estate tax liability was determined to be $95—respondent failed to deduct the $10 from, and included the $5 in, its gross income for that year.[2]

Believing that this treatment of the $15 in 1951 was erroneous and resulted in its paying a lesser amount of federal income taxes in each of the years 1946 through 1950, and more in the year 1951, than it should have paid,[3] respondent filed in February 1955 its claim for refund of so much of its 1951 income taxes as resulted (1) from its failure to deduct the $10 of real estate tax that was determined, in that year, to be valid, and (2) from its inclusion in gross income of the $5 returned to it in that year. Upon rejection of that claim, respondent timely brought this action in the District Court to recover the refund claimed and obtained the result already stated.

It is settled that each "taxable year" must be treated as a separate unit, and all items of gross income and deduction must be reflected in terms of their posture at the close of such year. *Burnet* v. *Sanford & Brooks Co.*, 282 U.S. 359 [Ct. D. 277, C.B. X–1, 363 (1932)]; *Heiner* v. *Mellon*, 304 U.S. 271 [Ct. D. 1345, C.B. 1938–1, 349]; *Guaranty Trust Co.* v. *Commissioner*, 303 U.S. 493 [Ct. D. 1327, C.B. 1938–1, 258]; *Security Mills Co.* v. *Commissioner*, 321 U.S. 281 [Ct. D. 1603, C.B. 1944, 526]. And the parties agree that, under the applicable federal statutes,[4] neither the Government nor an accrual-basis taxpayer may cause an item to be deducted in a year other than the one in which it accrued. *United States* v. *Anderson*, 269 U.S. 422 [T.D. 3839, C.B. V–1, 179 (1926)]; *Security Mills Co.* v. *Commissioner, supra; United States* v. *Olympic Radio & Television*, 349 U.S. 232 [Ct. D. 1785, C.B. 1955–1, 376]. They also agree that the "touchstone" for determining the year in which an item of deduction accrues is the "all events" test established by this Court in *United States* v. *Anderson, supra*,[5] and since reaffirmed by this Court on numerous occasions, so that it is now a

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[2] Respondent asserts that this treatment of the $15 in its 1951 federal income tax return was made under compulsion of the Commissioner's erroneous G.C.M. 25298, issued directly to it in 1947 (C.B. 1947–2, 39), saying, "a contested tax liability accrues not later than time of payment, notwithstanding continuation of contest. The accrual basis of accounting relates to the deductibility of unpaid items," and that the Commissioner insisted upon that treatment, despite his modification thereof in *Mim.* 6444 (C.B. 1949–2, 11), saying in pertinent part, that "payment of [a] contested tax liability as a prerequisite for appeal is not deductible under G.C.M. 25298."

[3] The economic consequences to the parties arise from the fact that corporate income tax rates (normal plus surtax) were increased from 38% in 1946 to 50¾% in 1951, and, in this particular instance, more revenue would be produced by taking the deduction in 1946–1950 than in 1951. The taxpayer recognizes that, if its position be sustained, the Commissioner will have one year after entry of final judgment herein to reaudit the taxpayer's 1946–1950 returns and to assess deficiencies based upon deduction of the $15 in those years, in accordance with the provisions of secs. 1311–1315 of the Internal Revenue Code of 1954.

[4] The applicable statutes are secs. 23(c), 41, 42, 43 and 48 of the Internal Revenue Code of 1939 (26 U.S.C. (1952 ed.), secs. 23(c), 41, 42, 43, 48). These provisions are the same as their counterparts in prior Revenue Acts and in the Internal Revenue Code of 1954. Inasmuch as those statutes are not really in contest in this case, it would serve no useful purpose even to abstract them here.

[5] In the *Anderson* case this Court declared the so-called "all events" test as follows: "In a technical legal sense it may be argued that a tax does not accrue until it has been assessed and becomes due; but it is also true that in advance of the assessment of a tax, all the events may occur which fix the amount of the tax and determine the liability of the taxpayer to pay it. In this respect, for purposes of accounting and of ascertaining true income for a given accounting period, the munitions tax here in question did not stand on a different footing than other accrued expenses appearing on appellee's books. In the economic and bookkeeping sense with which the statute and Treasury decision were concerned, the taxes had accrued." 269 U.S., at 441.

fundamental principle of tax accounting. See, *e.g.*, *Lucas* v. *American Code Co.*, 280 U.S. 445 [Ct. D. 168, C.B. IX-1, 314 (1930)]; *Brown* v. *Helvering*, 291 U.S. 193 [Ct. D. 786, C.B. XIII-1, 223 (1934)]; *Dixie Pine Co.* v. *Commissioner*, 320 U.S. 516 [Ct. D. 1598, C.B. 1944, 509]; *Security Mills Co.* v. *Commissioner*, *supra*.[6] The parties also recognize that this Court amplified, or as the Government says "added a refinement to," the "all events" test by its holding, in *Dixie Pine Co.* v. *Commissioner*, *supra*, that an accrual-basis taxpayer could not, while "contesting liability in the courts," deduct "the amount of the tax, on the theory that the state's exaction constituted a fixed and certain liability," but "must, in the circumstances, await the event of the state court litigation and might claim a deduction only for the taxable year in which its liability for the tax was finally adjudicated." 320 U.S., at 519. That principle was specifically reaffirmed in *Security Mills Co.* v. *Commissioner*, *supra*.[7]

That $85 of the $100 assessment was admitted to be owing and was intended to be paid and satisfied by the remittance, and thus accrued in the year of the remittance, is not in dispute. Respondent's good faith, in contesting $15 of the assessment, is not in dispute, for the Government expressly "disavow[s] any suggestion that the respondent * * * filed its claims against the City of New York in bad faith, * * * calculatingly inflated those claims, or * * * failed to prosecute them with diligence." Nor it is questioned that accrual of such taxes in the proper year accords with "good accounting" principles.

But concordance of the views of the parties ends at this point. The Government contends that the remittance by respondent to the city, in each of the years in question, of cash in an amount equal to the whole of the assessed tax admitted liability for, and was intended to and did constitute "payment" and "satisfaction" of, both the disputed and undisputed parts of the assessment; and that when "the taxpayer pays the item and thereby discharges its liability, the expense has been incurred and there is no longer any contingency which would prevent its accrual." Respondent, on the other hand, insists that its remittance to the city was not intended to and did not admit liability for, nor constitute "payment" and "satisfaction" of, the contested $15 of the assessment, but was, in effect, a mere deposit, in the nature of a cash bond, required of respondent, in a practical sense, by the local law as the only available mode of avoiding the risk of seizure and sale of the property for the contested tax while its validity was being diligently contested in the only way allowed by the laws of the State.

Thus the very narrow issue here is whether the remittance admitted liability for, and constituted "payment" and "satisfaction" of, the contested part of the assessment and thereby rendered it accruable in the year of the remittance. Like the Court of Appeals, we think the respondent is right in its contention, and that $10 of the contested $15 of the tax accrued when liability in that amount was finally determined by the New York court in 1951, and that the $5, for which respondent was by that judgment held not liable, and which was returned to it by the city, was not income to respondent in 1951.

Although the Government attempts to distinguish the *Anderson*, *Dixie Pine* and *Security Mills* cases on the ground that "payment" of the contested taxes had not been made in those cases, it primarily relies on the decisions of the Court of Claims in *Chestnut Securities Co.* v. *United States*, 104 Ct. Cl. 489 and *Consolidated Edison Co.* v. *United States*, 133 Ct. Cl. 376.

The *Chestnut Securities* case turned on the question whether certain judicially contested state income taxes (for the years 1936-1938) accrued when they were paid in 1940, as claimed by the accrual-basis taxpayer, or when the final judgment upholding their validity was rendered in 1942, as contended by the Government. Squarely contrary to its contention here, the Government,

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[6] In the *Dixie Pine* case, this Court reaffirmed the "all events" test as follows: "It has long been held that in order truly to reflect the income of a given year, all the events must occur in that year which fix the amount and the fact of the taxpayer's liability for items of indebtedness deducted though not paid; and this cannot be the case where the liability is contingent and is contested by the taxpayer." 320 U.S., at 519.

In the *Security Mills* case, this Court reaffirmed that test as follows: "It is settled by many decisions that a taxpayer may not accrue an expense the amount of which is unsettled or the liability for which is contingent, and this principle is fully applicable to a tax, liability for which the taxpayer denies, and payment whereof he is contesting." 321 U.S., at 284.

[7] In the *Security Mills* case, after saying "that a taxpayer may not accrue an expense the amount of which is unsettled or the liability for which is contingent," the Court concluded that "[s]ince [the taxpayer] denied liability for, and failed to pay, the tax during the taxable year 1935, it was not in a position in its tax accounting to treat the [tax] claim as an accrued liability." 321 U.S., at 284.

relying on *Security Mills Co.* v. *Commissioner*, supra, there contended that "since the [taxpayer's] accounts were kept and its tax returns made on the accrual basis, it could not take its deduction for the taxes * * * paid to the State * * * until the year 1942, when its suit for their return was finally decided adversely to it." On the facts of that case, the Court of Claims held that "the Government [was] wrong" in that contention. Although, in full consonance with the *Security Mills* case, the Court of Claims said "[o]ne is not entitled to accrue a debt or other liability which is asserted against him but which he disputes and litigates, until the litigation is concluded," it went on to say "[b]ut if a liability is asserted against him and he pays it, though under protest, and though he promptly begins litigation to get the money back, the status of the liability is that it has been discharged by payment. It is hardly conceivable that a liability asserted against him, which he had discharged by payment, has not yet 'accrued' within the meaning of the tax laws and the terminology of accounting. Accrual, from the debtor's standpoint, precedes payment, and does not survive it." 104 Ct. Cl., at 494–495. And after pointing to this Court's use of the phrase "and failed to pay" in its holding in the *Security Mills* case that "Since [the taxpayer] denied liability for, and failed to pay, the tax during the taxable year 1935, it was not in a position in its tax accounting to treat the Government's claim as an accrued liability," the Court of Claims concluded: "In the instant case the taxpayer denied liability, but paid. We think it thereby 'accrued' the taxes and interest, if accrual is requisite at all, in the case of the debtor, when actual payment has occurred." 104 Ct. Cl., at 495.

The *Consolidated Edison* case involved the same parties, facts and questions as the present case, though in respect to earlier tax years. Although recognizing that this Court's opinions in *Security Mills Co.* v. *Commissioner, supra*, and *Dixie Pine Products Co.* v. *Commissioner, supra*, had "settled" the law to be "that a taxpayer may not accrue an expense when he is denying liability and refusing and contesting its payment," the Court of Claims rejected, as "not necessarily true," the taxpayer's argument "that there must therefore be an admission or absence of denial of liability before an item may be accrued, and that the payment of the liability within the taxable year has no effect on its accrual since payment was made under protest and litigation was immediately started to obtain a repayment" (133 Ct. Cl., at 382); and, purporting to follow, but seemingly departing from, its decision in the *Chestnut Securities* case, the Court concluded "that payment of an item *which is otherwise accruable in the taxable year* accrues the item even though payment is made under protest and even though litigation is started within the taxable year to obtain repayment." 133 Ct. Cl., at 383–384. (Emphasis added.) On that conclusion the Court rendered judgment for the Government.

Just what the Court meant by the phrase we have italicized was not explained, but it is evident that if the tax item was "otherwise accruable in the taxable year," payment—whether of a character that would constitute an admission of the asserted liability or a mere deposit to enable contest of the liability—certainly would not render the item non-accruable; and if, in the absence of payment, the item was "otherwise accruable in the taxable year," payment would be immaterial, or at least unnecessary, to the question of accruability. It thus appears that the Court's judgment was contrary to its rule in that case, for, although it regarded the remittance as "payment" of the asserted tax liability, admittedly the contested part of the tax was not "*otherwise*" accruable in the taxable year."

Disagreeing with the conclusion of the Court of Claims in the *Consolidated Edison* case, the Court of Appeals concluded, we think correctly, that the question of accruability of the tax—apart from the issue respecting "payment" and "satisfaction"—was governed by the "all events" test established by this Court in *United States* v. *Anderson, supra* (see note 5), as amplified and affirmed in *Dixie Pine Co.* v. *Commissioner, supra*, and reaffirmed as amplified in *Security Mills Co.* v. *Commissioner, supra*. See notes 6 and 7.

As to whether respondent's remittance of the full $100 to the city, in the circumstances of this case, constituted an admission of liability for, and a "payment" and "satisfaction" of, the contested $15 of the assessment, the Court of Appeals recognized that this Court's opinions in the *Anderson*, *Dixie Pine* and *Security Mills* cases refer to the fact that "payment" of the taxes sought to be deducted in those cases had not been made by the taxpayers, but it

thought, and we agree, that those references were made only for the sake of complete accuracy to an important but, so far as those cases were concerned, a collateral matter, and not to the determinative considerations of those cases, which were the "all events" test as they state it.

"Payment" is not a talismanic word. It may have many meanings depending on the sense and context in which it is used. As correctly observed by the Court of Appeals, "A payment may constitute a capital expenditure, an exchange of assets, a prepaid expense, *a deposit*, or a current expense," and "[w]hen the exact nature of the payment is not immediately ascertainable because it depends on some future event, such as the outcome of litigation, its treatment for income tax purposes must await that event." 299 F. 2d, at 156. (Emphasis added.)

Of course, an unconditional "payment" made by a taxpayer in apparent "satisfaction" of an asserted matured tax liability is, without more, plain and persuasive evidence, at least against the taxpayer, that "all the events [have] occur[red] which fixed the amount of the tax and determine the liability of the taxpayer to pay it," *United States* v. *Anderson, supra*, at 441, and that the item so paid and satisfied has accrued.

But where, as stipulated by the parties in this case, the remittance or "payment" did not admit, but specifically denied, liability for, and was not intended to satisfy, the contested $15 of the assessment, but was, in effect, a mere deposit, "in the nature of a cash bond for the payment of [so much, if any, of the contested] taxes [as might] thereafter be found to be due" (*Rosenman* v. *United States*, 323 U.S. 658, 662 [Ct. D. 1628, C.B. 1945, 410], and see *Lewyt Corp.* v. *Commissioner*, 215 F. 2d 518, 523 (C.A. 2d Cir.)), and was made for the sole purpose of staying—there being no other way to stay—an otherwise possible seizure and sale of the property for the contested tax while its validity was being honestly and diligently contested in the only way allowed by the law of the State, it will not do to say that the taxpayer has made an unconditional "payment" in apparent "satisfaction" of the contested part of an asserted matured tax liability, and thereby rendered it immediately accruable.

We therefore conclude that $10 of the contested $15 tax liability accrued not in the year of the remittance, but in 1951 when the New York court entered its final order determining that liability; and that the $5, for which respondent was held not liable by that judgment and which was returned to it by the city, was not income to respondent in 1951.

Affirmed.

SECTION 23(s).—DEDUCTIONS FROM GROSS INCOME: NET OPERATING LOSS DEDUCTION

De facto liquidation doctrine applied in net operating loss cases. See Rev. Rul. 61-191, page 251.

SECTION 23(u).—DEDUCTIONS FROM GROSS INCOME: ALIMONY, ETC., PAYMENTS

REGULATIONS 111, SECTION 29.23(u)-1:
Periodic alimony payments.

Treatment of alimony payments and payments for support of children. See Ct. D. 1862, below.

REGULATIONS 118, SECTION 39.23(u)-1: Periodic alimony payments. Ct. D. 1862

(Also Section 22(k); Regulations 118, Section 39.22 (k)-1.)

(Also Sections 22(k), 23(u); Regulations 111, Sections 29.22(k)-1, 29.23(u)-1.)

(Also Part I, Sections 71, 215; 26 CFR 1.71-1, 1.215-1.)

INCOME TAX—INTERNAL REVENUE CODE OF 1939—DECISION OF COURT.

1. DEDUCTIONS FROM GROSS INCOME—ALIMONY PAYMENTS—ALLOCATIONS FOR CHILD SUPPORT MUST BE SPECIFICALLY "FIXED."

Congress intended that to come within the exception portion of section 22(k) of the Internal Revenue Code of 1939, an agreement providing for periodic payments must specifically state the amounts or parts thereof allocable to the support of children. The statutory requirement is strict and does not allow for an allocation based on "a sufficiently clear purpose" in the instrument. Accordingly, an agreement providing for payment of certain monies to the wife for support of herself and children which does not "fix" an amount for child support but merely provides for a specific percentage reduction in payment to the wife upon marriage, emancipation, or death of any child, fails to meet the strict requirements of the statute and the payments are fully deductible by the husband. Further, a local law's construction of non-specific provisions imposing upon a wife the duty to use a certain portion of the payments solely for child support has no effect for Federal income tax purposes.

2. JUDGMENT AFFIRMED.

Judgment of the United States Circuit Court of Appeals for the Second Circuit, 279 Fed. (2d) 354, affirmed.

SUPREME COURT OF THE UNITED STATES

Commissioner of Internal Revenue, petitioner v. *Jerry Lester*

On writ of certiorari to the United States Court of Appeals for the Second Circuit

[May 22, 1961]

MR. JUSTICE CLARK delivered the opinion of the Court.

The sole question presented by this suit, in which the Government seeks to recover personal income tax deficiencies, involves the validity of respondent's deductions from his gross income for the taxable years 1951 and 1952 of the whole of his periodic payments during those years to his divorced wife pursuant to a written agreement entered into by them and approved by the divorce court. The Commissioner claims that language in this agreement providing "[i]n the event that any of the [three] children of the parties hereto shall marry, become emancipated, or die, then the payments herein specified shall . . . be reduced in a sum equal to one-sixth of the payments which would thereafter otherwise accrue" sufficiently identifies one-half of the periodic payments as having been "payable for the support" of the taxpayer's minor children under § 22(k) of the Internal Revenue Code of 1939 and, therefore, not deductible by him under § 23(u) of the Code.[1] The Tax Court approved the Commissioner's disallowance, 32 T.C. 1156, but the Court of Appeals reversed, 279 F. 2d 354, holding that the agreement did not "fix" with requisite clarity any specific amount or portion of the periodic payments as payable for the support of the children and that all sums paid to the wife under the agreement were, therefore, deductible from respondent's gross income under the alimony provision of § 23(u). To resolve a conflict among the Courts of Appeals on the question,[2] we granted certiorari. 364 U.S. 890. We have concluded that the Congress intended that, to come within

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[1] Section 22(k) of the Internal Revenue Code of 1939, 56 Stat. 816–817, provided in part that

". . . periodic payments . . . received [by the wife] subsequent to [a decree of divorce] . . . in discharge of . . . a legal obligation which, because of the marital or family relationship, is imposed upon or incurred by such husband under . . . a written instrument incident to such divorce . . . shall be includible in the gross income of such wife . . . . This subsection shall not apply to that part of any such periodic payment *which the terms of the . . . written instrument fix,* in terms of . . . a portion of the payment, as a sum which is payable for the support of minor children of such husband." (Emphasis added.)

Section 23(u), 56 Stat. 817, stated in pertinent part that there shall be allowed as a deduction

"[i]n the case of a husband described in section 22(k), amounts includible under section 22(k) in the gross income of his wife, payment of which is made within the husband's taxable year."

[2] Both *Metcalf* v. *Commissioner,* 271 F. 2d 288 (C.A. 1st Cir. 1959), *Eisinger* v. *Commissioner,* 250 F. 2d 303 (C.A. 9th Cir. 1957) [Ct. D. 1834, C.B. 1959–1, 661], have arrived at conclusions contrary to those of the court below.

the exception portion of § 22(k), the agreement providing for the periodic payments must specifically state the amounts or parts thereof allocable to the support of the children. Accordingly, we affirm the judgment of the Court of Appeals.

Prior to 1942, a taxpayer was generally not entitled to deduct from gross income amounts payable to a former spouse as alimony, *Douglas* v. *Willcuts*, 296 U.S. 1 (1935) [Ct. D. 1041, C.B. XIV–2, 250 (1935)], except in situations in which the divorce decree, the settlement agreement and state law operated as a complete discharge of the liability for support. *Helvering* v. *Fitch*, 309 U.S. 149 (1940) [Ct. D. 1439, C.B. 1940–1, 165]. The hearings, Senate debates and the Report of the Ways and Means Committee of the House all indicate that it was the intention of Congress, in enacting § 22(k) and § 22(u) of the Code, to eliminate the uncertain and inconsistent tax consequences resulting from the many variations in state law. "[T]he amendments are designed to remove the uncertainty as to the tax consequences of payments made to a divorced spouse . . . ." S. Rep. No. 673, Pt. 1, 77th Cong., 1st Sess. 32. They "will produce uniformity in the treatment of amounts paid . . . regardless of variance in the laws of different States . . . ." H.R. Rep. No. 2333, 77th Cong., 2d Sess. 72. In addition, Congress realized that the "increased surtax rates [3] would intensify" the hardship on the husband who, in many cases, "would not have sufficient income left after paying alimony to meet his income tax obligations," H.R. Rep. No. 2333, 77th Cong., 2d Sess. 46, and perhaps also that on the other hand, the wife, generally being in a lower income tax bracket than the husband, could more easily protect herself in the agreement and in the final analysis receive a larger net payment from the husband if he could deduct the gross payment from his income.

The first version of § 22(k) was proposed by the Senate as an amendment to the Revenue Act of 1941. The sums going to child support were to be includible in the husband's gross income only if the amount thereof was "specifically designated as a sum payable for support of minor children of the spouses." H.R. 5417, 77th Cong., 1st Sess., § 117. The proposed amendment thus drew a distinction between a case in which the amount for child support was "specifically designated" in the agreement, and one in which there was no such designation. In the latter event, "the whole of such amounts are includible in the income of the wife . . . ." S. Rep. No. 673, Pt. 1, 77th Cong., 1st Sess. 35. Action on the bill was deferred by the conference committee [4] and hearings on the measure were again held the following year. The subsequent Report of the Senate Finance Committee on § 22(k) carried forward the term "specifically designated," used in the 1941 Report (No. 673), with this observation:

"If, however, the periodic payments . . . are received by the wife for the support and maintenance of herself and of minor children of the husband without such specific designation of the portion for the support of such children, then the whole of such amounts is includible in the income of the wife as provided in section 22(k) . . . ." S. Rep. No. 1631, 77th Cong., 2d Sess. 86.

As finally enacted in 1942, the Congress used the word "fix" instead of the term "specifically designated," but the change was explained in the Senate hearings as "a little more streamlined language." Hearings before Senate Committee on Finance on H.R. 7378, 77th Cong., 2d Sess. 48. As the Office of the Legislative Counsel reported to the Senate Committee:

"If an amount is specified in the decree of divorce attributable to the support of minor children, that amount is not income of the wife . . . . If, however, that amount paid the wife includes the support of children, *but no amount is specified for the support of the children*, the entire amount goes into the income of the wife . . . ." *Ibid.* (Italics supplied.)

This language leaves no room for doubt. The agreement must expressly specify or "fix" a sum certain or percentage of the payment for child support before any of the payment is excluded from the wife's income. The statutory requirement is strict and carefully worded. It does not say that "a sufficiently clear purpose" on the part of the parties is sufficient to shift the tax. It says that the "written instrument" must "fix" that "portion of the payment" which is to go

[3] Sections 22(k) and 23(u) were enacted as part of the Revenue Act of 1942 which provided for greatly increased tax revenue to meet the expenses of World War II.
[4] H.R. Rep. No. 1203, 77th Cong., 1st Sess. 11.

to the support of the children. Otherwise, the wife must pay the tax on the whole payment. We are obliged to enforce this mandate of the Congress.

One of the basic precepts of the income tax law is that "[t]he income that is subject to a man's unfettered command and that he is free to enjoy at his own option may be taxed to him as his income, whether he sees fit to enjoy it or not." *Corliss* v. *Bowers*, 281 U.S. 376, 378 (1930) [Ct. D. 188, C.B. ix-1, 154]. Under the type of agreement here, the wife is free to spend the monies paid under the agreement as she sees fit. "The power to dispose of income is the equivalent of ownership of it." *Helvering* v. *Horst*, 311 U.S. 112, 118 (1940) [Ct. D. 1472, C.B. 1940-2, 206]. Including the entire payments in the wife's gross income under such circumstances, therefore, comports with the underlying philosophy of the Code. And, as we have frequently stated, the Code must be given "as great an internal symmetry and consistency as its words permit." *United States* v. *Olympic Radio & Television*, 349 U.S. 232, 236 (1955) [Ct. D. 1785, C.B. 1955-1, 376].

It does not appear that the Congress was concerned with the perhaps restricted uses of unspecified child-support payments permitted the wife by state law when it made those sums includible within the wife's alimony income. Its concern was with a revenue measure and with the specificity, for income tax purposes, of the amount payable under the terms of the written agreement for support of the children. Therefore, in construing that revenue act, we too are unconcerned with the variant legal obligations, if any, which such an agreement, by construction of its non-specific provisions under local rules, imposes upon the wife to use a certain portion of the payments solely for the support of the children. The Code merely affords the husband a deduction for any portion of such payment not specifically earmarked in the agreement as payable for the support of the children.

As we read § 22(k), the Congress was in effect giving the husband and wife the power to shift a portion of the tax burden from the wife to the husband by the use of a simple provision in the settlement agreement which fixed the specific portion of the periodic payment made to the wife as payable for the support of the children. Here the agreement does not so specifically provide. On the contrary, it calls merely for the payment of certain monies to the wife for the support of herself and the children. The Commissioner makes much of the fact that the agreement provides that as, if, and when any one of the children married, became emancipated or died the total payment would be reduced by one-sixth, saying that this provision did "fix" one-half (one-sixth multiplied by three, the number of children) of the total payment as payable for the support of the children. However, the agreements also pretermitted the entire payment in the event of the wife's remarriage and it is as consistent to say that this provision had just the opposite effect. It was just such uncertainty in tax consequences that the Congress intended to and, we believe, did eliminate when it said that the child support payments should be "specifically designated" or, as the section finally directed, "fixed." It does not say that "a sufficiently clear purpose" on the part of the parties would satisfy. It says that the written instrument must "fix" that amount or "portion of the payment" which is to go to the support of the children.

The Commissioner contends that administrative interpretation has been consistently to the contrary. It appears, however, that there was such a contrariety of opinion among the Courts of Appeals that the Commissioner was obliged as late as 1959 to issue a Revenue Ruling which stated that the Service would follow the rationale of *Eisinger* v. *Commissioner*, 250 F. 2d 303 (C.A. 9th Cir. 1957) [Ct. D. 1834, C.B. 1959-1, 661],[5] but that *Weil* v. *Commissioner*, 240 F. 2d 584 (C.A. 2d Cir. 1957),[6] would be followed "in cases involving similar facts and circumstances." Rev. Rul. 59-93, 1959-1 Cum. Bull. 22, 23.

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[5] The court there approved the rule that "when the settlement agreement, read as a whole, discloses that the parties have earmarked or designated . . . the payments to be made, one part to be payable for alimony, and another part to be payable for the support of children, with sufficient certainty and specificity to readily determine which is which without reference to contingencies which may never come in being, then the 'part of any periodic payment' has been fixed 'by the terms of the decree or written instrument' . . . ." 250 F. 2d, at 308.

[6] In that case the agreement provided for reductions only in the event the divorced wife remarried. The court stated that "[t]he fortuitous or incidental mention of a figure in a provision meant to be inoperative, unless some more or less probable future event occurred, will not suffice to shift the tax burden from the wife to the husband." 240 F. 2d, at 588.

All of these considerations lead to the conclusion that if there is to be certainty in the tax consequences of such agreements the allocations to child support made therein must be "specifically designated" and not left to determination by inference or conjecture. We believe that the Congress has so demanded in § 22(k). After all, the parties may for tax purposes act as their best interests dictate, provided, as that section requires, their action be clear and specific. Certainly the Congress has required no more and expects no less.

Affirmed.

Mr. Justice Douglas concurs in a separate opinion.

PART IV.—ACCOUNTING PERIODS AND METHODS OF ACCOUNTING

SECTION 41.—GENERAL RULE

REGULATIONS 118, SECTION 39.41–1: Computation of net income. Ct. D. 1865

(Also Part I, Sections 446, 451; 26 CFR 1.446–1, 1.451–1.)

INCOME TAX—INTERNAL REVENUE CODES OF 1939 AND 1954—DECISION OF COURT

1. PERIOD IN WHICH INCOME INCLUDED—PREPAID AUTOMOBILE CLUB MEMBERSHIP DUES—PRO RATA ACCRUAL OVER MEMBERSHIP PERIOD DENIED.

Prepaid membership dues paid to an automobile club are includible in income in the year received and may not be accrued on a prorated monthly basis over the period of the membership contract. Taxpayer's method of prorating such dues, because services to be rendered to its members would normally extend beyond the taxable year in which the dues were received, and of deducting expenses on a monthly basis upon an estimate of overall expenses computed on a group or pool basis was a "purely artificial" method since services were performed only upon a member's demand and taxpayer's performance was not related to fixed dates. While taxpayer's method was in accord with accepted business accounting practices, it was not binding on the government for income tax purposes, since it did not clearly reflect income. Whether or not the opinion in *Automobile Club of Michigan* v. *Commissioner*, 353 U.S. 180 (1957) Ct.D. 1807, C.B. 1957–1, 513, which held that a similar method of accounting was "artificial," is controlling in this case because of a difference in proof, the retroactive repeal by Congress of the "prepaid income" and "reserve for estimated expense" provisions in Sections 452 and 462 of the Internal Revenue Code of 1954, and the later enactment of Section 455 allowing deferral of prepaid subscription income, are considerations which require rejection of deferral of prepaid membership dues.

2. JUDGMENT AFFIRMED.

Judgment of the United States Court of Claims, 181 Fed. Supp. 255, affirmed.

SUPREME COURT OF THE UNITED STATES

United States v. *American Automobile Association, Petitioner*

On writ of certiorari to the United States Court of Claims

[June 19, 1961]

MR. JUSTICE CLARK delivered the opinion of the Court.

In this suit for refund of federal income taxes the petitioner, American Automobile Association, seeks determination of its tax liability for the years 1952

and 1953. Returns filed for its taxable calendar years were prepared on the basis of the same accrual method of accounting as was used in keeping its books. The Association reported as gross income only that portion of the total prepaid annual membership dues, actually received or collected in the calendar year, which ratably corresponded with the number of membership months, covered by those dues, occurring within the same taxable calendar year. The balance was reserved for ratable monthly accrual over the remaining membership period in the following calendar year as deferred or unearned income reflecting an estimated future service expense to members. The Commissioner contends that petitioner should have reported in its gross income for each year the entire amount of membership dues actually received in the taxable calendar year without regard to expected future service expense in the subsequent year. The sole point at issue, therefore, is in what year the prepaid dues are taxable as income.

In auditing the Association's returns for the years 1952 through 1954, the Commissioner, in exercise of his discretion under section 41 of the Internal Revenue Code of 1939,[1] determined not to accept the taxpayer's accounting system. As a result, adjustments were made for those years principally by adding to gross income for each taxable year the amount of prepaid dues which the Association had received but not recognized as income, and subtracting from gross income amounts recognized in the year although actually received in the prior year. A net operating loss claimed for 1954 and corresponding carryback deductions were greatly reduced, and tax deficiencies were assessed for 1952 and 1953. Petitioner paid the deficiencies and its timely claim for refund was denied. Suit to recover was instituted in the Court of Claims, but the court sustained the Commissioner, 181 F. Supp. 255. Recognizing a conflict between the decision below and that in *Bressner Radio, Inc.*, v. *Commissioner*, 267 F. 2d 520, we granted certiorari. 364 U.S. 813. We have concluded that for tax purposes the dues must be included as income in the calendar year of their actual receipt.

The Association is a national automobile club organized as a nonstock membership corporation with its principal office in Washington, D.C. It provides a variety of services[2] to the members of affiliated local automobile clubs and those of ten clubs which taxpayer itself directly operates as divisions, but such services are rendered solely upon a member's demand. Its income is derived primarily from dues paid one year in advance by members of the clubs. Memberships may commence or be renewed in any month of the year. For many years, the association has employed an accrual method of accounting and the calendar year as its taxable year. It is admitted that for its purposes the method used is in accord with generally accepted commercial accounting principles. The membership dues, as received, were deposited in the Association's bank accounts without restriction as to their use for any of its corporate purposes. However, for the Association's own accounting purposes the dues were treated in its books as income received ratably[3] over the 12-month membership period. The portions thereof ratably attributable to membership months occurring beyond the year of receipt, *i.e.*, in a second calendar year, were reflected in the Association's books at the close of the first year as unearned or deferred income. Certain operating expenses were chargeable as prepaid membership cost and deducted ratably over the same periods of time as those over which dues were recognized as income.

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[1] A taxpayer's "net income shall be computed * * * in accordance with the method of accounting regularly employed in keeping the books * * * but * * * if the method employed does not clearly reflect the income, the computation shall be made in accordance with such method as in the opinion of the Commissioner does clearly reflect the income * * *." 53 Stat. 24, 26 U.S.C. (1952 ed.) sec. 41. See also the similar provision in the Internal Revenue Code of 1954, 26 U.S.C. (1958 ed.) sec. 446.

[2] These generally include road maps, routing, tour books, etc.; emergency road service through contracts with local garages; bail bond protection; personal automobile accident insurance and theft protection; and, in some of its divisions, motor license procurement, brake and headlight adjustment service, notarial duties and advice in the prosecution of small claims.

[3] In 1952 and 1953 dues collected in any month were accounted as income to the extent of one-twenty-fourth for that month (on the assumption that the mean date of receipt was the middle of the month), one-twelfth for each of the next eleven months, and again one-twenty-fourth in the anniversary month. In 1954, however, guided by its own statistical average experience, the Association changed its system so as to more simply reach almost the same result by charging to year of receipt, without regard to month of receipt, one-half of the entire dues payment and deferring the balance to the following year.

The Court of Claims bottomed its opinion on *Automobile Club of Michigan* v. *Commissioner*, 353 U.S. 180 (1957) [Ct.D. 1807, C.B. 1957–1, 513], finding that "the method of treatment of prepaid automobile club membership dues employed [by the Association here was] * * * for Federal income tax purposes, 'purely artificial.'" 181 F. Supp. 255, 258. It accepted that case as "a rejection by the Supreme Court of the accounting method advanced by plaintiff in the case at bar." *Ibid.* The Association does not deny that its accounting system is substantially identical to that used by the petitioner in *Michigan*. It maintains, however, that *Michigan* does not control this case because of a difference in proof, *i.e.*, that in this case the record contains expert accounting testimony indicating that the system used was in accord with generally accepted accounting principles; that its proof of cost of member service was detailed, and that the correlation between that cost and the period of time over which the dues were credited as income was shown and justified by proof of experience. The holding of *Michigan*, however, that the system of accounting was "purely artificial" was based upon the finding that "substantially all services are performed only upon a member's demand and the taxpayer's performance was not related to fixed dates after the tax year." 353 U.S. 180, 189, note 20. That is also true here.[4] As the Association's own accounting expert testified:

> You are dealing with a group or pool. Any pooling or risk situation, particular members may in a particular year require very little of a specific service that is rendered to certain other members. I wouldn't know what the experience on that would be, but I would think it would be rather irregular between individual members * * * I am buying the availability of services, the protection * * * Frankly, the irregularity of the actual furnishing of the maps and helping you out when you run out of gasoline and so on, I frankly don't think that has a blessed thing to do with the overall accounting.

It may be true that to the accountant the actual incidence of cost in serving an individual member in exchange for his individual dues is inconsequential, or, from the viewpoint of commercial accounting, unessential to determination and disclosure of the overall financial condition of the Association. That "irregularity," however, is highly relevant to the clarity of an accounting system which defers receipt, as earned income, of dues to a taxable period in which no, some, or all the services paid for by those dues may or may not be rendered. The Code exacts its revenue from the individual member's dues which, no one disputes, constitute income. When their receipt as earned income is recognized ratably over two calendar years, without regard to correspondingly fixed individual expense or performance justification, but consistently with overall experience, their accounting doubtless presents a rather accurate image of the total financial structure, but fails to respect the criteria of annual tax accounting and may be rejected by the Commissioner.

The Association further contends that the findings of the court below support its position. We think not. The Court of Claims' only finding as to the accounting system itself is as follows:

> 22. The method of accounting employed by plaintiff during the years in issue has been used regularly by plaintiff since 1931 and is in accord with generally accepted commercial accounting principles and practices and was, prior to the adverse determination by the Commissioner of the Internal Revenue, customarily and generally employed in the motor club field.

This is only to say that in performing the function of business accounting the method employed by the Association "is in accord with generally accepted commercial accounting principles and practices." It is not to hold that for income tax purposes it so clearly reflects income as to be binding on the Treasury.[5] Likewise, other findings merely reflecting statistical computations of average monthly cost per member on a group or pool basis are without determinant significance to our decision that the federal revenue cannot, without legislative consent and over objection of the Commissioner, be made to depend upon average

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[4] *Beacon Publishing Co.* v. *Commissioner*, 218 F. 2d 697, and *Schuessler* v. *Commissioner*, 230 F. 2d 722, may be distinguished from the present case on the same grounds which made them distinguishable in *Automobile Club of Michigan* v. *Commissioner*, 353 U.S. 180, 189, note 20.

[5] The Hearing Commissioner of the Court of Claims had specifically found as fact that petitioner's "method of accounting * * * clearly reflected its net income for such years." The court, however, did not adopt that finding.

experience in rendering performance and turning a profit. Indeed, such tabulations themselves demonstrate the inadequacy from an income tax standpoint of the *pro rata* method of allocating each year's membership dues in equal monthly installments not in fact related to the expenses incurred. Not only did individually incurred expenses actually vary from month to month, but even the average expense varied—recognition of income nonetheless remaining ratably constant. Although the findings below seem to indicate that it would produce substantially the same result as that of the system of ratable monthly recognition actually employed, we consider similarly unsatisfactory, from an income tax standpoint, allocation of monthly dues to gross monthly income to the extent of actual service expenditures for the same month computed on a group or pool basis. In addition, the Association's election in 1954 to change its monthly recognition formula [6] to one which treats one-half of the dues as income in the year of receipt and the other half as income received in the subsequent year, without regard to month of payment, only more clearly indicates the artificiality of its method, at least so far as controlling tax purposes are concerned. Moreover, the Association realized that the findings of the Court of Claims were not alone sufficient for its purposes. In its petition for rehearing below, petitioner specifically asked that they be amended and enlarged, especially as to No. 22 set out above. Rehearing and amendment were denied.

Whether or not the Court's judgment in *Michigan* controls our disposition of this case, there are other considerations requiring our affirmance. They concern the action of the Congress with respect to its own positive and express statutory authorization of employment of such sound commercial accounting practices in reporting taxable income. In 1954 the Congress found dissatisfaction in the fact that "as a result of court decisions and rulings, there have developed many divergencies between the computation of income for tax purposes and income for business purposes as computed under generally accepted accounting principles. The areas of difference are confined almost entirely to questions of when certain types of revenue and expenses should be taken into account in arriving at net income." House Ways and Means Committee Report, H.R. Rep. No. 1337, 83d Cong., 2d Sess. 48. As a result, it introduced into the Internal Revenue Code of 1954 section 452 and section 462 [7] which specifically permitted essentially the same practice as was employed by the Association here.[8] Only one year later, however, in June 1955, the Congress repealed these sections retroactively. It appears that in this action Congress first overruled the long administrative practice of the Commissioner and holding of the courts in disallowing such deferral of income for tax purposes and then within a year reversed its own action. This repeal, we believe, confirms our view that the method used by the Association could be rejected by the Commissioner. While the claim is made that Congress did not "intend to disturb prior law as it affected permissable accrual accounting provisions for tax purposes. . . ." H.R. Rep. No. 293, 84th Cong., 1st Sess. 4 [C.B. 1955–2, 852], the cold fact is that it repealed the only law incontestably permitting the practice upon which the Association depends. To say that, as to taxpayers using such systems, Congress was merely declaring existing law when it adopted section 452 in 1954, and that it was merely restoring unaffected the same prior law when it repealed the new section in 1955 for good reason, is a contradiction in itself, "varnishing nonsense with the charm of sound." Instead of constituting a merely duplicative creation, the fact is that section 452 for the first time specifically declared petitioner's system of accounting to be acceptable for income tax purposes, and overruled the long-standing position of the Commissioner and courts to the contrary. And the repeal of the section the following year, upon insistence by the Treasury that the proposed endorsement of such tax accounting would have a disastrous impact on the Government's revenue, was just as clearly a mandate from the Congress that petitioner's system was not acceptable for tax purposes. To interpret its careful consideration of the problem otherwise is to accuse the Congress of engaging in sciamachy. We are further confirmed in this view by consideration of the even more recent action of the Congress in 1958, subsequent to the decision in

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[6] See note 2, *supra*.

[7] 26 U.S.C. (1952 ed., Supp. II) secs. 452, 462, repealed, 69 Stat. 134 (1955).

[8] The Senate Report included this language:
"Under the 1939 Code, regardless of the method of accounting * * * amounts are includible in gross income by the recipient not later than the time of receipt if they are subject to free and unrestricted use by the taxpayer even though the payments are for goods or services to be provided by the taxpayer at a future time." S. Rep. No. 1622, 83d Cong., 2d Sess. 301.

Michigan, supra. In that year section 455[9] was added to the Internal Revenue Code of 1954. It permits publishers to defer receipt as income of prepaid subscriptions of newspapers, magazines and periodicals. An effort was made in the Senate to add a provision in section 455 which would extend its coverage to prepaid automobile club membership dues.[10] However, in conference the House Conferees refused to accept this amendment. Senator Byrd explained the rejection of the amendment to the Senate (104 Cong. Rec., Part 14, p. 17744):

> It was the position of the House conferees that this matter of prepaid dues and fees received by nonprofit service organizations was a part of the entire subject dealing with the treatment of prepaid income and that such subject should be left for study of this entire problem * * *.[11]

It appears, therefore, that, pending its own further study, Congress has given publishers but denied automobile clubs the very relief that the Association seeks in this Court.

To recapitulate, it appears that Congress has long been aware of the problem this case presents. In 1954 it enacted section 452 and section 462, but quickly repealed them. Since that time Congress has authorized the desired accounting only in the instance of prepaid subscription income, which, as was pointed out in *Michigan*, is ratably earned by performance on "publication dates after the tax year." 353 U.S. 180, 189, note 20. It has refused to enlarge section 455 to include prepaid membership dues. At the very least, this background indicates congressional recognition of the complications inherent in the problem and its seriousness to the general revenue. We must leave to the Congress the fashioning of a rule which, in any event, must have wide ramifications. The Committees of the Congress have standing committees expertly grounded in tax problems, with jurisdiction covering the whole field of taxation and facilities for studying considerations of policy as between the various taxpayers and the necessities of the general revenues. The validity of the long established policy of the Court in deferring, where possible, to congressional procedures in the tax field is clearly indicated in this case.[12] Finding only that, in light of existing provisions not specifically authorizing it, the exercise of the Commissioner's discretion in rejecting the Association's accounting system was not unsound, we need not anticipate what will be the product of further "study of this entire problem."

Affirmed.

MR. JUSTICE STEWART, whom MR. JUSTICE DOUGLAS, MR. JUSTICE HARLAN, and MR. JUSTICE WHITTAKER join, dissenting, in a separate opinion.

SECTION 43.—PERIOD FOR WHICH DEDUCTIONS AND CREDITS TAKEN

REGULATIONS 118, SECTION 39.43–1: "Paid or incurred" and "paid or accrued."

Whether contested real property taxes accrue in the year of remittance. See Ct. D. 1864, page 236.

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[9] 28 U.S.C. (1958 ed.) sec. 455.

[10] An unsuccessful attempt to induce congressional action on this problem was made last year, see H.R. 11266, 86th Cong., 2d Sess., which passed in the House in August, 1960, 106 Cong. Rec. Daily ed.) 16256 but failed to draw any action by the Senate before adjournment. An identical bill is currently pending, see H.R. 929, 87th Cong., 1st Sess., and H.R. Rep. No. 381 accompanying the bill and recommending its passage. Under that measure the taxpayer's liability to its members *"shall be deemed to exist ratably* over the period that such services are required to be rendered, or * * * privileges * * * made available."

[11] The Eighty-fourth Congress started the study of "legislation dealing with prepaid income and reserves for estimated expenses * * *." S. Rep. No. 372, 84th Cong., 1st Sess. 6 [C.B. 1955–2, 858].

[12] In 1955 it was estimated that transitional loss of revenue under sec. 452 and sec. 462, repealed that year, would total in excess of a billion dollars. H.R. Rep. No. 293, 84th Cong., 1st Sess. 3 [C.B. 1955–2, 852]. That this impact on the revenue continues to be an important factor in congressional consideration of the problem is indicated by the observation of the House Committee on Ways and Means that a "transitional rule" is necessary "to minimize the initial revenue impact" of the measure currently pending. H.R. Rep. No. 381, 87th Cong., 1st Sess. 4. That the system used by petitioner here is, perhaps, presently not uncommon may be indicated by the fact that during this Term alone several cases involving similar systems have reached this Court.

PART V.—RETURNS AND PAYMENT OF TAX

SECTION 55.—PUBLICITY OF RETURNS

26 CFR 458.324: Inspection of returns by committees of Congress other than those enumerated in section 55(d) of the Internal Revenue Code of 1939.

Inspection of certain returns by the House Committee on Public Works. See E.O. 10947, page 227.

Inspection of certain returns by the House Committee on Government Operations. See E.O. 10966, page 228.

26 CFR 458.326: Inspection of returns by the Advisory Commission on Intergovernmental Relations.

Inspection of returns by the Advisory Commission on Intergovernmental Relations. See E.O. 10962, page 229.

Regulations under the Internal Revenue Code of 1939. See T.D. 6570, page 229.

SUBCHAPTER C.—SUPPLEMENTAL PROVISIONS

SUPPLEMENT B.—COMPUTATION OF NET INCOME

SECTION 115.—DISTRIBUTIONS BY CORPORATIONS

REGULATIONS 111, SECTION 29.115–1: Dividends: (Also Section 22(b); Regulations 111, Section 29.22(b)(1)–1.) (Also Sections 22(b), 115; Regulations 118, Sections 39.22(b)(1)–1, 39.115(a)–1.) (Also Part I, Sections 101, 316; 26 CFR 1.101–1, 1.316–1.) — Rev. Rul. 61–134[1]

The Internal Revenue Service will not follow the decision of the United States Court of Appeals for the Sixth Circuit in *Francis H. W. and Phyllis A. Ducros* v. *Commissioner*, 272 Fed. (2d) 49(1959).

In the *Ducros* case, a closely held corporation caused insurance to be taken out on the life of a corporate officer with the intention of distributing the proceeds to various shareholders by making them beneficiaries. The corporation paid all the premiums and had all the incidents of ownership.

The Service contended that the proceeds were a taxable dividend flowing from the corporation to the beneficiary-stockholders.

[1] Based on Technical Information Release 321, dated June 9, 1961.

The beneficiary-stockholders in *Ducros* contended the amounts were excludable from gross income as the proceeds of a life insurance contract paid by reason of the insured's death.

The court held that, under local law, there was a valid life insurance contract and that the insurance proceeds were never an asset of, nor distributed by, the corporation and, therefore, the proceeds did not constitute a taxable dividend.

In so holding, the court distinguished *Edwin L. Cummings et al.* v. *Commissioner*, 73 Fed. (2d) 477, Ct. D. 952, C.B. XIV-1, 209 (1935), where the insurance proceeds were paid to the corporation which, in turn, distributed the proceeds to the stockholders, and *Delia B. Golden* v. *Commissioner*, 113 Fed. (2d) 590 (1940), where, although the insurance proceeds were paid to a trust as agent of the corporation for distribution to stockholders, the corporation retained valuable incidents of ownership.

It is the position of the Service that life insurance proceeds paid to shareholders of a corporation are taxable as dividends in cases where the corporation uses its earnings to pay the insurance premiums and has all the incidents of ownership including the right to name itself beneficiary, even though the corporation does not name itself beneficiary and, therefore, is not entitled to, and does not in fact, receive the proceeds.

Although review by the Supreme Court of the United States was not requested in the *Ducros* case, the decision will not be followed as a precedent in the disposition of similar cases, and the Service will maintain its position pending further developments on the issue.

REGULATIONS 118, SECTION 39.115(a)-1: Dividends.

Proceeds of insurance on the life of an officer of a closely held corporation paid directly to shareholders of the corporation. See Rev. Rul. 61-134, page 250.

SECTION 122.—NET OPERATING LOSS DEDUCTION

REGULATIONS 118, SECTION 39.122-4: Computation of net operating loss carryback. Rev. Rul. 61-191

(Also Section 23(s).)

(Also Part I, Section 172; 26 CFR 1.172-1.)

Losses sustained or excess profits tax credits remaining unused by a corporation subsequent to the date that it is de facto dissolved may not be carried back to prior taxable years. For the purpose of such carrybacks a de facto dissolution occurs when a corporation has disposed of all or most of its operating assets, terminated its regular business activities, and become a mere shell, a corporation in name and semblance only, without real corporate substance, serving no real corporate purpose, and having no valid or compelling business reason for continuing its existence, even though not formally dissolved.

Nonacquiescence substituted for acquiescence in *Acampo Winery and Distilleries, Inc.* v. *Commissioner*, 7 T.C. 629.

Reconsideration has been given to the acquiescence by the Commissioner of Internal Revenue in the decision in *Acampo Winery and Distilleries, Incorporated* v. *Commissioner*, 7 T.C. 629 (1946), ac-

quiescence, C.B. 1949–1, 1, insofar as it relates to the fourth issue involved, namely, a carryback to the year 1943 of net operating losses sustained in the years 1944 and 1945.

In the *Acampo* case, the taxpayer corporation in the early part of 1943 had a large inventory of wine which the majority of its stockholders desired to dispose of but which the officers and directors refused to permit it to sell because of the heavy taxes which would result. Accordingly, on February 11, 1943, a majority of the stockholders approved a plan of dissolution under which the corporation was to distribute the bulk of its assets to three trustees, who, acting in behalf of the stockholders, were to sell the assets, thus avoiding the tax liability which would have been incurred by the corporation were it to make such a sale. The assets involved included wine, winery, real estate, and other items. On or about February 26, 1943, the corporation made appropriate conveyances thereof to the trustees, retaining only a small portion of the wine and a few other assets to meet some commitments, to pay some taxes and other obligations, and to pay the expenses of winding up its affairs. Thereupon, the corporation ceased doing business and proceeded to conclude its affairs in complete liquidation and dissolution. On March 25, 1943, the trustees sold the assets conveyed to them to a third party.

In 1944 and 1945 the corporation sustained net losses which it sought to carry back and use as a net operating loss deduction for 1943, under sections 23(s) and 122 of the Internal Revenue Code of 1939. The Commissioner disallowed the net operating loss deduction on the ground that the corporation was substantially liquidated and marking time during 1944 and 1945 and that it was no more the taxpayer it was in previous years, in substance and in fact, than if it had formally changed its existence. However, the Tax Court of the United States allowed the carryback and deduction in question, stating, in effect that the words of the statute are general in their application and that to warrant denial of the carryback something which is not there would have to be read into the pertinent provisions of law to limit them so that they would not apply.

Notwithstanding the fact that in *Acampo* the Tax Court thus *allowed* carrybacks of *net operating losses* from years in which the corporate taxpayer had become moribund, in the subsequent case of *Wier Long Leaf Lumber Company* v. *Commissioner*, 9 T.C. 990, affirmed in part and reversed in part, 173 Fed. (2d) 549(1949), it was held that where, pursuant to resolutions of the stockholders and board of directors consenting to liquidation and dissolution, a corporation had in 1942 ceased productive activity and sold the bulk of its operating properties, including land, a sawmill and other improvements, tractors, and automobiles, it was *not* entitled to carry back its *unused excess profits tax credits* for 1944 and 1945 to a prior year.

In affirming in part and reversing in part, the United States Court of Appeals for the Fifth Circuit stated:

> We agree with * * * [the Commissioner] * * * that if it appears that the corporation is a corporation in name and semblance only, without corporate substance and serving no real corporate purpose, it must, though not formally dissolved, be treated as dissolved de facto.

Thereupon, on the facts present in *Wier*, the Court of Appeals concluded that in *1943* the taxpayer was still in fact as well as in form a

corporation and was, therefore, entitled to carry back its unused excess profits credit for that year. However, the Court of Appeals also found from the facts that by the *end* of 1943, liquidation of the corporation had progressed to a point at which there was no longer any valid reason for delaying complete dissolution and that, though not dissolved de jure, the corporation must be regarded as dissolved de facto and a carryback of the unused excess profits credit from *1944* denied.

Following the decision of the Court of Appeals for the Fifth Circuit in *Wier*, in *Winter & Company, Inc.* (*Indiana*) v. *Commissioner*, 13 T.C. 108 (1949), appeal dismissed by the United States Court of Appeals for the Seventh Circuit on April 16, 1951, the Tax Court itself denied carrybacks of *both* unused excess profits credits *and* net operating losses where the corporation involved had ceased all operations, had no earnings and no business expense and had shipped its plant equipment, inventories, and all other tangible assets to its parent, retaining only intangible assets consisting of credits on the parent's books in respect of such assets and of accounts receivable. As authority for its denial of the unused excess profits credit carryback in *Winter*, the Tax Court quoted the statement of the Court of Appeals in *Wier* as to de facto dissolution, and, in denying the *net operating loss carryback*, the court held also that since, after the date by which the corporation had disposed of its assets and ceased its activities, it was not engaged in a business or other operation, it could not have had an operating loss for a tax year subsequent to that date.

Other cases subsequent to the decision of the Court of Appeals in *Wier* and the Tax Court decision in *Winter*, in which a carryback of a net operating loss, an unused excess profits credit, or both, was denied in circumstances indicating a de facto corporate dissolution, include *ABC Brewing Corporation* v. *Commissioner*, 20 T.C. 515 (1953), acquiescence, C.B. 1954–1, 3, affirmed, 224 Fed. (2d) 483 (1955); *Diamond A. Cattle Company* v. *Commissioner*, 21 T.C. 1 (1953), affirmed in part and vacated and remanded in part, 233 Fed. (2d) 739 (1956); *Wheeler Insulated Wire Company Incorporated* v. *Commissioner*, 22 T.C. 380 (1954); and *American Well and Prospecting Company* v. *Commissioner*, 23 T.C. 503 (1954), affirmed, 232 Fed. (2d) 934 (1956), certiorari denied, 352 U.S. 840 (1956).

The principle of de facto dissolution is well established in the law and has been followed in determining corporate existence in connection with numerous questions other than carrybacks of net operating losses and unused excess profits tax credits. See *Kamin Chevrolet Company* v. *Commissioner*, 3 T.C. 1076 (1944), acquiescence, C.B. 1944, 15; *Eastern Grain Elevator Corp.* v. *McGowan*, 95 Fed. Supp. 40 (1950); I.T. 3871, C.B. 1947–2, 62; Rev. Rul. 215, C.B. 1953–2, 149; Rev. Rul. 54–518, C.B. 1954–2, 142; and Rev. Rul. 55–94, C.B. 1955–1, 419. Compare *James P. Neill, et al.* v. *Phinney*, 245 Fed. (2d) 645 (1957).

In the light of the foregoing, it is held that net operating losses sustained or excess profits tax credits remaining unused by a corporation subsequent to the date that it is de facto dissolved may not be carried back to prior taxable years. For the purpose of such carrybacks, a de facto dissolution occurs when a corporation has disposed

of all or most of its operating assets, terminated its business activities, and become a mere shell, a corporation in name and semblance only, without real corporate substance, serving no real corporate purpose, and having no valid or compelling reason for continuing its existence, even though not formally dissolved.

In the *Acampo Winery & Distilleries, Inc.*, case, in reaching the conclusion that the net operating loss carrybacks there in issue were allowable, the court appears not to have given consideration to the question whether or not the corporation involved was de facto dissolved prior to the years in which the net operating losses were sustained. Accordingly, insofar as it relates to the net operating loss carryback issue, the decision in *Acampo* will not be followed and the prior acquiescence, C.B. 1949–1, 1, is withdrawn and non-acquiescence substituted therefor. See page 6, this Bulletin. As to the remaining issues in *Acampo*, the prior acquiescence remains unchanged.

SUPPLEMENT D.—RETURNS AND PAYMENT OF TAX

SECTION 145.—PENALTIES

REGULATIONS 118, SECTION 39.145–1: Penalties.

Exclusion of embezzled funds from gross income. See Ct. D. 1863, page 9.

SUBCHAPTER D.—EXCESS PROFITS TAX

PART I.—RATE AND COMPUTATION OF TAX

SECTION 456.—ABNORMALITIES IN INCOME IN TAXABLE PERIOD

REGULATIONS 130, SECTION 40.456–2: Classification of income. Ct. D. 1866

1. EXCESS PROFITS TAXES—ABNORMAL INCOME RECEIVED IN EXCESS PROFITS TAX YEAR—NEW DRUGS AND PATENTED PRODUCTS AS "DISCOVERIES."

The relief afforded by section 456(a)(2)(B) of the Excess Profits Tax Act of 1950 for abnormal income resulting from "discovery" does not extend to income from sales of newly patented drugs and photographic equipment made under new patents. The word "discovery," as read in context with "exploration, discovery, or prospecting," means only the discovery of mineral resources and does not include the development of patentable products or processes. Taxpayer's contention that even if the income here was not specifically provided for in any of the subparagraphs of paragraph (2) it would come under the final sentence of that paragraph as "income of any class not described in subparagraphs (A) to (D)" is without merit. Even if the statute gave the Secretary of the Treasury power to expand the classes of abnormal income beyond those enumerated he has not done so. His regulations specifically exclude "research and development" income from classification of abnormal income.

2. JUDGMENT REVERSED AND JUDGMENT AFFIRMED.

Judgment of the United States Court of Appeals for the Seventh Circuit, 274 Fed. (2d) 129, reversed, and judgment of the United States Court of Appeals for the First Circuit, 278 Fed. (2d) 148, affirmed.

SUPREME COURT OF THE UNITED STATES

Nos. 151 and 169. October Term, 1960

John T. Jarecki, former Collector of Internal Revenue, et al., petitioners, v. *G. D. Searle & Co.*, No. 151

On writ of certiorari to the United States Court of Appeals for the Seventh Circuit

Polaroid Corporation, petitioner, v. *Commissioner of Internal Revenue,* No. 169

On writ of certiorari to the United States Court of Appeals for the First Circuit

[June 12, 1961]

MR. CHIEF JUSTICE WARREN delivered the opinion of the court.

These cases present problems in the interpretation of section 456(a) of the Internal Revenue Code of 1939, a section of the Excess Profits Tax Act of 1950, 64 Stat. 1137. The Act, which is intended to tax at high rates unusually high profits earned during the Korean War, imposes a tax on profits in excess of an amount deemed to represent the taxpayer's normal profits.[1] Recognizing, however, that some profits otherwise subject to tax under this scheme might stem from causes other than the inflated wartime economy, Congress enacted § 456. This section grants relief in certain cases of "abnormal income" as defined in section 456(a)[2] by allocating some of this income to years other than those in which it was received for purposes of computing the tax.

The dispute in these cases is whether income from the sales of certain new products falls within the statutory definition of "abnormal income." Taxpayers claim that the income from the sales of their products is income resulting from "discovery." They claim it is therefore "abnormal income" within the class defined by section 456(a)(2)(B) as

> "Income resulting from exploration, discovery, or prospecting, or any combination of the foregoing, extending over a period of more than 12 months."

Taxpayer in No. 151 is a corporation engaged in the manufacture and marketing of drugs. As a result of research extending for more than 12 months, it produced two new drugs, "Banthine," used in the treatment of peptic ulcers, and "Dramamine," for relief from motion sickness. Taxpayer received patents on both drugs, and it asserts that both were new products and not merely improve-

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[1] See H.R. Rep. No. 3142, 81st Cong., 2d Sess. 2 [C.B. 1951–1, 187], S. Rep. No. 2679, 81st Cong., 2d Sess. 2 [C.B. 1951–1, 240].

[2] Section 456(a) provides in part:

"(a) DEFINITIONS.—For the purpose of this section—

"(1) ABNORMAL INCOME.—The term "abnormal income" means income of any class described in paragraph (2) includible in the gross income of the taxpayer for any taxable year under this subchapter if it is abnormal for the taxpayer to derive income of such class, or, if the taxpayer normally derives income of such class but the amount of such income of such class includible in the gross income of the taxable year is in excess of 115 per centum of the average amount of the gross income of the same class for the four previous taxable years, or, if the taxpayer was not in existence for four previous taxable years, the taxable years during which the taxpayer was in existence.

"(2) SEPARATE CLASSES OF INCOME.—Each of the following subparagraphs shall be held to describe a separate class of income:

"(A) Income arising out of a claim, award, judgment, or decree, or interest on any of the foregoing; or

"(B) Income resulting from exploration, discovery, or prospecting, or any combination of the foregoing, extending over a period of more than 12 months; or

"(C) Income from the sale of patents, formulae, or processes, or any combination of the foregoing, developed over a period of more than 12 months; or

"(D) Income includible in gross income for the taxable year rather than for a different taxable year by reason of a change in the taxpayer's method of accounting.

"All the income which is classifiable in more than one of such subparagraphs shall be classified under the one which the taxpayer irrevocably elects. The classification of income of any class not described in subparagraphs (A) to (D), inclusive, shall be subject to regulations prescribed by the Secretary."

ments on pre-existing compounds. Taxpayer received income from the sale of "Banthine" and "Dramamine" in the years 1950 through 1952. It paid its tax without claiming relief under § 456, and then claimed a refund. On denial of its claim, taxpayer filed a complaint in the District Court for the Northern District of Illinois. The District Court dismissed the complaint, but the Court of Appeals for the Seventh Circuit reversed. It held that "discovery" might include the preparation of new products and that the case must be remanded for a trial on the issue of whether taxpayer's drugs "were actually discoveries." 274 F. 2d 129, 131.

Taxpayer in No. 169 is the inventor and producer of the "Polaroid Land Process," a camera and film which produce a photograph in 60 seconds, and the "Polaroid 3-D Synthetic Polarizer," a device incorporated in the "viewers" through which audiences watched the three dimensional motion pictures in vogue some years ago. These inventions, each the product of more than 12 months research, are novel, according to taxpayer, and each has been patented. The Polaroid Land equipment was the subject of 238 patents by the end of 1958, and taxpayer characterizes this invention as "revolutionary." Its production was a new departure in the business of taxpayer, which had hitherto been engaged primarily in manufacturing and selling such optical products as polarizing sunglasses, visors and camera filters. In its returns for 1951 through 1953 taxpayer utilized the provisions of section 456 in computing its tax on income from the sales of its photographic equipment and 3-D polarizers. The Commissioner determined that § 456 was not applicable, and the Tax Court upheld his determination of a deficiency. The Court of Appeals for the First Circuit affirmed, holding that taxpayer's inventions were not "discoveries" and its income from their sale not "abnormal income." 278 F. 2d 148.

We granted certiorari in each case to resolve the conflict between the decisions of the First and Seventh Circuits. 364 U.S. 812, 813.

I.

For present purposes we accept, as did the First Circuit, taxpayers' assertions of the novelty of their products. But we also agree with that court that taxpayers' inventions are not "discoveries" as that word is used in section 456(a)(2)(B) and that income from sales of the new products may not receive the special treatment provided by section 456.

We look first to the face of the statute. "Discovery" is a word usable in many contexts and with various shades of meaning. Here, however, it does not stand alone, but gathers meaning from the words around it. These words strongly suggest that a precise and narrow application was intended in section 456. The three words in conjunction, "exploration," "discovery" and "prospecting," all describe income-producing activity in the oil and gas and mining industries, but it is difficult to conceive of any other industry to which they all apply. Certainly the development and manufacture of drugs and cameras are not such industries. The maxim *noscitur a sociis*, that a word is known by the company it keeps, while not an inescapable rule, is often wisely applied where a word is capable of many meanings in order to avoid the giving of unintended breadth to the Acts of Congress. See, *e.g.*, *Neal* v. *Clark*, 95 U.S. 704, 708-709. The application of the maxim here leads to the conclusion that "discovery" in section 456 means only the discovery of mineral resources.

When we examine further the construction of section 456(a)(2) and compare subparagraphs (B) and (C), it becomes unmistakably clear that "discovery" was not meant to include the development of patentable products. If "discovery" were so wide in scope, there would be no need for the provision in subparagraph (C) for "income from the sale of patents, formulae, or processes." All of this income, under taxpayers' reading of "discovery," would also be income "resulting from * * * discovery" within subparagraph (B). To borrow the homely metaphor of Judge Aldrich in the First Circuit, "if there is a big hole in the fence for the big cat, need there be a small hole for the small one?" The statute admits a reasonable construction which gives effect to all of its provisions. In these circumstances we will not adopt a strained reading which renders one part a mere redundancy. See, *e.g.*, *United States* v. *Menasche*, 348 U.S. 528, 538-539.

Taxpayers assert that it is the "ordinary meaning" of "discovery" which must govern. We find ample evidence both on the face of the statute and, as we shall show, in its legislative history that a technical usage was intended. But even if we were without such evidence we should find it difficult to believe that Con-

gress intended to apply the layman's meaning of "discovery" to describe the products of research. To do so would lead to the necessity of drawing a line between things found and things made, for in ordinary present-day usage things revealed are discoveries, but new fabrications are inventions.[3] It would appear senseless for Congress to adopt this usage, to provide relief for income from discoveries and yet make no provision for income from inventions. Perhaps in the patent law "discovery" has the uncommonly wide meaning taxpayers suggest, but the fields of patents and taxation are each lores unto themselves, and the usage in the patent law (which is by no means entirely in taxpayers' favor)[4] is unpersuasive here. All the evidence is to the effect that Congress did not intend to introduce the difficult distinction between inventions and discoveries into the excess profits tax law.

The relevant legislative history fortifies the conclusions to which the words of the statute lead us. The word "discovery" has been used for many years in the tax laws, and has always been used with the limited meaning of the finding of mineral deposits. In the Revenue Act of 1918, enacting one of the earliest excess profits tax laws, a limit was placed on the excess profits tax on income from a "bona fide sale of mines, oil or gas wells, or any interest therein, where the principal value of the property has been demonstrated by prospecting or exploration and discovery work done by the taxpayer." Revenue Act of 1918, section 337, 40 Stat. 1096.[5] An identical limitation was imposed on the income tax levied under that Act,[6] and the same usage of "discovery" obtained in the allowance of depletion deductions.[7] The limitation on the income tax on the proceeds of the sale of mineral deposits was re-enacted without significant change in the Revenue Acts of 1921, 1924, 1926, 1928, 1932, 1936 and 1938.[8] It remains in the income tax provisions of the Internal Revenue Code of 1939 as section 105 and has been carried forward as section 632 of the 1954 Code. In each re-enactment "discovery" is linked with "exploration" and "prospecting," and in each the word is restrictively applied to extractive industries. A correspondingly narrow use of "discovery" has continued since 1918 in the depletion allowance sections[9] and appears in section 114(b)(2) of the 1939 Code. In the more than 30 years preceding the enactment of the section here at issue, during which time "discovery" was used and re-used in successive taxing statutes, the word developed into a term of art of precise and limited meaning.

The Excess Profits Tax Act of 1940, 54 Stat. 975, made specific mention of more types of "abnormal income" qualifying for relief than did the earlier excess profits tax statutes, but there is no indication that it worked any transformation in the meaning of "discovery." Section 721, 54 Stat. 986, as amended, 55 Stat. 21, classified six types of "abnormal income." Among them was the following, at section 721(a)(2)(C):

> "Income resulting from exploration, discovery, prospecting, research, or development of tangible property, patents, formulae, or processes, or any combination of the foregoing, extending over a period of more than 12 months."

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[3] In lay terms, Polaroid's photographic equipment and Searle's drugs are probably better called inventions than discoveries. Webster's New International Dictionary, Unabridged (2d ed.) p. 745, makes this distinction: "One discovers what existed before, but had remained unknown; one invents by forming combinations which are either entirely new, or which attain their end by means unknown before; as, Columbus *discovered* America; Newton *discovered* the law of gravitation; *Edison* invented the phonograph. * * *"

[4] The United States Constitution, Art. I, sec. 8, cl. 8 gives Congress the power to secure to "Inventors the exclusive Right to their * * * Discoveries." While the terms "discover" and "discovery" are used throughout the patent statutes, they seem generally to appear with "invent" and "invention" as if the terms have separate meanings. See, *e.g.*, 35 U.S.C. § 101: "Whoever invents or discovers any new and useful process, machine, manufacture, or composition of matter * * * may obtain a patent therefore. * * *" And see *Dolbear* v. *American Bell Telephone Co.* (*Telephone Cases*), 126 .US. 1, 532–533.

[5] This section was re-enacted by the Revenue Act of 1921, sec. 337, 42 Stat. 277.

[6] Revenue Act of 1918, sec. 211(b), 40 Stat. 1064.

[7] Revenue Act of 1918, secs. 214(a)(10), 234(a)(9), 40 Stat. 1067, 1078, providing "That in the case of mines, oil and gas wells, discovered by the taxpayer * * * where the fair market value of the property is materially disproportionate to the cost, the depletion allowance shall be based upon the fair market value of the property at the date of discovery. * * *"

[8] Revenue Act of 1921, sec. 211(b), 42 Stat. 237; Revenue Act of 1924, sec. 211(b), 43 Stat. 267; Revenue Act of 1926, sec. 211(b), 44 Stat. 23; Revenue Act of 1928, sec. 102(a), 45 Stat. 812; Revenue Act of 1932, sec. 102(a), 47 Stat. 192; Revenue Act of 1936, sec. 105, 49 Stat. 1678; Revenue Act of 1938, sec. 105, 52 Stat. 484.

[9] Revenue Act of 1921, secs. 214(a)(10), 234(a)(9), 42 Stat. 241, 256; Revenue Act of 1924, sec. 204(c), 43 Stat. 260; Revenue Act of 1926, sec. 204(c)(1), 44 Stat. 16; Revenue Act of 1928, sec. 114(b)(2), 45 Stat. 821; Revenue Act of 1932, sec. 114(b)(2), 47 Stat. 202; Revenue Act of 1934, sec. 114(b)(2), 48 Stat. 710; Revenue Act of 1936, sec. 114(b)(2), 49 Stat. 1686; Revenue Act of 1938, sec. 114(b)(2), 52 Stat. 495.

This was the first time specific provision was made for income from invention, relief in cases of such income having previously been obtainable, if at all, only under the "general relief" provisions of the earlier Acts.[10] It is instructive that the formula "exploration, discovery, or prospecting" was not considered broad enough to cover invention and that the words "research" and "development" were added to cover that source of income. Plainly, "discovery" retained in the World War II excess profits Act the limited meaning which it had had in the previous Acts and which it continued to have in the income tax provisions of the then-current code.[11]

The relief provisions of the Excess Profits Tax Act of 1950, which we here construe, were modeled in part on section 721 of the World War II Act, but were different in significant respects. In the classifications of income in the new section 456, Congress gave separate treatment to income from discovery of minerals and income from invention. It provided relief in subparagraph (B) for "income *resulting from* exploration, discovery, or prospecting," but provided in subparagraph (C) only for "income *from the sale of* patents, formulae, or processes." (Emphasis added.) Subparagraph (C) does not encompass all income from inventions. It does not cover income from the sale of products made under a new patent, the sort of income at issue here. Taxpayers assert that the income from their inventions is, realistically speaking, as "abnormal" in their businesses as the discovery of a new mine would be in the business of a prospector. Their income is within the spirit of section 456, they say, and should be held to be within the letter of subparagraph (B). It is clear, however, that Congress, while it may have recognized the abnormal nature of this sort of income, chose deliberately to deny relief for it and to limit relief in cases of research and development to that provided in subparagraph (C).

The relief provisions of the World War II Act had been intended to provide "flexible rules," [12] and their application had often been an uncertain affair. In administering section 721 the Commissioner often faced the difficult task of separating income which was the product of "research, or development" from that resulting merely from improved management or sales efforts. The difficulty of distinction led the Tax Court to hold that the distinction must be made "by exercising common sense and judgment," and that "It is entirely possible that the allocation made by one person would never match that made by another." *Ramsey Accessories Mfg. Corp.* v. *Commissioner*, 10 T.C. 482, 489. Congress in 1950 recognized the delay and uncertainty caused by the element of administrative discretion in this and other [13] sections and set about drafting an excess profits tax law on the principle that "subjective judgments * * * should be avoided in the new law." H. R. Rep. No. 3142, 81st Cong., 2d Sess. 20 [C.B. 1951–1, 187]. This principle was expressly followed in the drafting of section 456. The Senate Committee reported on section 456 as follows:

> "The equivalent provision in the World War II law (sec. 721) also permitted adjustments with reference to certain other types of income, particularly that resulting from the sale of tangible property arising out of research and development which extended over a period of more than 12 months. This provision in the old law was a potential loophole of major dimensions. Because there appeared to be no means of restricting such an adjustment to truly meritorious cases other than by the introduction of a large degree of administrative discretion of the type required by the general relief clause of the World War II law (sec. 722), and because the need for a reallocation of such income seemed to be materially less than for the other classes of income described above, the bill omits this item from the list of

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[10] Section 327(d) of the Revenue Act of 1918, 40 Stat. 1093, gave the Commissioner power to grant relief in any case in which "the tax * * * would, owing to abnormal conditions affecting the capital or income of the corporation, work upon the corporation an exceptional hardship. * * *" Section 721 of the World War II law classified specific types of abnormal income for purposes of computing the tax, and, while it provided relief for all abnormal income of whatever class, was not considered a "general relief" section.

[11] I.R.C. of 1939, secs. 105, 114(b)(2). It was expressly provided by sec. 728 of the World War II excess profits tax statute, 54 Stat. 989, that the words used in that statute should have the same meaning as when used in the income tax chapter of the Code.

[12] H.R. Rep. No. 146, 77th Cong., 1st Sess. 2.

[13] The "general relief" section of the World War II Act, sec. 722, 54 Stat. 986, as amended, 55 Stat. 23, 701, 56 Stat. 914, 57 Stat. 56, 601, 58 Stat. 55, provided for adjustments in the computation of base period income if the taxpayer established, among other things, "what would be a fair and just amount representing normal earnings" during the base period.

abnormal types of income for which a reallocation can be made." S. Rep. No. 2679, 81st Cong., 2d Sess. 14 [C.B. 1951-1, 240].

The House Committee Report was virtually identical. H. R. Rep. No. 3142, 81st Cong., 2d Sess. 13 [C.B. 1951-1, 187].

Taxpayers recognize, as they must, that Congress intended its change in language to limit the kinds of income eligible for relief. They say, however, that not all income from research and development was excluded. That which comes from inventions not merely patentable but also sufficiently revolutionary to be called "genuine discoveries" is still within the protection of section 456. We find it impossible to believe that an amendment designed to eliminate uncertainty and administrative discretion would introduce into the law—without a congressional word of warning or explanation—a distinction as vague, as dependent upon nuances of scientific opinion, and as unprecedented as that urged by taxpayers.

II.

Taxpayers have another argument, which the First Circuit rejected and which the Seventh Circuit did not reach. Paragraph (1) of section 456(a) defines "abnormal income" as "income of any class described in paragraph (2)" which meets certain requirements. Paragraph (2) lists four classes of income and provides in its concluding sentence:

> "The classification of income of any class not described in subparagraphs (A) to (D), inclusive, shall be subject to regulations prescribed by the Secretary."

Taxpayers argue that even if the income here at issue was not provided for under any of the subparagraphs of paragraph (2), it is nevertheless included within this final sentence and is hence eligible for relief.

We need not decide the precise effect of the sentence relied on. In light of the clear purpose of Congress in enacting section 456 to cut down not only the amount of administrative discretion which had prevailed under the predecessor section but also the scope of available relief, the power of the Secretary to extend relief far beyond the four corners of the statute may be doubted.[14] It is sufficient to note that, unlike its predecessor (which made relief available for all "abnormal income," whether or not specified in a particular class),[15] section 456 applies only to those classes specified in section 456(a)(2). Section 456 does not apply in terms to all abnormal income and contains no indication that the Secretary should create administrative classifications embracing all such income. And even if the sentence relied on gives the Secretary power to expand the classes of abnormal income somewhat beyond the four enumerated in the statute, he has clearly not done so here. The regulations[16] specifically provide that "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." This specific exclusion is clearly in furtherance of the purpose of Congress in deleting "research" and "development" income from its classification of abnormal income. The Commissioner, effecting the will of Congress, has barred relief for the type of income here at issue.

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[14] In fact, the Committee reports state that "Adjustments * * * [under sec. 456] are limited to income arising out of" the four classes specified in subparagraphs (A) through (D). H.R. Rep. No. 3142, 81st Cong., 2d Sess. 13, S. Rep. No. 2679, 81st Cong., 2d Sess. 14.

[15] Excess Profits Tax Act of 1940, sec. 721, 54 Stat. 986, as amended, 55 Stat. 21. Section 721(a)(1) defines "abnormal income" as "income of any class includible in the gross income of the taxpayer. * * *"

[16] Treas. Regs. sec. 40.456-2(b) (1951), as amended, T.D. 6026, 1953-2 Cum. Bull. 235: "Other income, not within a class described in subparagraphs (A)-(D) of section 456(a)(2), to which section 456 is applicable may be grouped by the taxpayer, subject to approval by the Commissioner on the examination of the taxpayer's return, in such classes similar to those specified in subparagraphs (A)-(D) of section 456(a)(2) as are reasonable in a business of the type which the taxpayer conducts, and as are appropriate in the light of the taxpayer's business experience and accounting practice. 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)."

The last sentence of the regulation, on which taxpayers also rely, does not aid them. It provides merely that "research" and "development" income is eligible for relief if it is properly includible in a class of income to which section 456 otherwise applies. As we have held, however, taxpayers' income does not fall within any such class.

Therefore, the judgment of the Court of Appeals for the Seventh Circuit must be reversed and the judgment of the Court of Appeals for the First Circuit affirmed.

It is so ordered.

SUBPART B.—RULINGS AND DECISIONS UNDER OTHER PUBLIC LAWS

Rulings and decisions published in Part II, Subpart B, of the Internal Revenue Bulletin are based on the application of provisions of other public laws on internal revenue matters, except those relating to the various alcohol taxes, which appear in Part III.

PUBLIC LAW 87-312

26 CFR 1.9004: Statutory provisions; the Act of September 26, 1961 (Public Law 87-312, 75 Stat. 674). (Also Part I, Section 613; 1.613-3.) T. D. 6575 [1]

TITLE 26—INTERNAL REVENUE.—CHAPTER I, SUBCHAPTER A, PART 1.—INCOME TAX; TAXABLE YEARS BEGINNING AFTER DECEMBER 31, 1953

Regulations under the Act of September 26, 1961 (Public Law 87-312, 75 Stat. 674).

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

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

The regulations set forth below are hereby prescribed under the Act of September 26, 1961 (Public Law 87-312, 75 Stat. 674) [page 339, this Bulletin]:

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Section

1.9004 Statutory provisions; the Act of September 26, 1961 (Public Law 87-312, 75 Stat. 674).

1.9004-1 Election relating to the determination of gross income from the property for taxable years beginning prior to 1961 in the case of certain clays and shale.

1.9004-2 Effect of election.

1.9004-3 Statutes of limitation.

1.9004-4 Manner of exercising election.

1.9004-5 Terms; applicability of other laws.

§ 1.9004 STATUTORY PROVISIONS: THE ACT OF SEPTEMBER 26, 1961 (PUBLIC LAW 87-312, 75 STAT. 674).

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That

(a) ELECTION FOR PAST YEARS.—In the case of brick and tile clay, fire clay, or shale used by the mineowner or operator in the manufacture of building or paving brick, drainage and roofing tile, sewer pipe, flower pots, and kindred products (without regard to the applicable rate of percentage depletion), if an election is made under subsection (c), for the purpose of applying section 613(c) of the Internal Revenue Code of 1954 (and corresponding provision of the Internal Revenue Code of 1939) for each of the taxable years with respect to which the election is effective—

(1) Gross income from the property shall be 50 per centum of the amount for which the manufactured products are sold during

[1] 26 F.R. 9631.

the taxable year except that with respect to such manufactured products, gross income from the property shall not exceed an amount equal to $12.50 multiplied by the number of short tons used in the manufactured products sold during the taxable year, and

(2) For purposes of computing the 50 per centum limitation under section 613(a) of the Internal Revenue Code of 1954 (or the corresponding provision of the Internal Revenue Code of 1939), the taxable income from the property (computed without allowance for depletion) shall be 50 per centum of the taxable income from the manufactured products sold during the taxable year (computed without allowance for depletion).

(b) YEARS TO WHICH APPLICABLE.—An election made under subsection (c) to have the provisions of this section apply shall be effective for all taxable years beginning before January 1, 1961, in respect of which—

(1) The assessment of a deficiency,

(2) The refund or credit of an overpayment, or

(3) The commencement of a suit for recovery of a refund under section 7405 of the Internal Revenue Code of 1954,

is not prevented on the date of the enactment of this Act by the operation of any law or rule of law. Such election shall also be effective for any taxable year beginning before January 1, 1961, in respect of which an assessment of a deficiency has been made but not collected on or before the date of the enactment of this Act.

(c) TIME AND MANNER OF ELECTION.—An election to have the provisions of this section apply shall be made by the taxpayer on or before the sixtieth day after the date of publication in the Federal Register of final regulations issued under authority of subsection (f), and shall be made in such form and manner as the Secretary of the Treasury or his delegate shall prescribe by regulations. Such election, if made, may not be revoked.

(d) STATUTES OF LIMITATION.—Notwithstanding any other law, the the period within which an assessment of a deficiency attributable to the election under subsection (c) may be made with respect to any taxable year for which such election is effective, and the period within which a claim for refund or credit of an overpayment attributable to the election under such subsection may be made with respect to any such taxable year, shall not expire prior to one year after the last day for making an election under subsection (c). An election by a taxpayer under subsection (c) shall be considered as a consent to the application of the provisions of this subsection.

(e) TERMS; APPLICABILITY OF OTHER LAWS.—Except where otherwise distinctly expressed or manifestly intended, terms used in this section shall have the same meaning as when used in the Internal Revenue Code of 1954 (or corresponding provisions of the Internal Revenue Code of 1939) and all provisions of law shall apply with respect to this section as if this section were a part of such Code (or corresponding provisions of the Internal Revenue Code of 1939).

(f) REGULATIONS.—The Secretary of the Treasury or his delegate shall prescribe such regulations as may be necessary to carry out the provisions of this section.

§ 1.9004–1 ELECTION RELATING TO THE DETERMINATION OF GROSS INCOME FROM THE PROPERTY FOR TAXABLE YEARS BEGINNING PRIOR TO 1961 IN THE CASE OF CERTAIN CLAYS AND SHALE.—(a) *In general.*—The Act of September 26, 1961 (Public Law 87–312, 75 Stat. 674), provides that certain taxpayers may elect to apply the provisions thereof to all taxable years beginning before January 1, 1961, with respect to which the election is effective. The Act prescribes special rules for the application of section 613 (a) and (c) of the Internal Revenue Code of 1954 (and corresponding provisions of the Internal Revenue Code of 1939) in the case of shale and certain clays used by the mine owner or operator in the manufacture of certain clay and shale products.

(b) *Election.*—The election to apply the provisions of the Act may be made only by a mine owner or operator with respect to brick and tile clay, fire clay, or shale which he mined and used in the manufacture of building or paving brick, drainage and roofing tile, sewer pipe, flower pots, and kindred products. The election must be made in accordance with § 1.9004–4 on or before December 11, 1961, and the election shall become irrevocable on December 11, 1961.

(c) *Years to which the election is applicable.*—If the election described in paragraph (b) of this section is made by the taxpayer, the provisions of the Act shall be effective for all taxable years beginning before January 1, 1961, in respect of which the—

(1) Assessment of a deficiency,

(2) Refund or credit of an overpayment, or

(3) Commencement of a suit for recovery of a refund under section 7405 of the Internal Revenue Code of 1954,

is not prevented on September 26, 1961, by the operation of any law or rule of law. The election is also effective for any taxable year beginning before January 1, 1961, in respect of which an assessment of a deficiency has been made but not collected on or before September 26, 1961.

§ 1.9004–2 Effect of Election.—(a) *In general.*—If a taxpayer makes the election described in paragraph (b) of § 1.9004–1, he shall be deemed to have consented to the application of the Act with respect to all the clay and shale described in that paragraph for all taxable years for which the election is effective whether or not the taxpayer is litigating the issue for any of such years. Thus, in applying section 613 of the Internal Revenue Code of 1954 (and corresponding provisions of the Internal Revenue Code of 1939) to those years—

(1) The "gross income from the property" for purposes of section 613(c) of the Internal Revenue Code of 1954 (and corresponding provisions of the Internal Revenue Code of 1939) shall be 50 percent of the amount for which the mineowner or operator sold during the taxable year, the building or paving brick, drainage and roofing tile, sewer pipes, flower pots, and kindred products manufactured from the clay and shale described in paragraph (b) of § 1.9004–1, but shall not exceed an amount equal to $12.50 multiplied by the number of short tons of all such clay or shale mined and used by the mineowner or operator in the manufacture of the products sold during the taxable year; and

(2) The "taxable income from the property" (computed without allowance for depletion) for purposes of section 613(a) of the Internal Revenue Code of 1954 (and corresponding provisions of the Internal Revenue Code of 1939) shall be 50 percent of the taxable income from the manufactured products sold during the taxable year (computed without allowance for depletion).

(b) *Effect on depletion rates and other items.*—The election shall have no effect on the applicable rate of percentage depletion for the taxable years to which the election is effective. In applying the election to the years affected there shall be taken into account the effect that any adjustments resulting from the election shall have on

other items affected thereby, such as charitable contributions, foreign tax credit, net operating loss, and the effect that adjustments to any such items shall have on other taxable years. The provisions of the Act are applicable with respect to taxable years subject to the Internal Revenue Code of 1939 for purposes of applying section 450 and 453 of that Code.

§ 1.9004–3 STATUTES OF LIMITATION.—The period within which the assessment of any deficiency or the credit or refund of any overpayment attributable to the election may be made shall not expire sooner than one year after December 11, 1961. Thus, if assessment of a deficiency or credit or refund of an overpayment, whichever is applicable, is not prevented on September 26, 1961, the time for making assessment or credit or refund shall not expire for at least one year after December 11, 1961, notwithstanding any other provision of law to the contrary. Even though assessment of a deficiency is prevented on September 26, 1961, if commencement of a suit for recovery of a refund under section 7405 of the Internal Revenue Code of 1954 may be made on such date, then any deficiency resulting from the election may be assessed at any time within 1 year after December 11, 1961. If a taxpayer makes the election, he shall be deemed to have consented to the application of the provisions of the Act extending the time for assessing a deficiency attributable to the election. The Act does not shorten the periods of limitation otherwise applicable. An agreement may be entered into under section 6501 (c)(4) of the Internal Revenue Code of 1954 and corresponding provisions of prior law to extend the period for assessment.

§ 1.9004–4 MANNER OF EXERCISING ELECTION.—(a) *By whom election is to be made.*—Generally, the taxpayer whose tax liability is affected by the election shall make the election. In the case of a partnership, or a corporation electing under the provisions of subchapter S, chapter 1 of the Internal Revenue Code of 1954, the election shall be exercised by the partnership or such corporation, as the case may be.

(b) *Time and manner of making election.*—The election shall be made on or before December 11, 1961, by filing a statement with the district director with whom the taxpayer's income tax return for the taxable year in which the election is made is required to be filed. The statement shall include the following:

(1) A clear indication that an election is being made under the Act, and

(2) The taxable years to which the election applies.

Amended income tax returns reflecting any increase or decrease in tax attributable to the election shall be filed for the taxable years to which the election applies. In the case of partnerships and electing small business corporations under subchapter S, chapter 1 of the Internal Revenue Code of 1954, amended returns shall be filed by the partnership or electing small business corporation, as well as by the partners or shareholders, as the case may be. Any amended return shall be filed with the office of the district director with whom the taxpayer files his income tax return for the taxable year in which the election is made and, if practicable, on the same date the statement of election is filed, but amended returns shall be filed in no event later

than March 31, 1962, unless an extension of time is granted under section 6081 of the Internal Revenue Code of 1954. Whenever the amended returns do not accompany the statement of election, a copy of the statement shall be submitted with the amended returns. The amended returns shall be accompanied by payment of the additional tax (together with interest thereon) resulting from the election.

§ 1.9004–5 TERMS; APPLICABILITY OF OTHER LAWS.—All other terms which are not otherwise specifically defined shall have the same meaning as when used in the Internal Revenue Code of 1954 (or the corresponding provisions of prior law) except where otherwise distinctly expressed or manifestly intended to the contrary. Further, all provisions of law contained in the Code (or the corresponding provisions of prior law) shall apply to the extent that they can apply. Thus, all the provisions of subtitle F of the Code (and the corresponding provisions of prior law) shall apply to the extent they can apply, including the provisions of law relating to assessment, collection, credit or refund, and limitations. For purposes of this section and §§ 1.9004–1 to 1.9004–4, inclusive, the term "Act" means the Act of September 26, 1961 (Public Law 87–312, 75 Stat. 674).

Because this Treasury Decision is designed to inform taxpayers as to how, when, and where to perform certain acts required or permitted under the Act of September 26, 1961 (Public Law 87–312, 75 Stat. 674), it is found 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 subsection (f) of the Act of September 26, 1961 (Public Law 87–312, 75 Stat. 674).)

MORTIMER M. CAPLIN,
Commissioner of Internal Revenue.

Approved October 9, 1961.

STANLEY S. SURREY,
Assistant Secretary of the Treasury.

(Filed by the Division of the Federal Register on October 11, 1961, 8:49 a.m., and published in the issue of the Federal Register for October 12, 1961. 26 F.R. 9631)

PART III

ALCOHOL TAX RULINGS AND DECISIONS

SUBPART A.—RULINGS AND DECISIONS UNDER THE INTERNAL REVENUE CODE OF 1954

Rulings and decision published in Part III, Subpart A, of the Internal Revenue Bulletin are based on the application of provisions of the Internal Revenue Code of 1954 and, unless otherwise noted therein, are published without consideration as to any application of the provisions of the Internal Revenue Code of 1939, the Federal Alcohol Administration Act, or other public laws.

SUBTITLE E.—ALCOHOL, TOBACCO, AND CERTAIN OTHER EXCISE TAXES

CHAPTER 51.—DISTILLED SPIRITS, WINES AND BEER

SUBCHAPTER A.—GALLONAGE AND OCCUPATIONAL TAXES

PART I.—GALLONAGE TAXES

Subpart A.—Distilled Spirits

SECTION 5006.—DETERMINATION OF TAX

26 CFR 201.26: Time for tax determination. Rev. Rul. 61–166

Spirits of 190 degrees or more of proof which are reduced to a proof below 190 degrees (either by reduction with water or by mingling with other spirits of less than 190 degrees of proof) any time after entry for deposit into bonded storage become subject to the 20-year bonding period limitations at the time they are so reduced.

Revenue Ruling 60–381, C.B. 1960–2, 509, revoked.

The Internal Revenue Service has reconsidered Revenue Ruling 60–381, C.B. 1960–2, 509. That Revenue Ruling holds that the 20-year bonding period limitation applicable to distilled spirits under section 5006(a)(2) of the Internal Revenue Code of 1954 is not applicable to distilled spirits which were distilled at and entered for deposit into bonded storage at 190 degrees or more of proof but subsequently reduced in proof below 190 degrees.

The reconsideration has been made in the light of the specific language of section 5006(a)(2) of the Code on which the ruling was based and in the light of the administrative problems involved in applying the concepts of the ruling to the various sections of the Distilled Spirits Plants Regulations and the various Treasury Department forms where language similar to that in the statute appears and where the applicability of the various sections and forms to specified spirits depends on the meaning of such language as it relates to the proof of the spirits.

The Internal Revenue Service has concluded that section 5006(a)(2)(B) (i) and (ii) of the Code provides exemption from the bonding period limitation only for spirits which are, in fact, "of 190 degrees or more of proof" or are denatured. This position is consistent with the use of the statutory language in the applicable sections of the regulations and in the various forms.

Accordingly, it is held that section 5006(a)(2)(B) (i) and (ii) of the Code provides an exception to the bonding period limitation only when spirits are 190 degrees or more of proof or are denatured. Therefore, spirits of 190 degrees or more of proof, which are reduced to a proof below 190 degrees (either by reduction with water or by mingling with other spirits of less than 190 degrees of proof) any time after entry for deposit into bonded storage, become subject to the bonding period limitation at the time they are so reduced and must, thereafter, be accounted for in the same manner as other spirits subject to the bonding period limitation.

The date of the reduction in proof shall be considered the date of original entry applicable to such spirits for purposes of determining the bonding period.

Conversely, spirits of less than 190 degrees of proof which (while in bonded storage) are increased to 190 degrees or more of proof by mingling with spirits of a higher proof, or which are denatured, become exempt from the bonding period limitation (and the attendant record-keeping requirements) at the time their proof is so increased or at the time they are so denatured.

It is further held that for imported spirits of less than 190 degrees of proof, the date of the Form 236, Transfer of Spirits or Denatured Spirits in Bond, pursuant to which such spirits are transferred from Customs custody for deposit into internal revenue bonded storage facilities shall be considered the date of original entry for the purpose of applying the provisions of section 5006(a)(2) of the Code.

Revenue Ruling 60–381, is hereby revoked.

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26 CFR 201.303: Determining date of original entry.

Reporting of the date of original entry of spirits on deposit and withdrawal forms covering mingled and blended spirits. See Rev. Proc. 61–17, page 549.

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26 CFR 201.634: Semiannual report of spirits in warehouse, Form 332.

Reporting gin of 190 degrees or more of proof. See Rev. Proc. 61–25, page 561.

SECTION 5008.—ABATEMENT, REMISSION, REFUND, AND ALLOWANCE FOR LOSS OR DESTRUCTION OF DISTILLED SPIRITS

26 CFR 201.45: Claims relating to spirits lost or destroyed after tax determination.

Claims for refund on distilled spirits lost by reason of leakage and spillage. See Rev. Rul. 61–131, below.

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26 CFR 201.482: Allowable losses. (Also 201.45.) Rev. Rul. 61–131

Claims for refund of the tax paid on distilled spirits lost by reason of leakage and spillage from the failure of a temporary hose connection from a bottling tank on bottling premises are allowable under section 5008(c)(1)(B) of the Internal Revenue Code of 1954 and section 201.482(b) of the Distilled Spirits Plants Regulations.

Advice has been requested whether a claim for refund of the tax paid on distilled spirits lost by reason of leakage and spillage from a temporary hose connection from a bottling tank on bottling premises is allowable as a loss by accident or disaster, or allowable as a part of the monthly operating losses of the distilled spirits plant.

Distilled spirits were lost on the bottling premises of the permittee when a temporary hose connection was blown off from the outlet line of a bottling tank. A portion of the permanent outlet pipeline from the bottling tank had previously been disconnected and a part of the pipeline removed. The removed pipeline section was replaced with a rubber hose section. At the time the outlet line of the bottling tank was opened to transfer the distilled spirits by gravity, the temporary hose connection blew off from the pipeline causing distilled spirits to pour from the bottling tank onto the floor. None of the distilled spirits lost was recoverable.

Section 5008(c)(1) of the Internal Revenue Code of 1954 provides as follows:

> (1) GENERAL.—Whenever any distilled spirits withdrawn from bond on payment or determination of tax for rectification or bottling are lost before the completion of the bottling and casing or other packaging of such spirits for removal from the bottling premises of the distilled spirits plant to which removed from bond, the Secretary or his delegate shall, under such regulations as he may prescribe, abate, remit, or, without interest, credit or refund the tax imposed on such spirits under section 5001(a)(1) to the proprietor of the distilled spirits plant who withdrew the distilled spirits on payment or determination of tax for removal to the bottling premises, if it is established to the satisfaction of the Secretary or his delegate that—
>
> (A) such loss occurred (i) by reason of accident while being removed from bond to bottling premises, or (ii) by reason of flood, fire, or other disaster; or
>
> (B) such loss occurred by reason of, and was incident to, authorized rectifying, packaging, bottling, or casing operations (including losses by leakage or evaporation occurring during removal from bond to the bottling premises and during storage on bottling premises pending rectification or bottling).

Section 201.482(a)(2) of the Distilled Spirits Plants Regulations provides in part that where spirits withdrawn from internal revenue bond on payment or determination of tax, or from customs bond on

payment of tax, for rectification or bottling are lost before the com pletion of such bottling and casing or other packaging of such spiri for removal from the bottling premises of the plant to which remove from bond, the tax imposed on such spirits under section 5001(a)(1 of the Code, may be abated, remitted, or, without interest, refunde or credited to the proprietor who so withdrew the spirits for remov to his bottling premises, if it is established to the satisfaction of th Assistant Regional Commissioner, Alcohol and Tobacco Tax, tha such loss occurred by reason of flood, fire, or other disaster.

Section 201.482(b) of the regulations similarly provides for abat ment, remission, credit, or refund of tax where the loss of such spirit occurred by reason of, and was incident to, authorized rectifying packaging, bottling, or casing operations (including losses by leakag or evaporation occurring during storage on bottling premises pend ing rectification or bottling).

A claim for refund of tax for distilled spirits lost by reason o leakage and spillage from a temporary hose connection to a bottlin tank on bottling premises is not allowable under section 5008(c)(1 (A)(ii) of the Code and section 201.482(a)(2) of the regulations a a loss by reason of fire, flood, or other disaster.

However, where such a loss is incident to authorized rectifying packaging, bottling or casing operations on bottling premises, an did not involve theft or unauthorized voluntary destruction, it i allowable under section 5008(c)(1)(B) of the Code and sectio 201.482(b) of the regulations.

Claims for losses incurred in rectifying, packaging, bottling, an casing operations must be filed under the provisions of sectio 201.45(d) of the regulations.

Rev. Rul. 61-14

Section 5008(c)(1)(A)(i) of the Internal Revenue Code of 195 provides, in part, for the allowance of losses of distilled spirits with drawn from bond for rectification or bottling where such losses oc curred by reason of accident while being removed from bond t bottling premises.

Held, spirits which have been lost by reason of accident whil being removed from bond to bottling premises and prior to comin to rest on the bottling premises should be considered as in-transi losses coming within the provisions of section 5008(c)(1)(A)(i) o the Code and section 201.482(a)(1) of the Distilled Spirits Plant Regulations. Therefore, the accidental loss of the whole, or of a part of the contents of a package, when dropped from a vehicle or ski during unloading at a point on the distilled spirits plant premises im mediately adjacent to, but not on the bottling premises, as well a spirits so lost from a package while unloading on the bottling premise would be eligible for allowance under section 201.482(a)(1) of th regulations.

Held further, distilled spirits which have been lost after they hav come to rest on the bottling premises and are susceptible of bein gauged thereon (whether or not actually gauged) are no longer i an in-transit status. Losses in respect of such spirits occurring afte they have come to rest, and losses due to leakage or evaporation oc curring during removal from bond to the bottling premises, shoul

be considered as bottling losses allowable under the provisions of section 5008(c)(1)(B) of the Code and section 201.482(b) of the regulations. This is true in respect of spirits removed from bond to a tank on bottling premises by pipeline or from a tank truck, as well as to spirits in packages. See Rev. Rul. 61–131, page 269, this Bulletin.

Subpart B.—Rectification

SECTION 5025.—EXEMPTION FROM RECTIFICATION TAX

26 CFR 201.297: Mingling of homogeneous spirits.

Reporting of the date of original entry of spirits on deposit and withdrawal forms covering mingled and blended spirits. See Rev. Proc. 61–17, page 549.

Subpart C.—Wines

SECTION 5041.—IMPOSITION AND RATE OF TAX

26 CFR 240.531: General.

The use of vitagen gas to remove air and reduce oxidation in the production of wine. See Rev. Rul. 61–200, page 283.

Subpart D.—Beer

SECTION 5053.—EXEMPTIONS

26 CFR 245.170: General.

Listing of foreign countries for which beer may be withdrawn free of tax or with benefit of drawback for use as supplies on aircraft. See Rev. Proc. 61–24, page 560.

Listing of foreign countries for which beer may be withdrawn free of tax or with benefit of drawback for use as supplies on aircraft. See Rev. Proc. 61–34, page 573.

Subpart E.—General Provisions

SECTION 5062.—REFUND AND DRAWBACK IN CASE OF EXPORTATION

26 CFR 252.23: Reciprocating foreign countries.

Listing of foreign countries for which liquors may be withdrawn free of tax or with benefit of drawback for use as supplies on aircraft. See Rev. Proc. 61–24, page 560.

Listing of foreign countries for which liquors may be withdrawn free of tax or with benefit of drawback for use as supplies on aircraft. See Rev. Proc. 61–34, page 573.

SUBCHAPTER C.—OPERATION OF DISTILLED SPIRITS PLANTS

PART I.—GENERAL PROVISIONS

SECTION 5201.—REGULATION OF OPERATIONS

26 CFR 201.270: Identification of spirits.

Reporting of the date of original entry of spirits on deposit and withdrawal forms covering mingled and blended spirits. See Rev. Proc. 61–17, page 549.

SECTION 5202.—SUPERVISION OF OPERATIONS

26 CFR 201.275: Distillates containing extraneous substances. Rev. Rul. 61–205

Section 201.275 of the Distilled Spirits Plants Regulations requires, in part, that prior to the removal of distillates containing aldehydes from the distilling system for addition to fermenting or distilling material, the distillates must be tested to determine the aldehyde content. This section further provides that where the test discloses an aldehyde content of less than one-tenth of one percent (.001) of aldehydes, the removal and use of the distillates shall be made pursuant to a written application filed with, and approved by, the Assistant Regional Commissioner, Alcohol and Tobacco Tax.

In order to assist proprietors, the National Office laboratory has devised the following simplified test for determining the aldehyde content of distillates containing one-tenth of one percent or more of aldehydes:

Reagent—0.02 grams potassium permanganate per liter of distilled water (freshly prepared solution).

To 1 ml of distillate add 10 ml of USP grade 190 proof ethyl alcohol.

Add 5 ml of reagent to the diluted sample.

0.1 percent (.001) or more aldehyde—color fades in one minute or less.

This test is authorized at any distilled spirits plant where distillates containing aldehydes are returned to fermenters under the provisions of section 201.275 of the regulations.

SECTION 5204.—GAUGING

26 CFR 201.269: Production gauge.

Recording losses of spirits from packages in bonded storage. See Rev. Proc. 61–16, page 548.

SECTION 5206.—CONTAINERS

26 CFR 175.11: Container. Rev. Rul. 61–180
(Also 175.17, 175.30, 175.34.)

Sections 175.11 and 175.17 of the Container Regulations provide that a container of not less than one-half pint capacity designed or intended to be used for the sale of distilled spirits for other than industrial use is a "liquor bottle" and may be made of glass, earthenware, or other suitable material approved by the Director, Alcohol and Tobacco Tax Division.

Held, aluminum has been found by the Director to be a suitable material (under prescribed conditions) for the manufacture of "liquor bottles." Accordingly, bottle manufacturers who have properly qualified under the permit provisions of the Container Regulations may make seamless "liquor bottles" of such material, with the bottom of the container so shaped that it may not readily be opened with household can openers. Such "liquor bottles" must bear the indicia required by section 175.34 of the regulations. The required indicia may be applied to the "bottles" either by lithographing or by embossing.

Distilled spirits plant proprietors who purchase aluminum "liquor bottles" from authorized bottle manufacturers and use them for marketing their products are cautioned that their finished products (after bottling in such containers) may not contain any greater concentration of aluminum than is permitted by the limitations prescribed by the Food and Drug Administration.

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26 CFR 175.17: Liquor bottle.

The use and manufacture of aluminum seamless liquor bottles. See Rev. Rul. 61–180, above.

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26 CFR 175.30: Permit to manufacture.

The use and manufacture of aluminum seamless liquor bottles in the shape of a can. See Rev. Rul. 61–180, above.

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26 CFR 175.34: Indicia for domestic liquor bottles.

The use and manufacture of aluminum seamless liquor bottles in the shape of a can. See Rev. Rul. 61–180, above.

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26 CFR 201.11: Meaning of terms.

Mandatory marks on the sides of cylindrical steel containers for distilled spirits which have a capacity of ten gallons or less. See Rev. Rul. 61–150, page 274.

26 CFR 201.62: Alternate methods or procedures; and emergency variations from requirements. (Also 201.11, 201.515.) Rev. Rul. 61–150

Section 201.11 of the Distilled Spirits Plants Regulations defines the term "package" to mean "A cask, or barrel or similar wooden container, or a drum or similar metal container." Section 201.515 of the regulations requires that the prescribed marks and brands for packages of distilled spirits shall be placed on one head which shall be called the Government head. This latter section does not include a provision for variation from such requirement in respect of small packages, as was the case under section 182.519 of prior regulations under which proprietors of industrial alcohol plants, for many years, marked small, cylindrical, steel containers, having a capacity of ten gallons or less, on their sides rather than on their heads. Section 201.515 of the regulations does, however, provide for marking "other containers" on their sides. *Held*, where proprietors of distilled spirits plants prefer to place the required marks on the sides of those cylindrical steel containers which have a capacity of ten gallons or less, such proprietors may file applications with the appropriate Assistant Regional Commissioner, Alcohol and Tobacco Tax, under section 201.62, for permission to do so, as an alternative to placing such marks on the heads of the containers.

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26 CFR 201.515: Specifications for marks and brands.

Mandatory marks on the sides of cylindrical steel containers for distilled spirits which have a capacity of ten gallons or less. See Rev. Rul. 61–150, above.

SECTION 5207.—RECORDS AND REPORTS

26 CFR 201.628: Records of spirits in storage.

Recording losses of spirits from packages in bonded storage. See Rev. Proc. 61–16, page 548.

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26 CFR 201.629: Summary of deposits and withdrawals, Form 1621.

Records and reports covering spirits in bonded storage. See Rev. Proc. 61–23, page 558.

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26 CFR 201.633: Monthly reports.

Reporting of imported spirits on Form 2730, Monthly Report of Production Operations. See Rev. Proc. 61–21, page 556.

PART II.—OPERATIONS ON BONDED PREMISES

Subpart A.—General

SECTION 5212.—TRANSFER OF DISTILLED SPIRITS BETWEEN BONDED PREMISES

26 CFR 201.368: Consignor premises.

Recording losses of spirits from packages in bonded storage. See Rev. Proc. 61–16, page 548.

Preparation of an additional copy of Form 2630 when spirits in packages are to be transferred in bond. See Rev. Proc. 61–28, page 19.

Form 236 shall accompany in-bond shipments of spirits by truck. See Rev. Proc. 61–37, page 575.

26 CFR 201.369: Consignee premises.

Form 236 shall accompany in-bond shipments of spirits by truck. See Rev. Proc. 61–37, page 575.

SECTION 5214.—WITHDRAWAL OF DISTILLED SPIRITS FROM BONDED PREMISES FREE OF TAX OR WITHOUT PAYMENT OF TAX

26 CFR 252.23: Reciprocating foreign countries.

Listing of foreign countries for which distilled spirits may be withdrawn free of tax or with benefit of drawback for use as supplies on aircraft. See Rev. Proc. 61–24, page 560.

Listing of foreign countries for which distilled spirits may be withdrawn free of tax or with benefit of drawback for use as supplies on aircraft. See Rev. Proc. 61–34, page 573.

Subpart C.—Storage

SECTION 5234.—MINGLING AND BLENDING OF DISTILLED SPIRITS

26 CFR 201.301: Mingling to consolidate packages under section 5234(a)(2), I.R.C.

Reporting of the date of original entry of spirits on deposit and withdrawal forms covering mingled and blended spirits. See Rev. Proc. 61–17, page 549.

26 CFR 201.307: Permissible blending.

Reporting of the date of original entry of spirits on deposit and withdrawal forms covering mingled and blended spirits. See Rev. Proc. 61–17, page 549.

PART III.—OPERATIONS ON BOTTLING PREMISES

SECTION 5251.—NOTICE OF INTENTION TO RECTIFY

26 CFR 201.432: Record of use. Rev. Rul. 61–220

The Internal Revenue Service has reconsidered the requirements of Revenue Ruling 61–32, C.B. 1961–1, 810, as they involve identification on Form 122, Bottler's Dump and Batch Record, of alcoholic flavoring material produced at other than a rectifying plant. It has decided that information concerning the proof gallons used and the serial number of the package in which the distilled spirits or alcohol were received may be omitted from Form 122. Accordingly, the Revenue Ruling is restated to read as follows:

Sections 201.432(b) and 201.432(c) of the Distilled Spirits Plants Regulations provide, in part, that Form 122, Bottler's Dump and Batch Record, shall identify the spirits, wines, and alcoholic flavoring material used in the batch, and require that where spirits are bottled or packaged especially for export with benefit of drawback, the proprietor shall prepare an additional copy of each related Form 122 and forward it to the Assistant Regional Commissioner, Alcohol and Tobacco Tax. *Held*, the identification of spirits, wines, and alcoholic flavoring materials on Form 122 must be sufficient to permit computation of the drawback rate to be used in settlement of claims covering distilled spirits contained in rectified products bottled or packaged especially for export. Where wine is used the form must show the wine gallons and the taxable class of wine. Where alcoholic flavoring material produced at other than a rectifying plant is used, the form must show the name and address of the manufacturer of the product, and the rate of nonbeverage drawback allowed thereon. *Held further*, an additional copy of all the related Forms 122 necessary for computing drawback, including a copy of any Forms 122 which were prepared to cover previous dumps or batches and which are related to the current bottling or packaging for export, should be prepared by the proprietor and forwarded to the Assistant Regional Commissioner, Alcohol and Tobacco Tax.

Revenue Ruling 61–32, C.B. 1961–1, 810, is hereby superseded.

SECTION 5271.—PERMITS

26 CFR 211.161: Application for withdrawal permit. Rev. Rul. 61–132

Section 211.161 of the Distribution and Use of Denatured Alcohol and Rum Regulations requires Form 1485, Application and With-

drawal Permit of User To Procure Specially Denatured Spirits, to show the total quantity of each formula of specially denatured alcohol to be withdrawn during the term of the permit and the total quantity of each formula which the applicant desires to withdraw during any calendar month. *Held*, where a specially denatured alcohol permittee desires to withdraw during any one calendar month a specified aggregate quantity of any combination of formulas of specially denatured alcohol listed in section I, Form 1485 (original or amended), such listing as to the quantity of each formula of specially denatured alcohol per calendar month should be followed by the applicant's statement in section I to the effect that "the aggregate quantity of the above formulas (or of formulas nos. ———, ———, as the case may be) consisting of any combination thereof which will be withdrawn in any calendar month will not exceed ———gallons, subject to the limitations of 26 CFR 211.72 as to bond coverage." In the event of approval, such a statement should also be inserted in section II, form 1485, under the heading "Conditions," so modified as to reflect whatever further limitations are to be imposed. The quantity per calendar month of each formula specified by the applicant in section I, Form 1485, as to those formulas to be included in the discretion sought by the applicant, must be the same in order that the aggregate quantity authorized to be withdrawn may be specifically limited.

The following examples are given as illustrations:

1. A permittee desires to withdraw 2,000 gallons of specially denatured alcohol, Formula No. 1, regularly during the month and 1,000 gallons of specially denatured alcohol, Formula No. 3–A or Formula No. 23–A or a combination of each. The amount shown for Formula No. 1 would be 2,000 gallons and 1,000 gallons each for Formulas Nos. 3–A and 23–A and the statement to be inserted in section I, Form 1485, should be to the effect that the aggregate quantity of specifically denatured alcohol, Formulas Nos. 3–A and 23–A to be withdrawn during the month will not exceed 1,000 gallons, the total withdrawal to be 3,000 gallons.

2. Where Form 1485 lists four formulas of specially denatured alcohol and specifies 1,000 gallons of each and the permittee desires to withdraw an aggregate of 1,000 gallons of any combination of such formulas, the statement to be inserted in section I of the form should be to the effect that the aggregate quantity of any combination of such formulas to be withdrawn during the month will not exceed 1,000 gallons.

SECTION 5275.—RECORDS AND REPORTS

26 CFR 211.271: Reports of users. Rev. Rul. 61–154

Where, during a fiscal year, a permittee discontinues the use of specially denatured alcohol or rum, a summary report, covering all transactions from July 1 to the date of discontinuance, should be submitted on Form 1482, User's Report of Denatured Alcohol or Rum, whether or not the permittee had been filing reports on a monthly basis. A permittee changing from monthly to annual reporting during the fiscal year should include, on his report at the close of the fiscal year, the same information as any other permittee

who files on an annual basis. However, a permittee who goes from an annual to a monthly reporting basis during a fiscal year will, in his first monthly report, cover all transactions from July 1 to the close of the month covered by the report.

The Internal Revenue Service has been requested to answer a series of questions concerning the preparation and submission of Form 1482, User's Report of Denatured Alcohol or Rum.

Section 5275 of the Internal Revenue Code of 1954 provides, in part, that every person procuring or using distilled spirits withdrawn under section 5214(a) (2) or (3) of the Code, or procuring, dealing in, or using specially denatured distilled spirits, or recovering specially denatured or completely denatured distilled spirits, shall keep such records and file such reports of the receipt and use of distilled spirits withdrawn free of tax, of the receipt, disposition, use, and recovery of denatured distilled spirits, the manufacture and disposition of articles, and such other information as the Secretary of the Treasury or his delegate may by regulations prescribe.

Section 211.271 of the Distribution and Use of Denatured Alcohol and Rum Regulations provides as follows:

Persons who use specially denatured spirits or recover specially denatured spirits or articles shall prepare monthly reports on Form 1482: *Provided*, That in any instance where—

(a) The user is authorized to withdraw not over 660 gallons per annum, or

(b) The assistant regional commissioner, pursuant to application by the user who is authorized to withdraw more than 660 gallons per annum, finds that the permittee has an accounting system which will afford an adequate measure of control, and that the filing of an annual report will not interfere with the effective administration of the regulations in this part, such permittees may submit an annual report on Form 1482, on a fiscal year basis, in lieu of monthly reports for such period. Notwithstanding the foregoing provisions, the assistant regional commissioner may at any time require the submission of monthly reports on Form 1482 by any permittee. Where both specially denatured alcohol and specially denatured rum are used, a separate report shall be prepared for each. The user shall submit the original of the Form 1482 to the assistant regional commissioner not later than the 10th day of the month succeeding the period for which the report is submitted and retain the duplicate for his files.

The specific questions presented to the service and the answers thereto are as follows:

Question 1. The "General Instructions" on Form 1482 require that permittees who discontinue business during the year must file a summary report of all transactions from July 1 to the date of discontinuance. Such a summary report is to be marked "Final Report." Does this instruction apply where monthly reports are filed?

Answer. Where, during a fiscal year, a permittee discontinues the use of specially denatured alcohol or rum, a summary report, covering all transactions from July 1 to the date of discontinuance, should be submitted on Form 1482, whether the permittee had been filing reports on a monthly or annual basis. However, if monthly reports have been filed, entries in section II of the form may be limited to the month in which the business was discontinued and to the total columns.

Question 2. A permittee, filing reports on a monthly basis, is authorized to withdraw more than 660 gallons per annum. During the

fiscal year he reduces his authorized withdrawals to less than 660 gallons per annum. Should the permittee in his summary include the quantity used and recovered during the period in which he filed monthly reports and reflect in the annual report, sections I, II, and III of the form, the transactions for the remaining portion of the fiscal year?

Answer. Where, during the fiscal year, a permittee changes from monthly to annual reporting, his report at the close of the fiscal year should include the same information as that which would be included by any other permittee who files on a annual basis, *i.e.*, summaries in sections I, II, and III of the form must cover transactions for the entire year.

Question 3. A permittee withdrawing less than 660 gallons per annum increased his annual allowance during the fiscal year to more than 660 gallons. Should the permittee file a report of all transactions, sections I, II, and III of Form 1482, for the period during which he was authorized to withdraw less than 660 gallons and file an annual summary of the quantity used and recovered during the period for which he filed monthly reports?

Answer. A permittee who goes from an annual to a monthly reporting basis during a fiscal year will, in his first monthly report, cover all transactions from July 1 to the close of the month covered by the report. Subsequently, monthly reports will be prepared in the same manner as for a permittee who filed on a monthly basis for the entire year, and the annual summary will be prepared to cover the entire fiscal year, as provided in the instructions on the form.

SUBCHAPTER F.—BONDED AND TAXPAID WINE PREMISES

PART II.—OPERATIONS

SECTION 5361.—BONDED WINE CELLAR OPERATIONS

26 CFR 240.134: Other operations. T.D. 6566 [1]
(Also Section 5382; 240.527a.)

TITLE 26—INTERNAL REVENUE.—CHAPTER I, SUBCHAPTER E, PART 240.—WINE

Amendments relating to use of premises and to removal of excess color from wine.

DEPARTMENT OF THE TREASURY,
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 implement the provisions of section 5361, Internal Revenue Code, and to liberalize the provisions of 26 CFR Part 240 with respect to the removal with activated carbon of excess color

[1] 26 F.R. 7264.

from white wine, 26 CFR Part 240 is amended as follows:

§ 240.130 [Amendment]

1. Section 240.130 is amended:

(A) By striking from the first sentence the phrase "and no materials," and inserting in lieu thereof the phrase "and, except in connection with other operations approved pursuant to § 240.134, no materials,"; and

(B) By changing the citation at the end of the section to read "(72 Stat. 1378, 1380; 26 U.S.C. 5351, 5361)."

2. A new section, reading as follows, is inserted immediately following § 240.133:

§ 240.134 OTHER OPERATIONS.—(a) The proprietor of a bonded wine cellar may, under the provisions of this section, conduct on bonded wine cellar premises such other operations not specifically provided for in this part as the Director, Alcohol and Tobacco Tax Division, finds may be conducted in a manner that will not jeopardize the revenue, or conflict with wine operations, or be contrary to law.

(b) A proprietor desiring to conduct other operations as provided in paragraph (a) of this section shall file an application, in triplicate, with the assistant regional commissioner setting forth in detail the operation to be conducted and the building and equipment to be used. The proposed operation shall not be conducted until the Director, Alcohol and Tobacco Tax Division, has made his finding, as required by paragraph (a) of this section, and the assistant regional commissioner has approved the application. Where the Director, Alcohol and Tobacco Tax Division, has found that the conduct of such other operation will not jeopardize the revenue, or conflict with wine operations, or be contrary to law, the assistant regional commissioner may approve applications to conduct a similar type of operation, unless he finds there are particular conditions in respect of the applicant's premises or operations that would cause the conduct of such operation to be a jeopardy to the revenue or to conflict with wine operations.

(c) Operations authorized under this section shall be conducted with such degree of segregation from wine operations as may be required by the assistant regional commissioner under the provisions of § 240.131.

(d) The proprietor shall, with respect to each operation authorized under this section, keep records of the kind and quantity of materials received and used, the products produced, and the disposition of such products. If sugar is used in the production of such products, the receipt and use of the sugar so used will be shown on the sugar record required by § 240.914. (72 Stat. 1380; 26 U.S.C. 5361.)

§ 240.527 [Amendment]

3. Section 240.527 is amended:

(A) By striking from the first sentence the phrase "during its production or storage" and inserting in lieu thereof the phrase "during the production or storage of a particular lot or lots"; and

(B) By changing the citation at the end of the section to read "(72 Stat. 1383; 26 U.S.C. 5382)."

4. A new section, reading as follows, is inserted immediately following § 240.527:

§ 240.527a CONTINUING AUTHORITY TO USE ACTIVATED CARBON.—(a) *Application.*—A proprietor desiring to obtain continuing authority to use activated carbon to remove excess color from white wine (other than vermouth) shall file application, in duplicate, with the assistant regional commissioner. Such application shall contain all of the information required by § 240.527, except that the quantity of wine to be treated may be estimated, and shall also set forth:

(1) The range of color (Lovibond scale in a one-half inch cell) of the expressed juice before treatment with any material having a decolorant effect.

(2) The pounds of activated carbon to be used per 1,000 gallons of wine and/or juice and the length of time such carbon will be in contact with the wine and/or juice.

(3) The approximate temperature of the juice or wine during treatment.

(4) A description or explanation of any unusual factors of the treatment.

(b) *Conditions.*—Proprietors authorized pursuant to application under paragraph (a) of this section to treat white wine with activated carbon shall conform with the following conditions:

(1) The vinous character of the product treated shall not be reduced.

(2) The quantity of activated carbon used per 1,000 gallons of wine, including any activated carbon used in the basic wine-producing material, shall not exceed 9 pounds.

(3) The wine treated with activated carbon shall have a color of not less than 0.6 Lovibond in a one-half inch cell; however, if a proprietor by using usual methods produces wine having a color of less than 0.6 Lovibond scale, without the use of carbon, such production is permitted.

(c) *Records.*—Proprietors authorized pursuant to application under paragraph (a) of this section to treat white wine with activated carbon shall keep records showing, for each batch of wine or basic wine-producing material so treated, the exact details of such treatment, including the kind and quantity of juice (if grape, by grape variety), and the kind and quantity of activated carbon used. Such records shall also show the complete cellar treatment given the finished wine, such as the use of sulphur dioxide, and the length of time the activated carbon is in contact with the wine.

(d) *Transfers in bond.*—Where wine has been treated under the provisions of this section and is later transferred in bond, the consignor proprietor shall record on Form 703 covering such transfer, and the consignee proprietor shall record in his records, the amount of activated carbon used in treating the wine before its transfer. The consignee proprietor may further treat such wine with activated carbon provided (1) he has received authority pursuant to application under paragraph (a) of this section to so treat wine, and (2) the total amount of activated carbon used before and after the transfer of the wine does not exceed 9 pounds per 1,000 gallons of wine, i.e., if 5 pounds of activated carbon per 1,000 gallons were used in the wine before its transfer, not more than 4 pounds of activated carbon per 1,000 gallons shall be used by the consignee proprietor in treating the same wine. (72 Stat 1383; 26 U.S.C. 5382.)

Because this Treasury Decision will liberalize these regulations by enabling proprietors (1) to conduct other operations on their bonded wine cellar premises, and (2) to obtain continuing authority to treat white wine with activated carbon, 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. Accordingly, this Treasury Decision shall become effective on the date of its publication in the Federal Register.

(This Treasury Decision is issued under the authority contained in section 7805 of the Internal Revenue Code (68A Stat. 917; 26 U.S.C. 7805).)

MORTIMER M. CAPLIN,
Commissioner of Internal Revenue.

Approved August 8, 1961.

STANLEY S. SURREY,
Assistant Secretary of the Treasury.

(Filed by the Division of the Federal Register on August 10, 1961, 8:53 a.m., and published in the issue of the Federal Register for August 11, 1961, 26 F.R. 7264)

SECTION 5362.—REMOVALS OF WINE FROM BONDED WINE CELLARS

26 CFR 240.670: General.

Listing of foreign countries for which wines may be withdrawn free of tax or with benefit of drawback for use as supplies on aircraft. See Rev. Proc. 61–34, page 573.

Listing of foreign countries for which wines may be withdrawn free of tax or with benefit of drawback for use as supplies on aircraft. See Rev. Proc. 61–24, page 560.

SECTION 5368.—GAUGING, MARKING, AND STAMPING

26 CFR 240.575: Remarking, reshipping, or tax-paying containers received from other premises. Rev. Rul. 61–125

Section 240.575 of the Wine Regulations provides in part that when wine received in bond from other premises is removed, in the containers in which received, for consumption or sale, the proprietor shall mark the containers "Taxpaid" or "TP," followed by the registry number and state of the taxpaying premises, on the same side of the container as the original marks.

Held, when wine received in bond is, because the original cases were damaged, recased prior to removal, the new cases must, in addition to the marking required in section 240.575 of the regulations, be marked with all of the required marks and brands on the original cases, except that proprietors of bonded wine cellars may substitute the date of repacking preceded by the letter "P" for the serial number and the date of filling which appeared on the original case, if such original marking is no longer legible or if the new case contains bottles repacked from more than one original case.

Revenue Ruling 61–39, C.B. 1961–1, 820, is hereby superseded.

PART III.—CELLAR TREATMENT AND CLASSIFICATION OF WINE

SECTION 5382.—CELLAR TREATMENT OF NATURAL WINE

26 CFR 240.364: Acids.

Use of lactic acid in natural grape and fruit wines. See Rev. Rul. 61–151, page 283.

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26 CFR 240.404: Acids.

Use of lactic acid in natural grape and fruit wine. See Rev. Rul. 61–151, page 283.

26 CFR 240.524: Finishing of wine. Rev. Rul. 61–126
(Also 240.1051, 240.1052.)

The use of uncharred and untreated oak chip sawdust by winemakers, in the treatment of wines, is considered as being consistent with good commercial practice within the limitations of section 240.524 of the Wine Regulations. Winemakers desiring to use uncharred and untreated oak chip sawdust in the treatment of wines may receive the approval of the Assistant Regional Commissioner, Alcohol and Tobacco Tax, by the filing of appropriate notice pursuant to section 240.1052 of the regulations.

(Also 240.364, 240.404, 240.526, 240.1052.) Rev. Rul. 61–151

The use of lactic acid to correct natural deficiencies in natural grape wine and natural fruit wine and to stabilize such wines is considered as being consistent with good commercial practice within the limitations of section 240.524 of the Wine Regulations. Winemakers desiring to use lactic acid may receive the approval of the Assistant Regional Commissioner, Alcohol and Tobacco Tax, by the filing of appropriate notice pursuant to section 240.1052 of the regulations.

The use of lactic acid to correct natural deficiencies will be subject to the same conditions and limitations prescribed by section 240.364 and 240.404 of the regulations in respect of the use of other kinds of acids for the same purpose. The use of lactic acid for stabilizing either natural grape wine or natural fruit wine will be subject to the conditions and limitations imposed by section 240.526 of the regulations on the use of citric acid for this purpose.

(Also 240.1051, 240.1052.) Rev. Rul. 61–199

The use of a product, consisting of Locust Bean Gum, Carragheen, Alginate, Bentonite, Agar Agar, and Diatomaceous Earth, within the general limitations of section 240.524 of the Wine Regulations, to clarify wine, in amounts not exceeding two pounds per 1,000 gallons of wine, is considered as being consistent with good commercial practice. Winemakers desiring to use this product in the clarification of wine may obtain the approval of the Assistant Regional Commissioner, Alcohol and Tobacco Tax, by filing a notice pursuant to section 240.1052 of the regulations.

(Also 240.1052.) Rev. Rul. 61–200
(Also Section 5041; 240.531.)

The use of vitagen gas within the general limitations of section 240.524 of the Wine Regulations, to remove air and to reduce oxidation in the production of wine is considered as being consistent with good commercial practice. The limitations prescribed by section 5041 (a) of the Internal Revenue Code of 1954 and section 240.531 of the regulations, with respect to the use of carbon dioxide (an ingredient of vitagen gas) in still wines, must be observed by winemakers using the material. Conditions prescribed by the Food Additives [Added] Regulations, 21 CFR 121, issued by the Food and Drug Administration of the Department of Health, Education, and Welfare, are also

applicable with respect to the use of the product. Winemakers desiring to use vitagen gas for these purposes may obtain approval of the Assistant Regional Commissioner, Alcohol and Tobacco Tax, by filing a notice pursuant to the provisions of section 240.1052 of the regulations.

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26 CFR 240.526: Stabilizing grape wine.

Use of lactic acid in natural grape and fruit wine. See Rev. Rul. 61–151, page 283.

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26 CFR 240.527(a): Continuing authority to use activated carbon.

Provisions relating to continuing authority to use activated carbon in the treatment of white wine. See T.D. 6566, page 279.

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26 CFR 240.1051: Materials authorized for treatment of wine.

Use of uncharred and untreated oak chip sawdust in the treatment of wine. See Rev. Rul. 61–126, page 283.

Use of a product consisting of Locust Bean Gum, Carragheen, Alginate, Bentonite, Agar Agar, and Diatomaceous Earth to clarify wine. See Rev. Rul. 61–199, page 283.

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26 CFR 240.1052: Notice.

Use of uncharred and untreated oak chip sawdust in the treatment of wine. See Rev. Rul. 61–126, page 283.

Use of lactic acid in natural grape and fruit wine. See Rev. Rul. 61–151, page 283.

Use of a product consisting of Locust Bean Gum, Carragheen, Alginate, Bentonite, Agar Agar, and Diatomaceous Earth to clarify wine. See Rev. Rul. 61–199, page 283.

The use of vitagen gas to remove air and reduce oxidation in the production of wine. See Rev. Rul. 61–200, page 283.

SUBCHAPTER I.—MISCELLANEOUS GENERAL PROVISIONS

SECTION 5555.—RECORDS, STATEMENTS, AND RETURNS

26 CFR 201.633: Monthly reports.

Reporting of imported spirits on Form 2730, Monthly Report of Production Operations. See Rev. Proc. 61–21, page 556.

SUBPART B.—RULINGS AND DECISIONS UNDER THE FEDERAL ALCOHOL ADMINISTRATION ACT

Rulings and decisions published in Part III, Subpart B, of the Internal Revenue Bulletin are based on the application of provisions of the Federal Alcohol Administration Act.

SECTION 5.—UNFAIR COMPETITION AND UNLAWFUL PRACTICES

27 CFR 5.21: The standards of identity.

Certificates of identification and analysis for French grape brandies other than Cognac and Armagnac. See Rev. Proc. 61–26, page 562.

SECTION 5(e).—UNFAIR COMPETITION AND UNLAWFUL PRACTICES: LABELING

27 CFR 4.45: Certifications of origin and identity.

Certificates of origin and identity for Portuguese wines. See Rev. Proc. 61–22, page 557.

Certificates of origin and identity for Spanish sherry wines. See Rev. Proc. 61–33, page 572.

PART IV

LEGISLATION AND TREATIES

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PART IV

LEGISLATION AND TREATIES

SUBPART A.—TAX CONVENTIONS

UNITED STATES-CANADA INCOME TAX CONVENTION

26 CFR 519.112: Reduction in rate of tax withheld at source.
(Also Part I, Section 1442; 1.1442–1.)

T. D. 6576 [1]

TITLE 26—INTERNAL REVENUE.—CHAPTER I, SUBCHAPTER G, PART 519.—CANADA

Treasury Decisions 5206 and 6047 amended to provide for the termination of paragraph 2 of Article XI of the income tax convention between the United States and Canada with respect to dividends paid by related corporations.

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

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

On March 28, 1961, a notice of proposed rulemaking with respect to amendments of the general regulations (Treasury Decision 5206, approved December 31, 1942 [C.B. 1943, 526]) and of the withholding regulations (Treasury Decision 6047, approved November 5, 1953 [C.B. 1953–2, 59]) under the income tax convention between the United States and Canada was published in the Federal Register (26 F.R. 2619). No objection to the amendments proposed having been received during the 30-day period prescribed in the notice, the amendments to Treasury Decisions 5206 and 6047 as so proposed are hereby adopted.

PARAGRAPH 1. On December 20, 1960, an Income Tax Act Resolution was introduced in the House of Commons by the Minister of Finance of Canada with his Budget Speech providing that the rate of tax payable by a corporation not resident in Canada on dividends received from a Canadian resident, which rate of tax was limited to 5 percent in accordance with paragraph 2 of Article XI of the income tax convention between the United States and Canada of March 4, 1942 [C.B. 1943, 526], as amended by the supplementary convention signed June 12, 1950 [C.B. 1955–1, 624], and by the supplemen-

[1] 26 F.R. 10129.

tary convention signed August 8, 1956 [C.B. 1957–2, 1014], was increased to 15 percent with respect to dividends paid after December 20, 1960. As announced in Technical Information Release No. 283, issued on December 29, 1960, the Internal Revenue Service stated that paragraph 2 of Article XI of the convention was terminated, by virtue of the provisions of paragraph 3 of Article XI of the convention, effective with respect to dividends paid after December 20, 1960. As indicated in the Technical Information Release, United States income tax and withholding of United States tax at source will apply without regard to the provisions of paragraph 2 of Article XI of the convention (as amended) in the case of dividends paid after December 20, 1960. In conformity thereto, the general regulations (Treasury Decision 5206, approved December 31, 1942) and the withholding regulations (Treasury Decision 6047, approved November 5, 1953) which were issued under the income tax convention between the United States and Canada are amended as follows:

Treasury Decision 5206

(A) Section 7.31 (26 CFR 519.112) is amended by revising the second and third undesignated subparagraphs of paragraph (a) thereof. These amended provisions read as follows:

SEC. 7.31 REDUCTION IN RATE OF THE TAX WITHHELD AT SOURCE.—(a) *General.* * * *

Under the provisions of Article XI, dividends paid to a Canadian corporation not engaged in trade or business within the United States and not having an office or place of business therein by a domestic subsidiary corporation are subject to tax at the rate of only 5 percent, such dividends constituting an exception to the general rule laid down in paragraph 1 of Article XI. Since paragraph 2 of Article XI of the convention (as amended) was terminated with respect to dividends paid after December 20, 1960, the rate of 5 percent prescribed therein will not apply in determining the income tax imposed upon dividends paid after such date to a Canadian corporation. For the purposes of that article, a "subsidiary corporation" is defined in paragraph 6 of the protocol as a corporation (in this case a domestic corporation) all of whose shares (less directors' qualifying shares) having full voting rights are beneficially owned by another corporation (in this case a Canadian corporation), provided that 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. Thus, for example, the A Corporation is a domestic corporation all of whose shares are owned by B Company, Ltd., a Canadian corporation not engaged in trade or business within the United States and not having any office or place of business therein. The A Corporation pays a dividend to B Company, Ltd., on June 30, 1943. The A Corporation is on a calendar year basis and throughout 1940, 1941, and 1942 derived not more than 15 percent of its gross income from interest and dividends from corporations not controlled by the A Corporation. The Commissioner ascertains and has so notified the A Corporation that the corporate relationship between the A Corporation and the B Company, Ltd., has not been arranged and is not maintained primarily for the purpose of securing the lower rate of tax prescribed in paragraph 2 of Article XI of the convention. The dividend paid by the A Corporation is subject to withholding of the tax at the lower rate of 5 percent.

Any domestic corporation which claims or contemplates claiming, that dividends paid by it, or to be paid by it, are subject only to the 5 percent rate, shall file, as soon as practicable, with the Commissioner the following information: (1) The date and place of its organization; (2) the number of its outstanding shares of stock having full voting rights; (3) the person or persons beneficially owning such stock and their relationship to such corporations; (4) the amount of gross income, by years, of the paying corporation for the 3-year period immediately

preceding the taxable year in which such dividend is paid; (5) the amount of interest and dividends, by years, included in such gross income and the amount of interest and dividends, by years, received from the subsidiary corporations, if any, of such domestic corporation; and (6) the corporate relationship between such domestic corporation and the Canadian corporation to which it pays the dividend. As soon as practicable after such information is filed, the Commissioner shall examine it and determine whether the dividends concerned fall within the provisions of such paragraph and may authorize the release of excess tax withheld with respect to dividends which are shown to the satisfaction of the Commissioner to come within the provisions of paragraph 2 of Article XI of the convention. In any case in which the Commissioner has notified such domestic corporation that it comes within the provisions of paragraph 2 of Article XI of the convention, the reduced rate of 5 percent applies to any dividends subsequently paid by such corporation before December 21, 1960, unless its stock ownership or the character of its income materially changes. In the event of such changes occurring, such corporation shall promptly notify the Commissioner of the then existing facts with respect to such stock ownership and income.

Treasury Decision 6047

(B) Section 7.46 (26 CFR 519.2) is amended by adding a new subparagraph at the end of paragraph (b) thereof and by revising the first undesignated subparagraph of paragraph (d) thereof. These amended provisions read as follows:

SEC. 7.46 DIVIDENDS.

* * * * * * *

(b) *Dividends paid by related corporation.* * * *

Since Article XI (2) of the convention (as amended) was terminated with respect to dividends paid after December 20, 1960, the rate of 5 percent prescribed therein will not apply in determining the income tax imposed upon, or the amount of tax to be withheld at the source from, dividends paid after such date to a Canadian corporation.

* * * * * * *

(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). However, see the last subparagraph of paragraph (b) of this section.

(C) Section 7.52 (26 CFR 519.8) is amended by revising paragraph (c) thereof. This amended provision reads as follows:

SEC. 7.52 RELEASE OF EXCESS TAX WITHHELD AT SOURCE.

* * * * * * *

(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. This paragraph shall not apply with respect to dividends paid after December 20, 1960.

PAR. 2. The withholding of United States tax at the rate of 5 percent from dividends paid after December 20, 1960, and before Decem-

ber 30, 1960, to a Canadian corporation, which would have been entitled to the benefit of such rate in accordance with paragraph 2 of Article XI of the income tax convention between the United States and Canada of March 4, 1942, as amended, if such paragraph had been in effect during such period, shall be considered to constitute compliance with the provisions of law respecting withholding of tax at source upon such dividends. A Canadian corporation receiving such dividends upon which United States tax at the rate of only 5 percent was withheld shall, however, make a return of income in accordance with paragraph (g) of § 1.6012–2 of the Income Tax Regulations and pay the additional tax due.

(This Treasury Decision is issued under the authority contained in section 7805 of the Internal Revenue Code of 1954 (68A Stat. 917; 26 U.S.C. 7805) and in 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.)

MORTIMER M. CAPLIN,
Commissioner of Internal Revenue.

Approved October 24, 1961.

STANLEY S. SURREY,
Assistant Secretary of the Treasury.

(Filed by the Division of the Federal Register on October 27, 1961, 8:48 a.m., and published in the issue of the Federal Register for October 28, 1961, 26 F.R. 10129)

SUBPART B.—LEGISLATION

DIGEST OF PUBLIC LAWS ENACTED DURING THE FIRST SESSION OF THE 87TH CONGRESS WHICH PERTAIN TO INTERNAL REVENUE MATTERS

Public laws pertaining to internal revenue matters which were enacted during the first session of the 87th Congress are as follows:

Public law number	Date approved	Digested on page	Public law number	Date approved	Digested on page
87-6 (H.R. 4806)	3-24-61	294	87-235 (S.1518)	9-14-61	306
87-15 (H.R. 5463)	3-31-61	294	87-256 (H.R. 8666)	9-21-61	300
87-24 (S. 1295)	4-24-61	306	87-262 (H.R. 6302)	9-21-61	306
87-29 (H.R. 5189)	5- 4-61	294	87-293 (H.R. 7500)	9-22-61	302
87-59 (H.R. 1877)	6-27-61	295	87-298 (H.R. 8236)	9-26-61	307
87-61 (H.R. 6713)	6-29-61	296	87-312 (H.R. 7057)	9-26-61	307
87-64 (H.R. 6027)	6-30-61	298	87-321 (H.R. 2585)	9-26-61	304
87-72 (H.R. 7446)	6-30-61	299	87-345 (H.R. 2010)	10- 3-61	307
87-109 (H.R. 929)	7-26-61	299	87-370 (H.R. 4317)	10- 4-61	305
87-205 (H.R. 5964)	9- 6-61	306	87-397 (H.R. 8876)	10- 5-61	305

The following sections of the Internal Revenue Code of 1954, and the following Public Laws, have been amended by the Public Laws indicated.

INDEX OF INTERNAL REVENUE CODE OF 1954—SECTIONS AMENDED

Code section	Public law number	Public law section	Code section	Public law number	Public law section
11(b)	87-72	2	3306(c)	87-256	110(f)
117(b)(2)(A)	87-256	110(a)	3401(a)	87-293	201(c)
403(b)	87-370	3(a)	3401(a)(6)	87-256	110(g)(1)
456	87-109	1(a)	3402(f)	87-256	110(g)(2)
809(d)(11)	87-59	2(a)	4041(a)	87-61	201(a)
809(g)(3)	87-59	2(b)	4041(b)	87-61	201(a)
821(a)(1)(A)	87-72	2	4041(c)	87-61	201(c)
821(b)(1)	87-72	2	4041(f)	87-61	201(d)
871	87-256	110(b)	4061	87-72	3(a)(1)
872(b)	87-256	110(c)	4061(a)(1)	87-61	204
895	87-29	1(a)	4071(a)(1)	87-61	202(a)
912	87-293	201(a)	4071(a)(3)	87-61	202(b)
1303(b)	87-293	201(b)	4071(a)(4)	87-61	202(c)
1372	87-29	2	4071(c)	87-61	202(d)
1401	87-64	201(a)	4081(a)	87-61	201(b)
1402(e)	87-64	202(a)	4081(b)	87-61	201(c)
1441(a)	87-256	110(d)(1)	4081(c)	87-61	201(d)
1441(b)	87-256	110(d)(2)	4218(a)	87-61	205(b)
1441(c)(4)	87-256	110(d)(3)	4221(d)(6)	87-61	205(a)
3101	87-64	201(b)	4226(a)	87-61	206(a)
3111	87-64	201(c)	4226(d)	87-61	206(b)
3121	87-293	202(a)(2)	4251(b)(2)	87-72	3(a)(2)
3121(b)	87-256	110(e)(1)	4261	87-72	3(a)(3)
3121(i)	87-293	202(a)(1)	4481(a)	87-61	203(a)
3122	87-293	202(a)(3)	4481(a)	87-61	203(b)(2)(A)
3301	87-6	14(a)	4481(c)	87-61	203(b)(2)(B)
3302	87-321	1(a)	4481(d)	87-61	203(b)(2)(B)
3302(d)(1)	87-6	14(b)	4481(e)	87-61	203(b)(1)

INDEX OF INTERNAL REVENUE CODE OF 1954—SECTIONS AMENDED—Continued

Code section	Public law number	Public law section	Code section	Public law number	Public law section
4482(c)	87–61	203(b)(2)(C)	6109	87–397	1(a)
4501(c)	87–15	2(a)	6156	87–61	203(c)(1)
5001(a)(1)	87–72	3(a)(4)	6412(a)(1)	87–72	3(b)(3)
5001(a)(3)	87–72	3(a)(5)	6412(a)(2)	87–61	206(c)
5022	87–72	3(a)(6)	6412(a)(3)	87–61	206(d)
5041(b)	87–72	3(a)(7)	6412(d)	87–15	2(b)
5051(a)	87–72	3(a)(8)	6416(b)(2)(E)	87–61	205(d)
5063	87–72	3(b)(1)	6416(b)(3)	87–61	205(c)
5701(c)(1)	87–72	3(a)(9)	6421(h)	87–61	201(e)
5707(a)	87–72	3(b)(2)	6601(c)(2)	87–61	203(c)(2)
5707(b)	87–72	3(b)(2)	6676	87–397	1(b)
6051(a)	87–293	202(a)(4)	7448	87–370	1

Following is a brief explanation of the provisions of the above public laws and the respective Code sections amended thereby. The statements explaining Code sections before amendments and the amendments thereto are not intended as interpretations but are intended merely to indicate the general nature or effect of the provisions involved. Alcohol, tobacco and firearm provisions are omitted.

AMENDMENTS TO THE 1954 CODE

PUBLIC LAW 87–6 (C.B. 1961–1, 854).

3301

Temporary increase in tax rate under Federal Unemployment Tax Act.—Section 14(a) of this Act amends section 3301 by temporarily increasing the present tax rate of 3.1 percent to 3.5 percent for the calendar years 1962 and 1963.

3302(d)(1)

Use of 3 percent tax rate in application of limit on total credits.—Section 14(b) of this Act amends section 3302(d)(1) to provide that in applying the limit on total credits under section 3302(c), the amount of tax under section 3301 shall be computed at the rate of 3 percent.

PUBLIC LAW 87–15 (C.B. 1961–1, 855).

4501(c), 6412(d)

Amendment of the Sugar Act of 1948.—Section 2(a) of this Act amends section 4501(c) to postpone the termination of the tax on manufactured sugar from September 30, 1961, to December 31, 1962.

Section 2(b) of this Act amends section 6412(d) to provide that floor stocks refund shall apply to manufactured sugar held by importers for sale on December 31, 1962, rather than September 30, 1961, if claim for such refund is filed on or before March 31, 1963.

PUBLIC LAW 87–29 (page 307, this Bulletin).

895

Exemption from tax of income derived from obligations of the United States by foreign central banks of issue.—Section 1 of this

Act adds a new section 895 which exempts from tax all income derived from investments in United States obligations maintained for the central banking function of foreign central banks of issue. This exemption does not extend to income derived from similar holdings used in connection with their commercial banking activities. This section is effective with respect to income received during taxable years beginning after December 31, 1960.

1372

Consents to elections by small business corporations.—Section 2 of this Act amends section 1372 (relating to elections by small business corporations) by adding a new subsection (g) under which the period for filing a consent to an election in the case of a husband and wife holding shares of stock as community property (or the income from which was community income) shall not expire prior to May 15, 1961, if either spouse filed a timely consent to such election for a taxable year beginning before January 1, 1961.

PUBLIC LAW 87–59 (page 308, this Bulletin).

Retroactive tax exemption for Plumbers' Local 12 pension fund.—Where a pension plan for employees has been negotiated under and pursuant to a collective bargaining agreement between a union and one or more employers, the employer contributions toward the cost of such plan usually begin immediately. Normally the only detail of the plan agreed upon at the time of the collective bargaining agreement is the rate of contributions to be made thereto by the bargaining employer or employers. All other necessary details of a plan meeting the requirements of section 401(a) of the Code are to be worked out, agreed upon, and adopted after employer contributions have begun. Prior to the adoption of a plan sufficient in all of its details to meet the requirements of section 401(a), often from 1 or 2 or more years, the employer contributions are made to a trust (or escrow fund) not exempt under section 501(a) of the Code and such contributions are usually not deductible under section 404(a) of the Code. Section 1 of this Act provides retroactive tax relief for the trust, and therefore also for the employers who made contributions thereto prior to June 4, 1959, in the case of Plumbers' Union Local Numbered 12 Pension Fund, which found itself in this situation. This Fund came into existence on September 1, 1954, but a plan meeting the requirements of section 401(a) was not adopted until the later date. However, the retroactive relief is granted only on the condition that it be shown to the satisfaction of the Service that the trust did not operate during the period September 1, 1954, to June 3, 1959, in a manner which would jeopardize the interests of its beneficiaries.

809(d)(11), 809(g)(3)

Certain Mutualization Distributions by Stock Life Insurance Companies.—Section 2 of this Act amends section 809(d)(11) (relating to deductions in computing gain from operations in the case of certain mutualization distributions) and section 809(g)(3) (relating to application of section 815 to certain mutualization distributions) so as to extend their application to 1960 and 1961.

Retroactive tax exemption for Composition Roofers, Damp and Waterproof Workers' Local 8 pension fund. Section 4 of this Act

provides retroactive tax relief for the trusts, and therefore also for the employers who made contributions thereto prior to November 25, 1958, in the case of the pension fund of the Composition Roofers, Damp and Waterproof Workers Association, Local Union Numbered 8, which found itself in the same situation as the Plumbers' Local Numbered 12 Pension Fund (Section 1 of this Act). This fund came into existence on July 1. 1957, but a plan meeting the requirements of section 401(a) was not adopted until November 25, 1958. However, the retroactive relief is granted only on the condition that it be shown to the satisfaction of the Service that the trust did not operate during the period July 1, 1957, to November 24, 1958, in a manner which would jeopardize the interests of its beneficiaries.

PUBLIC LAW 87-61 (page 309, this Bulletin).

4041(a), 4041(b), 4041(c), 4041(f), 4081(a), 4081(b), 4081(c), 6421(h)

FEDERAL-AID HIGHWAY ACT OF 1961

Continuation of motor fuel tax and repeal of temporary provisions.—The tax on gasoline, diesel and special motor fuels had been temporarily increased from 3 cents to 4 cents per gallon for the period October 1, 1959, through June 30, 1961, and the 3-cent per gallon rate was scheduled to be reduced to 1½ cents a gallon on July 1, 1972. Section 201 of this Act repeals the temporary provisions, sections 4041(f) and 4081(c), and continues the 4-cent per gallon rate on these products until October 1, 1972, when the rate of tax shall be reduced to 1½ cents per gallon. In the case of diesel and special motor fuels purchased at the 2 cent per gallon tax rate for use in unregistered highway vehicles or in highway vehicles owned by the United States but not used on the highway, section 201(a) of the Act amends sections 4041(a) and (b) to provide for an increase to 2 cents per gallon of tax imposed on the subsequent use of such fuel on the highway. Section 201(e) amends section 6421(h) so that the provisions of section 6421, relating to claims for payment for gasoline used for certain non-highway purposes or by local transit systems, would be applicable to gasoline purchased after June 30, 1956, and before October 1, 1972. These amendments take effect on July 1, 1961.

4071(a)(1), 4071(a)(3), 4071(a)(4), 4071(c)

Increase in tax rates on certain tires, tubes, and tread rubber.—Section 202 of this Act amends section 4071 to provide for an increase in tax on tires of the type used on highway vehicles from 8 to 10 cents per pound; on inner tubes for tires from 9 to 10 cents per pound; and on tread rubber from 3 to 5 cents per pound. This section also amends section 4071(c) to extend from July 1, 1972 to October 1, 1972, the scheduled reduction in tax rates on tires of the type used on highway vehicles and inner tubes and the termination of the tax on tread rubber. These amendments take effect on July 1, 1961.

4481(a), 4481(c), 4481(d), 4481(e), 4482(c)

Increase in highway use tax and conforming amendments required by the new definition of the term "taxable period".—Section 203(a) of this Act amends section 4481(a) to increase the highway use tax rate on certain motor vehicles from $1.50 to $3.00 a year for each 1,000

pounds of taxable gross weight or fraction thereof. However, for the taxable period beginning on July 1, 1972 and ending on September 30, 1972, which period comes within the term "taxable period" as provided by section 203(b) of this Act, such rate of tax shall be 75 cents for each 1,000 pounds of taxable gross weight or fraction thereof. Section 203(b) of the Act amends section 4481(e) to extend the present expiration date of the highway use tax from July 1, 1972 to October 1, 1972. Section 203(b) also makes conforming amendments to subsections (c) and (d) of section 4481 in view of the new definition of the term "taxable period" which includes within such term the period beginning on July 1, 1972 and ending on September 30, 1972, as provided in new paragraph (4) of section 4482(c) of the Code. The amendments take effect on July 1, 1961.

6156, 6601(c)(2)

Installment payments of highway use tax.—Section 203(c) of this Act provides for the renumbering of section 6156 as 6157 and for the insertion of a new section 6156. Subsection (a) of new section 6156 provides an election for the payment of the highway use tax in equal installments provided the taxpayer filed a return of the tax imposed by section 4481 on or before the date prescribed for the filing of such return. Subsection (b) of new section 6156 provides for specific dates for paying the installments when the election has been made. Subsection (e) of new section 6156 provides that no election is available to any liability for tax incurred in April, May, or June of any year, nor in July, August, or September of 1972. Subsection (c) of new section 6156 provides that, upon election, if additional tax is assessed on a return before the date prescribed for payment of the last installment such additional tax will be so prorated that the portion due with respect to prior installments will be payable upon notice and demand from the Secretary or his delegate and that the portion due with respect to the remaining installments will be payable as a part of the remaining installments. Subsection (d) of new section 6156 provides that in the event the taxpayer fails to pay any installment on or before the due date of such installment, the entire unpaid tax shall be paid upon notice and demand. Section 6601(c)(2), relating to determination of last date prescribed for payment of tax, is amended to conform to the new installment payment provisions. These amendments take effect on July 1, 1961.

4061(a)(1)

Extension of period of 10 percent tax on trucks, buses, and certain tractors.—Section 204 of this Act amends section 4061(a)(1) to provide for an extension of the 10 percent tax rate on trucks, buses, and certain tractors from June 30, 1972 to and including September 30, 1972.

4218(a), 4221(d)(6), 6416(b)(2)(E), 6416(b)(3)

Exemption for gasoline used for nonfuel purposes as material in the manufacture of another article.—Section 205(a) of this Act amends section 4221(d)(6) to provide an exemption from the manufacturers' excise tax for gasoline sold for use by the purchaser, for

nonfuel purposes, as a material in the manufacture or production of another article to be manufactured or produced by him. Section 205(b) amends section 4218(a), relating to use considered sale, to provide that such section does not apply in the case of gasoline used for such purposes. Finally, section 205 provides for credit and refund provisions with respect to gasoline resold for the above purposes (section 6416(b)(2)(E)) or purchased tax paid for such purposes (section 6416(b)(3)(F)). These amendments apply in the case of gasoline sold or used on or after October 1, 1961.

4226(a), 4226(d)

1961 floor stocks taxes on certain tires, inner tubes, and tread rubber.—Section 206(a) of this Act amends section 4226(a) by adding thereto new paragraphs (6) and (7). Paragraph (6) imposes a tax of 2 cents per pound in the case of tires subject to the tax under section 4071(a)(1) and a tax of 1 cent per pound in the case of inner tubes subject to the tax under section 4071(a)(3) which are held for sale or other specified disposition by dealers and certain other persons on July 1, 1961. However, the tax on inner tubes does not apply to inner tubes for bicycle tires as defined in section 4221(e)(4)(B). Paragraph (7) imposes a tax of 2 cents per pound on tread rubber subject to the tax under section 4071(a)(4) which is held by a dealer on July 1, 1961. This tax does not apply to any person if such person shows that all tread rubber held on July 1, 1961, will be used otherwise than in recapping or retreading of tires of the type used on highway vehicles as defined in section 4072(c). Section 206(b) of the Act provides that these taxes shall be paid at such time after September 30, 1961, as may be prescribed by the Secretary or his delegate.

6412(a)(2)
6412(a)(3)

Floor stocks refunds in 1972.—Section 206(c) of this Act provides for conforming amendments to section 6412(a)(2), relating to floor stocks refunds on trucks and buses, tires, tread rubber, and gasoline, including the extension of these provisions to October 1, 1972. Provision is made that such floor stocks refunds shall also apply to inner tubes, and that no credit or refund shall be allowable with respect to inner tubes for bicycle tires as defined in section 4221(e)(4)(B). Section 206(d) of this Act repeals paragraph (3) of section 6412(a), relating to 1961 floor stocks refund on gasoline.

PUBLIC LAW 87-64 (page 315, this Bulletin).

1401

SOCIAL SECURITY AMENDMENTS OF 1961

Increase in tax rate of self-employment tax.—Section 201(a) of this Act amends section 1401 to provide the following rates of self-employment tax: for any taxable year beginning in 1962 the rate is 4.7 percent; for any taxable year beginning in the years 1963 through 1965 the rate is 5.4 percent; for any taxable year beginning in the years 1966 and 1967 the rate is 6.2 percent; and for any taxable year beginning after 1967, the rate is 6.9 percent. The amendment applies with respect to taxable years beginning after December 31, 1961.

3101, 3111

Increase in rates of employee tax and employer tax under the Federal Insurance Contributions Act.—Sections 201 (b) and (c) of the Act amend sections 3101 and 3111, respectively, to provide the following rates of employee tax and employer tax under the Federal Insurance Contributions Act: with respect to wages paid in the calendar year 1962 the rate is 3⅛ percent; with respect to wages paid in the calendar years 1963 through 1965 the rate is 3⅝ percent; with respect to wages paid in the calendar years 1966 and 1967 the rate is 4⅛ percent; and with respect to wages paid after 1967, the rate is 4⅝ percent. The amendments apply with respect to remuneration paid after December 31, 1961.

1402(e)

Election of coverage on behalf of ministers, members of religious orders, and Christian Science practitioners.—Section 202(a) of the Act amends section 1402(e) by adding new paragraph (6) relating to the filing of a waiver certificate, in order to elect social security coverage, in the case of a minister, a member of a religious order, or a Christian Science practitioner who dies after September 12, 1960, and before April 16, 1962, without having filed the waiver certificate. Pursuant to the new paragraph (6), the survivor or the fiduciary of the estate may file the waiver certificate after June 30, 1961, and before April 16, 1962, and the certificate will be effective as if filed by the decedent on the day of his death.

PUBLIC LAW 87–72 (page 317, this Bulletin).

11(b), 821(a)(1)(A), 821(b)(1), 4061, 4251(b)(2), 4261, 5001(a)(1), 5001(a)(3), 5022, 5041(b), 5051(a), 5063, 5701(c)(1), 5707(a), 5707(b), 6412(a)(1)

Extension for one year of the existing corporate normal-tax rate and certain excise tax rates.—Section 2 of this Act extends the corporate normal-tax rate of 30 percent for an additional year to July 1, 1962. Section 3(a) of this Act postpones until July 1, 1962, the excise tax rate reductions on the following taxable articles and services which were to become effective on July 1, 1961: Passenger automobiles, automobile parts and accessories, transportation of persons, cigarettes, beer, wines, distilled spirits, imported perfumes containing distilled spirits, and cordials and liqueurs containing wine. This section of the Act also postpones the termination of the tax on general telephone service from July 1, 1961 to July 1, 1962. Section 3(b) of this Act provides that the floor stocks credits or refunds which would have been applicable to all the taxable articles listed above on hand as of July 1, 1961, except automobile parts and accessories for which no floor stock refund is provided, are postponed for one year.

PUBLIC LAW 87–109 (page 318, this Bulletin).

456

Deferral of prepaid dues income of certain membership organizations.—Section 1 of this Act adds a new section 456 to the Code, providing that a non-stock membership organization, no part of the net income of which is distributable to any member may elect to report pre-

paid dues income in taxable income as the related liability to render services or make available membership privileges is discharged. However, the term of such liability cannot exceed 36 months, and prepaid dues income relating to a liability extending over a longer period is not covered by the section. The election may not be made for a trade or business, the income from which is reported on the cash receipts and disbursements method of accounting. If the liability ends, or the taxpayer ceases to exist, any income received but not yet included in taxable income is reportable at that time. The Act provides a transitional rule designed to spread the Government's loss of revenue caused by an election to apply the section over a period not exceeding 7 years. Taxpayers may elect to apply the section without consent only for the first taxable year beginning after December 31, 1960, in which they receive prepaid dues income. The election may be made at any time with the consent of the Secretary or his delegate.

PUBLIC LAW 87-256 (page 322, this Bulletin).

117(b)(2)(A)

MUTUAL EDUCATIONAL AND CULTURAL EXCHANGE ACT OF 1961

Scholarship and fellowship grants.—Section 110(a) of this Act amends section 117(b)(2)(A) (relating to the conditions for exclusion from gross income of scholarship and fellowship grants in the case of individuals who are not candidates for degrees) so as to include as a recognized grantor of such scholarship or fellowship grants a foreign government, international organization, and a binational or multinational educational and cultural foundation or commission "created or continued pursuant to the Mutual Educational and Cultural Exchange Act of 1961". This amendment applies to taxable years beginning after December 31, 1961.

871

Certain nonresident aliens deemed to be engaged in trade or business.—In general, section 871, prior to this amendment, provided for a minimum tax of 30 percent on income from sources within the United States of nonresident aliens not engaged in trade or business within the United States. Nonresident aliens engaged in trade or business within the United States are taxed at the same rates as citizens. The term "engaged in trade or business" includes the performance of most personal services within the United States. The taxable portion of a scholarship or fellowship received by a nonresident alien is treated as income received while not engaged in a trade or business within the United States. Section 110(b) of this act amends section 871 by adding a new subsection to provide that any nonresident alien who is temporarily present in the United States as a nonimmigrant under subparagraph (F) or (J) of section 101(a)(15) of the Immigration and Nationality Act, as amended, shall be treated as a nonresident alien individual engaged in trade or business within the United States. Thus, those persons falling under the provisions of such subparagraph (F) or (J) (students, trainees, teachers, researchers, etc.) will now be taxed on their United States income at tax rates applicable to citizens rather than the minimum 30 percent rate to which they were generally subject prior to this amendment. This amendment applies to taxable years beginning after December 31, 1961.

872(b)

Exclusion of certain compensation paid to participants in exchange programs.—Section 872(b), prior to this amendment, provided that nonresident aliens shall exclude from gross income (1) earnings derived from the operation of ships documented under the flag of a foreign country, (2) earnings derived from the operation of aircraft registered under the laws of a foreign country if the foreign country granted an equivalent exemption to citizens of the United States. Employees of foreign branches of domestic corporations who come to the United States for training and who continue to receive their salary, even though it is actually paid to their dependents overseas, are deemed to have received gross income for performance of personal services within the United States. In order to overcome this result which has subjected the United States to criticism abroad, section 110(c) of this Act amends section 872(b) by adding a new paragraph (3) which excludes from gross income compensation paid by a "foreign employer" (including foreign branches of a domestic corporation) to a nonresident alien for the period he is temporarily in the United States as a nonimmigrant under subparagraph (F) or (J) of section 101(a)(15) of the Immigration and Nationality Act. This amendment applies to taxable years beginning after December 31, 1961.

1441(a), 1441(b), 1441(c)(4)

Change in nonresident withholding.—Section 1441 provides rules for the withholding of tax on nonresident aliens. Only nonresident aliens who are temporarily present in the United States as nonimmigrants under subparagraph (F) or (J) of section 101(a)(15) of the Immigration and Nationality Act, as amended, are affected by the amendments in this Act. These amendments are necessary to conform the withholding rates to the reduced tax rate now applicable to these nonimmigrants as a result of the amendment to sections 871 and 872 which are also a part of this Act. Section 110(d)(1) and (2) of this Act amends section 1441(a) and (b), respectively, so as to reduce the withholding rate from 30 percent to 18 percent with respect to (1) the taxable portion of any scholarship or fellowship which is received by those nonimmigrants who are not candidates for a degree, and (2) amounts received by such nonimmigrants for travel, research, clerical help, and equipment incident to the scholarship or fellowship grant to which section 117(a)(1) applies, to the extent such amounts are includible in gross income. Section 110(d)(3) of this Act amends section 1441(c)(4) by giving the Secretary or his delegate the power to exempt from withholding under section 1441 compensation for personal services which is received by these nonimmigrants. The effect of this amendment in conjunction with the amendment in section 110(g) of this Act is to relieve those nonimmigrants from the withholding requirements of section 1441 and make them subject to the withholding provisions in chapter 24 (section 3401 et seq). Thus, compensation for personal services will be subject to withholding at a maximum rate of 18 percent rather than 30 percent. These amendments apply with respect to payments made after December 31, 1961.

3121(b), 3306(c)

Services of certain nonresident aliens excluded from coverage under Federal Insurance Contributions Act and Federal Unemployment

Tax Act.—Section 110(e)(1) of this Act amends section 3121(b), relating to the definition of "employment" for purposes of the Federal Insurance Contributions Act, by adding a new paragraph (19), pursuant to which services performed by a nonresident alien while temporarily present in the United States as a nonimmigrant under section 101(a)(15)(F) or (J) of the Immigration and Nationality Act, are excepted from "employment" for purposes of the taxes imposed by the Federal Insurance Contributions Act, if such services are performed to carry out the purpose specified in section 101(a)(15)(F) or (J). Section 110(f) of the Act amends section 3306(c), relating to the definition of "employment" for purposes of the Federal Unemployment Tax Act, by adding a new paragraph (18) which provides a similar exclusion for purposes of the taxes imposed by the Federal Unemployment Tax Act. These amendments apply with respect to service performed after December 31, 1961.

3401(a)(6), 3402(f)

Wages of certain nonresident aliens subject to withholding under section 3402.—Section 110(g)(1) of this Act amends section 3401(a)(6), relating to the definition of "wages" for purposes of income tax withholding under section 3402, by adding a new subparagraph (C), pursuant to which withholding under section 3402 is required in respect of remuneration for employee services paid by an employer, other than a foreign employer, as defined in section 872(b)(3), to a nonresident alien individual temporarily present in the United States as a nonimmigrant under section 101(a)(15)(F) or (J) of the Immigration and Nationality Act, if such remuneration is exempt from withholding under section 1441(a) by reason of section 1441(c)(4)(B). Section 110(g)(2) of the Act amends section 3402(f), relating to withholding exemptions, by adding a new paragraph (6) which provides that a nonresident alien individual, other than one described in section 3401(a)(6)(A) or (B), may claim only one withholding exemption. These amendments apply with respect to wages paid after December 31, 1961.

PUBLIC LAW 87-293 (page 336, this Bulletin).

912

PEACE CORPS ACT

Exclusion for certain allowances.—In general, section 912, prior to this amendment, provided that certain allowances and cost-of-living allowances which are paid to civilian officers and employees of the Government of the United States shall be excluded from gross income and thus exempt from taxation. Section 201(a) of the Act amends section 912 by adding a new paragraph (3) to extend the exclusion to certain allowances received by an individual who is a volunteer or volunteer leader within the meaning of the Peace Corps Act and members of their families. Thus, any amount received as an allowance under section 5 or section 6 of the Act other than (1) termination payments under section 5(c) or section 6(1), (2) leave allowances, (3) if such individual is a volunteer leader training in the United States, allowances to members of his family, or (4) such portion of living allowances as the President may determine under the Act as

constituting basic compensation, shall be excluded from gross income, and shall be exempt from taxation. This amendment applies with respect to taxable years ending after March 1, 1961.

1303(b)

Income from back pay. Section 1303 of the Code limits the tax on income from back pay reported in the current year to the amount of tax that would have been due on the back pay if it had been received and taxed in the years to which it is attributable. Section 201(b) of this Act amends section 1303(b), relating to those items which qualify as back pay, by adding a new paragraph (4) to include termination payments received or accrued on account of services performed in prior taxable years as a volunteer or volunteer leader in the Peace Corps. This amendment applies with respect to taxable years ending after March 1, 1961.

3401(a)

Exclusion of certain payments from "wages" for withholding purposes. Section 201(c) of the Act amends section 3401(a), relating to the definition of "wages" for purposes of income tax withholding under section 3402, by adding a new paragraph (13) excepting from such withholding all payments, other than termination payments made under section 5(c) or 6(1) of the Act, for services performed as a volunteer or volunteer leader within the meaning of the Act. This Amendment applies with respect to remuneration paid after September 22, 1961.

3121(i), 3121(p), 3122, 6051(a)

Social security coverage of Peace Corps volunteers. Section 202(a)(1) of the Act amends section 3121(i) of the Code by adding a new paragraph (3), pursuant to which "wages" subject to the taxes imposed by the Federal Insurance Contributions Act, in the case of a volunteer leader within the meaning of the Peace Corps Act, includes only termination payments made under section 5(c) or 6(1) of the Peace Corps Act, subject to the $4,800 limitation in section 3121(a)(1). Section 202(a)(2) of the Act amends section 3121 to provide that, notwithstanding the provisions of section 3121(b), services performed as a volunteer or volunteer leader within the meaning of the Act shall constitute "employment" for purposes of the taxes imposed by the Federal Insurance Contributions Act. Section 202(a)(3) of the Act amends section 3122 so as to make clear that the head of the Federal agency having control of the Peace Corps services, or agents designated by him, will make the basic determinations as to whether services of volunteers or volunteer leaders constitute "employment" for purposes of the taxes imposed by the Federal Insurance Contributions Act, will make the basic determinations of the amount of their remuneration which constitutes "wages" for such purposes, will make returns and payments of such taxes, and, in determining the amount of such taxes, may disregard the $4,800 limitation in section 3121(a)(1). Section 202(a)(4) of the Act amends section 6051(a), relating to receipts for employees, to provide a special rule requiring that wages for purposes of the Federal Insurance Contributions Act shall, in the case of volunteers and volunteer leaders, be shown on the receipt

furnished any such individual as the amount of termination payments made to him in the calendar year pursuant to section 5(c) or 6(1) of the Peace Corps Act, subject to the $4,800 limitation in section 3121(a)(1). The amendments made by section 202(a) of the Act are applicable with respect to service performed after September 22, 1961, except that, in the case of any volunteer or volunteer leader enrolled pursuant to section 16(a) of the Act, the amendments apply with respect to service performed on or after the effective date of such enrollment.

PUBLIC LAW 87–321 (page 341, this Bulletin).

3302

Credits against the Federal Unemployment Tax for certain successor employers.—Section 3306(b)(1) provides that a successor employer, who acquires substantially all the property used in a trade or business or used in a separate unit of a trade or business of a predecessor employer (within the meaning of the Federal Unemployment Tax Act), and who employs immediately after acquisition an individual who was employed by the predecessor employer immediately prior to acquisition, shall consider the remuneration paid to such individuals by such predecessor during the calendar year of acquisition as remuneration paid by the successor subject to the $3,000-limitation for the purposes of determining wages subject to the tax. This provision is not applicable unless the predecessor qualifies as an employer within the meaning of the Federal Unemployment Tax Act. Section 1(a) of this Act amends section 3302, relating to credits against the Federal Unemployment Tax by adding thereto a new subsection (e) which provides that if a successor employer acquires substantially all the property used in a trade or business of a predecessor who does not qualify as an employer within the meaning of the Federal Unemployment Tax Act, and immediately after the acquisition employs in his trade or business one or more individuals who immediately prior to the acquisition were employed in the trade or business of such predecessor, then for the calendar year in which acquisition takes place such successor employer in addition to the credits allowed under section 3302 (a) and (b) may credit against the tax imposed by section 3301 an amount equal to the credits which would have been allowable to the predecessor had the predecessor qualified as an employer, but limited to credits applicable to remuneration paid to the employee or employees acquired from the predecessor. This amendment applies with respect to calendar year 1961 and each calendar year thereafter.

Election regarding depletion allowance for quartzite and clay used in production of refractory products.—Section 2 of this Act provides that crushing, grinding, and separating out waste are allowable mining processes in the case of quartzite and clay mined and used by the taxpayer in the production of refractory products. It is also provided that the value of each ton of such quartzite and clay used in the production of all refractory products sold by the taxpayer during the taxable year shall be equal to 87½ percent of the lesser of: the average of the lowest published or advertised price of the taxpayer, or the average of the lowest selling price of the taxpayer; at which (during the taxable year) he normally sold or offered for sale such minerals after application of only the processes named above. Under certain

circumstances the taxpayer may refer to recognized selling prices for his marketing area which are published in a trade journal or other industry publication. To have these new provisions apply, the taxpayer must make an election and, if made, the election would be effective on and after January 1, 1951, for all open taxable years beginning before January 1, 1961.

PUBLIC LAW 87-370 (page 344, this Bulletin).

7448

Annuities to widows and dependent children of judges.—Section 1 of this Act adds a new section 7448 which provides a system of annuities for the surviving widows and dependent children of judges of the Tax Court of the United States comparable to the survivorship protection already available to judges of the other Federal Courts. Under section 7448, Tax Court judges may within 6 months after taking office (either after appointment or reappointment), or within 6 months after the date of becoming eligible for retirement under section 7447(b), or within 6 months after October 4, 1961, the date of enactment of section 7448, elect to come under the system. Section 7448 sets up a Tax Court judges survivors annuity fund into which the deposits of the judges electing coverage shall be made and from which the annuities shall be paid. Section 7448 also authorizes the appropriation of funds necessary to carry out its provisions.

403(b)

Annuity contracts purchased for employees of public school systems.—Section 3 of this Act amends section 403(b), relating to taxability of beneficiaries under annuities purchased by section 501(c)(3) organizations. This amendment would extend the benefits of section 403(b) to public school teachers and other employes of public school systems for taxable years beginning after December 31, 1957.

PUBLIC LAW 87-397 (page 348, this Bulletin).

6109, 6676

Identifying numbers.—This Act adds a new section 6109 to the Code authorizing the Secretary or his delegate by regulations to require persons to (1) include in their returns, statements, or other documents their assigned identifying numbers; (2) furnish such numbers to other persons who are required to make returns, statements, or other documents concerning them; and (3) request from, and include in returns, statements, and other documents the assigned identifying numbers of, other persons.

Under a limitation in this Act returns of persons with respect to their liability for tax, and statements or other documents in support of such returns, are not considered as returns, statement, or other documents with respect to other persons. Thus, on Form 1040 the number of the doctor to whom the taxpayer paid a medical expense, and on Form 1120 the number of the newspaper to which the taxpayer paid an advertising expense, are not required. However, the Act also provides an exception to this limitation by requiring that assigned identifying numbers of beneficiaries be included in returns of estates and trusts, and statements or other documents in support of such returns.

Subsection (c) of section 6109 enables the Secretary or his delegate to require the information needed to assign any person his identifying number.

The Act also adds a new section 6676 to the Code. Such section imposes a civil penalty of $5 for each failure to include a number in a return, statement, or other document, or to furnish a number to another person unless the failure is shown to be due to reasonable cause. Assessment and collection of such penalties are excepted from the tax deficiency procedures.

Returns, statements, and other documents, for periods beginning after December 31, 1961, must contain the number of the person making such returns, statements, or other documents. Numbers must be requested of, furnished by, and contained in returns, statements, and other documents made with respect to other persons for periods beginning after December 31, 1962.

MISCELLANEOUS PUBLIC LAWS

PUBLIC LAW 87-24 (C.B. 1961-1, 856).

Provides that certain funds in the Treasury of the United States to the credit of the Nez Perce Tribe shall be divided by crediting 86.5854 percent to the Nez Perce Tribe of Idaho and 13.4146 percent to the Confederated Tribes of the Colville Reservation, to be expended for any purpose authorized by the respective tribal governing bodies and approved by the Secretary of the Interior; and exempts from income tax any part of the funds that may be distributed per capita to the members of the tribes.

PUBLIC LAW 87-205 (page 320, this Bulletin).

Provides that certain funds in the Treasury of the United States to the credit of the Potawatomi Nation of Indians be divided on the basis of 780/2,180ths to the Prairie Band of Potawatomi Indians of Kansas, and 1,400/2,180ths to the Citizen Band of Potawatomi Indians of Oklahoma, to be expended for any purpose authorized by their respective tribal governing bodies and approved by the Secretary of the Interior; and exempts from income tax any part of the funds that may be distributed per capita to the members of the bands.

PUBLIC LAW 87-235 (page 320, this Bulletin).

Authorizes the use of funds, including interest thereon, arising from a judgment awarded by the Indian Claims Commission in favor of the Omaha Indians and exempts from income tax any part of the funds that may be distributed per capita to the members of the Tribe.

PUBLIC LAW 87-262 (page 333, this Bulletin).

Retention of excluded employment status as Federal employees for those who transferred with Freedman's Hospital to Howard University.—Section 2(c) of the Act provides that an individual who was an employee of Freedman's Hospital on September 21, 1961 [date of enactment] and who transfers to Howard University shall during the period of his continuous employment by Howard University be regarded as an employee of the United States, with respect to such employment, for purposes of the Civil Service Retirement Act, the

Federal Employees' Group Life Insurance Act of 1954, and section 3121(b) of the Code.

PUBLIC LAW 87-298 (page 338, this Bulletin).

Provides that certain funds in the Treasury of the United States to the credit of the Colville Tribe, San Poeils-Nespelem Tribe, Okanogan, Tribe, Methow Tribe, and Lake Tribe shall be credited to the Confederated Tribes of the Colville Reservation and exempts from income tax any part of the funds that may be distributed per capita to the members of the Tribes.

PUBLIC LAW 87-312 (page 339, this Bulletin).

Percentage Depletion Base for Certain Clay and Shale.—This Act provides that in the case of a mineowner or operator of a mine who uses brick and tile clay, fire clay or shale that he mined in the manufacture of building or paving brick, drainage and roofing tile, sewer pipe, flower pots, and kindred products, gross income from the property, for depletion purposes, shall be 50 percent of the amount for which the mineowner or operator sells the manufactured products, but not more than $12.50 times the number of tons used in the manufactured products sold during the taxable year. To have the provisions of this Act apply, the taxpayer must make an election and, if made, the election would be effective for all open taxable years beginning before January 1, 1961.

PUBLIC LAW 87-345 (page 343, this Bulletin).

Extension of time within which foreign agricultural workers may be made available under title V of the Agricultural Act of 1949 as amended.—Section 6 of this Act amends section 510 of the Agricultural Act of 1949 to extend through December 31, 1963, the time within which foreign agricultural workers whose services are excepted from "employment" under section 3121(b)(1)(A) may be made available for agricultural services in the United States. The effect of this extension of time is to "give meaning" to section 3121(b)(1)(A) for an additional two years.

PUBLIC LAW 87-29
EIGHTY-SEVENTH CONGRESS, MAY 4, 1961
H.R. 5189 [1]

An Act to amend the Internal Revenue Code of 1954 to exempt from tax income derived by a foreign central bank of issue from obligations of the United States, 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) subpart C of part II of subchapter N of chapter 1 of the Internal Revenue Code of 1954 (relating to nonresident aliens and foreign corporations) is amended by adding at the end thereof the following new section:

SEC. 895. INCOME DERIVED BY A FOREIGN CENTRAL BANK OF ISSUE FROM OBLIGATIONS OF THE UNITED STATES.

Income derived by a foreign central bank of issue from obligations of the United States owned by such foreign central bank of issue shall not be included

[1] Senate Report No. 163, page 351, this Bulletin; since House Report No. 58 is substantially the same as the Senate Report, it is not published herein.

in gross income and shall be exempt from taxation under this subtitle unless such obligations are held for, or used in connection with, the conduct of commercial banking functions or other commercial activities.

(b) The table of sections for such subpart C is amended by adding at the end thereof the following:

Sec. 895. Income derived by a foreign central bank of issue from obligations of the United States.

(c) The amendments made by subsections (a) and (b) shall be effective with respect to income received in taxable years beginning after December 31, 1960.

SEC. 2. Section 1372 of the Internal Revenue Code of 1954 (relating to elections by small business corporations) is amended by adding at the end thereof the following new subsection:

(g) CONSENT TO ELECTION BY CERTAIN SHAREHOLDERS OF STOCK HELD AS COMMUNITY PROPERTY.—If a husband and wife owned stock which was community property (or the income from which was community income) under the applicable community property law of a State, and if either spouse filed a timely consent to an election under subsection (a) for a taxable year beginning before January 1, 1961, the time for filing the consent of the other spouse to such election shall not expire prior to May 15, 1961.

PUBLIC LAW 87-59
EIGHTY-SEVENTH CONGRESS, JUNE 27, 1961
H.R. 1877 [2]

An Act relating to the effective date of the qualification of Plumbers Union Local Numbered 12 Pension Fund as a qualified trust under section 401(a) of the Internal Revenue Code of 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 Plumbers Union Local Numbered 12 Pension Fund, which was established by a collective bargaining agreement effective September 1, 1954, and which has been held by the Internal Revenue Service to constitute a qualified trust under section 401(a) of the Internal Revenue Code of 1954, and to be exempt from taxation under section 501(a) of said Code, for years ending on or after June 3, 1959, shall be held and considered to have been a qualified trust under said section 401(a), and to have been exempt from taxation under said section 501(a), for the period beginning on September 1, 1954, and ending on June 3, 1959, but only if it is shown to the satisfaction of the Secretary of the Treasury or his delegate that the trust has not in this period been operated in a manner which would jeopardize the interests of its beneficiaries.

SEC. 2. (a) Section 809(d)(11) of the Internal Revenue Code of 1954 (relating to deductions in computing gain from operations in the case of certain mutualization distributions) is amended by striking out "in 1958 and 1959" and inserting in lieu thereof "in 1958, 1959, 1960, and 1961."

(b) Section 809(g)(3) of such Code (relating to application of section 815 to certain mutualization distributions) is amended by striking

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[2] Senate Report No. 280, page 353, this Bulletin; House Report No. 344 is not published herein.

out "in 1959" and inserting in lieu thereof "in 1959, 1960, or 1961."

(c) The amendments made by subsections (a) and (b) shall apply to taxable years beginning after December 31, 1959.

SEC. 3. (a) Paragraph 1102(b) of the Tariff Act of 1930, as amended (19 U.S.C. 1001; par. 1102), is amended by striking out "Cashmere goat," and by inserting after "other like animals" the following: "(including hair of animals like the Cashmere goat)."

(b) Paragraph 1102 of such Act is further amended by adding at the end thereof the following new subparagraph:

(c) Hair of the Cashmere goat, in the grease or washed, 18 cents per pound of clean content; scoured, 21 cents per pound of clean content; on the skin, 16 cents per pound of clean content; sorted, or matchings, if not scoured, 19 cents per pound of clean content.

(c) The amendments made by this section shall apply to articles entered, or withdrawn from warehouse, for consumption, on or after the date of enactment of this Act, and to articles covered by entries or withdrawals which have not been liquidated or the liquidation of which has not become final on such date of enactment.

SEC. 4. The pension fund of the slate, tile, and roofing industry in New York City, which was created as a result of an agreement between the Composition Roofers, Damp and Waterproof Workers Association, Local Union Numbered 8, and several employer associations and other individual employers in the industry, and which has been held by the Internal Revenue Service to constitute a qualified trust under section 401(a) of the Internal Revenue Code of 1954, and to be exempt from taxation under section 501(a) of such Code, shall be held and considered to have been a qualified trust under such section 401(a) and to be exempt from taxation under such section 501(a), for the period beginning July 1, 1957, and ending November 24, 1958, but only if it is shown to the satisfaction of the Secretary of the Treasury or his delegate that the trust has not in this period been operated in a manner which would jeopardize the interest of its beneficiaries.

Approved June 27, 1961.

PUBLIC LAW 87-61
EIGHTY-SEVENTH CONGRESS, JUNE 29, 1961
H.R. 6713 [3]

An act to amend certain laws relating to Federal-aid highways, to make certain adjustments in the Federal-aid highway program, and for other purposes.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,

TITLE I—FEDERAL-AID HIGHWAY PROGRAM

SEC. 101. SHORT TITLE.

This Act may be cited as the "Federal-Aid Highway Act of 1961".

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[3] This publication of the law is restricted to excerpts involving internal revenue matters; House Report No. 326, page 355, this Bulletin; Senate Report No. 367, page 363, this Bulletin; Conference Report No. 564, page 377, this Bulletin.

TITLE II—INTERNAL REVENUE CODE AND HIGHWAY TRUST FUND AMENDMENTS

SEC. 201. CONTINUATION OF MOTOR FUEL TAX RATES.

(a) DIESEL FUEL AND SPECIAL MOTOR FUELS.—Subsections (a) and (b) of section 4041 of the Internal Revenue Code of 1954 (relating to taxes on diesel fuel and special motor fuels) are each amended—

(1) by striking out "3 cents a gallon" and inserting in lieu thereof "4 cents a gallon" and

(2) by striking out "1 cent a gallon" and inserting in lieu thereof "2 cents a gallon".

(b) GASOLINE.—Section 4081(a) of such Code (relating to tax on gasoline) is amended by striking out "3 cents a gallon" and inserting in lieu thereof "4 cents a gallon".

(c) RATE REDUCTION IN 1972.—Sections 4041(c) and 4081(b) of such Code (providing a reduction to a 1½-cent a gallon rate on July 1, 1972) are each amended by striking out "July 1, 1972" and inserting in lieu thereof "October 1, 1972".

(d) REPEAL OF TEMPORARY PROVISIONS.—Sections 4041(f) and 4081(c) of such Code (relating to rates of tax for the period beginning October 1, 1959, and ending June 30, 1961) are hereby repealed.

(e) CONFORMING AMENDMENT.—Section 6421(h) of such Code (relating to nonhighway or local transit use of gasoline) is amended by striking out "July 1, 1972" and inserting in lieu thereof "October 1, 1972".

SEC. 202. INCREASE IN TAXES ON CERTAIN TIRES, TUBES, AND TREAD RUBBER.

(a) TIRES.—Paragraph (1) of section 4071(a) of the Internal Revenue Code of 1954 (relating to tax on tires used on highway vehicles) is amended by striking out "8 cents a pound" and inserting in lieu thereof "10 cents a pound".

(b) INNER TUBES.—Paragraph (3) of section 4071(a) of such Code (relating to tax on inner tubes for tires) is amended by striking out "9 cents a pound" and inserting in lieu thereof "10 cents a pound".

(c) TREAD RUBBER.—Paragraph (4) of section 4071(a) of such Code (relating to tax on tread rubber) is amended by striking out "3 cents a pound" and inserting in lieu thereof "5 cents a pound".

(d) RATE REDUCTION IN 1972.—Subsection (c) of section 4071 of such Code (relating to rate reduction on July 1, 1972) is amended to read as follows:

"(c) RATE REDUCTION.—On and after October 1, 1972—

(1) the tax imposed by paragraph (1) of subsection (a) shall be 5 cents a pound;

(2) the tax imposed by paragraph (3) of subsection (a) shall be 9 cents a pound; and

(3) paragraph (4) of subsection (a) shall not apply.

SEC. 203. TAX ON USE OF CERTAIN VEHICLES.

(a) INCREASE IN TAX.—Subsection (a) of section 4481 of the Internal Revenue Code of 1954 (relating to tax on use of certain vehicles) is amended by striking out "$1.50 a year" and inserting in lieu thereof "$3.00 a year".

(b) PERIOD TAX IN EFFECT.—

(1) EXTENSION FOR 3 MONTHS.—Section 4481(e) of such Code (relating to period tax in effect) is amended by striking out "after

June 30, 1956, and before July 1, 1972" and inserting in lieu thereof "before October 1, 1972".

(2) CONFORMING AMENDMENTS.—

(A) Section 4481(a) of such Code (relating to imposition of tax) is amended by adding at the end thereof the following new sentence: "In the case of the taxable period beginning on July 1, 1972, and ending on September 30, 1972, the tax shall be at the rate of 75 cents for such period for each 1,000 pounds of taxable gross weight or fraction thereof."

(B) Subsections (c) and (d) of section 4481 of such Code are amended to read as follows:

(c) PRORATION OF TAX.—If in any taxable period the first use of the highway motor vehicle is after the first month in such period, the tax shall be reckoned proportionately from the first day of the month in which such use occurs to and including the last day in such taxable period.

(d) ONE TAX LIABILITY PER PERIOD.—

(1) IN GENERAL.—To the extent that the tax imposed by this section is paid with respect to any highway motor vehicle for any taxable period, no further tax shall be imposed by this section for such taxable period with respect to such vehicle.

(2) CROSS REFERENCE.—For privilege of paying tax imposed by this section in installments, see section 6156.

(C) Subsection (c) of section 4482 of such Code is amended by adding at the end thereof the following new paragraph:

(4) TAXABLE PERIOD.—The term "taxable period" means any year beginning before July 1, 1972, and the period which begins on July 1, 1972, and ends at the close of September 30, 1972.

(c) INSTALLMENT PAYMENTS OF TAX.—

(1) Subchapter A of chapter 62 of such Code (relating to time and place for paying tax) is amended by renumbering section 6156 as 6157, and by inserting after section 6155 the following new section:

SEC. 6156. INSTALLMENT PAYMENTS OF TAX ON USE OF HIGHWAY MOTOR VEHICLES.

(a) PRIVILEGE TO PAY TAX IN INSTALLMENTS.—If the taxpayer files a return of the tax imposed by section 4481 on or before the date prescribed for the filing of such return, he may elect to pay the tax shown on such return in equal installments in accordance with the following table:

If liability is incurred in—	*The number of installments shall be—*
July, August, or September	4
October, November, or December	3
January, February, or March	2

(b) DATES FOR PAYING INSTALLMENTS.—In the case of any tax payable in installments by reason of an election under subsection (a)—

(1) the first installment shall be paid on the date prescribed for payment of the tax,

(2) the second installment shall be paid on or before the last day of the third month following the calendar quarter in which the liability was incurred,

(3) the third installment (if any) shall be paid on or before the last day of the sixth month following the calendar quarter in which the liability was incurred, and

(4) the fourth installment (if any) shall be paid on or before the last day of the ninth month following the calendar quarter in which the liability was incurred.

(c) PRORATION OF ADDITIONAL TAX TO INSTALLMENTS.—If an election has been made under subsection (a) in respect of tax reported on a return filed by the taxpayer and tax required to be shown but not shown on such return is assessed before the date prescribed for payment of the last installment, the additional tax shall be prorated equally to the installments for which the election was made. That part of the additional tax so prorated to any installment the date for payment of which has not arrived shall be collected at the same time as and as part of such installment. That part of the additional tax so prorated to any installment the date for payment of which has arrived shall be paid upon notice and demand from the Secretary or his delegate.

(d) ACCELERATION OF PAYMENTS.—If the taxpayer does not pay any installment under this section on or before the date prescribed for its payment, the whole of the unpaid tax shall be paid upon notice and demand from the Secretary or his delegate.

(e) SECTION INAPPLICABLE TO CERTAIN LIABILITIES.—This section shall not apply to any liability for tax incurred in—

(1) April, May, or June of any year, or

(2) July, August, or September of 1972.

(2) Section 6601(c)(2) of such Code (relating to determination of last date prescribed for payment of tax) is amended by striking out "6152(a)" and inserting in lieu thereof "6152(a) or 6156(a)", and by striking out "6152(b)" and inserting in lieu thereof "6152(b) or 6156(b), as the case may be".

(3) The table of sections for subchapter A of chapter 62 of such Code is amended by striking out

Sec. 6156. Payment of taxes under provisions of the Tariff Act.

and inserting in lieu thereof

Sec. 6156. Installment payments of tax on use of highway motor vehicles.
Sec. 6157. Payment of taxes under provisions of the Tariff Act.

SEC. 204. EXTENSION OF PERIOD OF 10 PERCENT TAX ON TRUCKS AND BUSES.

Section 4061(a)(1) of the Internal Revenue Code of 1954 (relating to tax on trucks and buses) is amended by striking out "July 1, 1972" and inserting in lieu thereof "October 1, 1972".

SEC. 205. CERTAIN GASOLINE SOLD FOR FURTHER MANUFACTURE.

(a) EXEMPTION FROM TAX.—Section 4221(d)(6) of the Internal Revenue Code of 1954 (relating to use in further manufacture) is amended—

(1) by striking "or" at the end of subparagraph (A),

(2) by striking the period at the end of subparagraph (B) and inserting in lieu thereof "; or", and

(3) by adding at the end thereof the following new subparagraph:

(C) in the case of gasoline taxable under section 4081, such gasoline is sold for use by the purchaser, for nonfuel purposes, as a material in the manufacture or production of another article to be manufactured or produced by him.

(b) USE BY MANUFACTURER OR IMPORTER CONSIDERED SALE.—Section 4218(a) of such Code (relating to use considered as sale) is amended by adding at the end thereof the following new sentence: "This subsection shall not apply in the case of gasoline used by any person, for nonfuel purposes, as a material in the manufacture or production of another article to be manufactured or produced by him."

(c) CREDIT OR REFUND.—Section 6416(b)(3) of such Code (relating to tax paid articles used for further manufacture) is amended—

(1) by striking out "or" at the end of subparagraph (D),

(2) by striking out the period at the end of subparagraph (E) and inserting in lieu thereof "; or", and

(3) by inserting after subparagraph (E) the following new subparagraph:

"(F) in the case of gasoline taxable under section 4081, such gasoline is used by the second manufacturer or producer, for nonfuel purposes, as a material in the manufacture or production of any other article manufactured or produced by him.

(d) CONFORMING AMENDMENT.—Section 6416(b)(2)(E) of such Code is amended by striking out "or (E)" and inserting in lieu thereof "(E), or (F)".

SEC. 206. FLOOR STOCKS TAXES AND REFUNDS.

(a) IMPOSITION ON CERTAIN TIRES, TUBES, AND TREAD RUBBER.—Subsection (a) of section 4226 of the Internal Revenue Code of 1954 (relating to floor stocks taxes) is amended by adding at the end thereof the following new paragraphs:

"(6) 1961 TAXES ON CERTAIN TIRES AND INNER TUBES.—On tires subject to tax under section 4071(a)(1), and on inner tubes subject to tax under section 4071(a)(3), which, on July 1, 1961, are held—

"(A) by a dealer for sale,

"(B) for sale on, or in connection with, other articles held by the manufacturer, producer, or importer of such other articles, or

"(C) for use in the manufacture or production of other articles.

there is hereby imposed a floor stocks tax at the rate of 2 cents a pound in the case of such tires, and a floor stocks tax at the rate of 1 cent a pound in the case of such inner tubes. The taxes imposed by this paragraph shall not apply to any tire or inner tube which is held for sale by the manufacturer, producer, or importer of such tire or tube, or which will be subject under section 4218(b) or 4219 to the manufacturers excise tax on tires or inner tubes. The tax on inner tubes imposed by this paragraph shall not apply to inner tubes for bicycle tires (as defined in section 4221(e)(4)(B)).

"(7) 1961 TAX ON TREAD RUBBER.—On tread rubber subject to tax under section 4071(a)(4) which, on July 1, 1961, is held by a dealer, there is hereby imposed a floor stocks tax at the rate of 2 cents a pound. The tax imposed by this paragraph shall not apply in the case of any person if such person establishes, to the satisfaction of the Secretary or his delegate, that all tread rubber held by him on July 1, 1961, will be used otherwise than in the recapping or retreading of tires of the type used on highway vehicles (as defined in section 4072(c)).

(b) DUE DATE OF TAXES.—Subsection (d) of section 4226 of such Code is amended by striking out the period at the end thereof and inserting in lieu thereof a comma and "and except that the taxes imposed by paragraphs (6) and (7) shall be paid at such time after September 30, 1961, as may be prescribed by the Secretary or his delegate."

(c) FLOOR STOCKS REFUNDS IN 1972.—Paragraph (2) of section 6412(a) of such Code (relating to floor stocks refunds on trucks and buses, tires, tread rubber, and gasoline) is amended—

(1) by inserting "TUBES," after "TIRES," in the heading;

(2) by striking out "4071(a) (1) or (4)," and inserting in lieu thereof "4071(a) (1), (3), or (4),";

(3) by striking out "July 1, 1972" each place it appears and inserting in lieu thereof "October 1, 1972";

(4) by striking out "November 10, 1972" each place it appears and inserting in lieu thereof "February 10, 1973";

(5) by striking out "October 1, 1972" and inserting in lieu thereof "January 1, 1973"; and

(6) by adding at the end thereof the following new sentence: "No credit or refund shall be allowable under this paragraph with respect to inner tubes for bicycle tires (as defined in section 4221(e)(4)(B))."

(d) REPEAL OF 1961 FLOOR STOCKS REFUND ON GASOLINE.—Paragraph (3) of section 6412(a) (relating to 1961 floor stocks refund on gasoline) is hereby repealed.

SEC. 207. HIGHWAY TRUST FUND.

(a) TRANSFER OF AMOUNTS EQUIVALENT TO TAX ON TRUCKS, BUSES, ETC.—Subparagraph (C) of section 209(c)(1) of the Highway Revenue Act of 1956 (relating to transfer to Highway Trust Fund of amounts equivalent to certain taxes) is amended to read as follows:

> (C) 50 percent of the tax received after June 30, 1957, and before July 1, 1962, under section 4061(a)(1) (tax on trucks, buses, etc.), and 100 percent of the tax received after June 30, 1962, under section 4061(a)(1);.

(b) REPEAL OF TRANSFER TO TRUST FUND OF EXCISE TAXES ON AUTOMOBILES, PARTS AND ACCESSORIES, ETC.—Paragraph (2) of section 209(c) of such Act (providing for the transfer to the Highway Trust Fund of amounts equivalent to a portion of the excise taxes on automobiles and parts and accessories received after June 30, 1961, and before July 1, 1964) is hereby repealed.

(c) RECEIPTS IN FISCAL YEAR 1973.—

(1) Paragraph (1) of section 209(c) of such Act (relating to transfer to Trust Fund of amounts equivalent to certain taxes) is amended by striking out "July 1, 1972" and inserting in lieu thereof "October 1, 1972".

(2) Paragraph (3) of such section 209(c) is amended—

(A) by striking out "JULY 1, 1972" in the heading and inserting in lieu thereof "OCTOBER 1, 1972";

(B) by striking out "after June 30, 1972, and before July 1, 1973, and which are attributable to liability for tax incurred before July 1, 1972," and inserting in lieu thereof "after September 30, 1972, and before July 1, 1973, and which are attributable to liability for tax incurred before October 1, 1972,";

(C) by striking out subparagraph (C) and inserting in lieu thereof the following:

(C) 50 percent of the tax under section 4071(a)(1) (tax on tires of the type used on highway vehicles) and 10 percent of the tax under section 4071(a)(3) (tax on inner tubes for tires); and".

(d) EXPENDITURES IN FISCAL YEAR 1973.—

(1) Paragraph (1) of section 209(f) of such Act (relating to expenditures from Trust Fund for Federal-aid highway program) is amended by striking out "July 1, 1972" and inserting in lieu thereof "October 1, 1972".

(2) Paragraph (3) of such section 209(f) relating to transfers from Trust Fund for gasoline used on farms and for certain other purposes) is amended by striking out "July 1, 1972" and inserting in lieu thereof "October 1, 1972".

(3) Subparagraphs (B) and (C) of section 209(f)(4) of such Act are amended to read as follows:

(B) 100 percent of the refunds in respect of articles subject to tax under section 4071(a) (1), (3), or (4) of such Code (certain tires, tubes, and tread rubber); and

(C) 80 percent of the refunds in respect of gasoline subject to tax under section 4081 of such Code.

(4) Paragraph (5) of such section 209(f) (relating to 1961 floor stocks refunds on gasoline) is hereby repealed.

SEC. 208. EFFECTIVE DATES.

(a) Except as provided in subsection (b), the amendments made by this title shall take effect on the date of the enactment of this Act.

(b)(1) The amendments made by sections 201, 202, and 203 shall take effect on July 1, 1961.

(2) The amendments made by section 205 (a), (c), and (d) shall apply only in the case of gasoline sold on or after October 1, 1961.

(3) The amendment made by section 205(b) shall apply only in the case of gasoline used on or after October 1, 1961.

Approved June 29, 1961.

PUBLIC LAW 87-64
EIGHTY-SEVENTH CONGRESS, JUNE 30, 1961
H.R. 6027 [4]

An Act to improve benefits under the old-age, survivors, and disability insurance program by increasing the minimum benefits and aged widow's benefits and by making additional persons eligible for benefits under the program, and for other 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 "Social Security Amendments of 1961".

* * * * * * *

TITLE II—AMENDMENTS TO THE INTERNAL REVENUE CODE OF 1954

CHANGES IN TAX SCHEDULES

SELF-EMPLOYMENT INCOME TAX

SEC. 201. (a) Section 1401 of the Internal Revenue Code of 1954 (relating to rate of tax on self-employment income) is amended to read as follows:

SEC. 1401. RATE OF TAX.

In addition to other taxes, there shall be imposed for each taxable year, on the self-employment income of every individual, a tax as follows:

(1) in the case of any taxable year beginning after December 31, 1961, and before January 1, 1963, the tax shall be equal to 4.7 percent of the amount of the self-employment income for such taxable year;

(2) in the case of any taxable year beginning after December 31, 1962, and before January 1, 1966, the tax shall be equal to 5.4 percent of the amount of the self-employment income for such taxable year;

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[4] This publication is restricted to excerpts involving internal revenue matters; Senate Report No. 425, page 379, this Bulletin; Conference Report No. 611, page 383, this Bulletin; House Report No. 216 is not published herein.

(3) in the case of any taxable year beginning after December 31, 1965, and before January 1, 1968, the tax shall be equal to 6.2 percent of the amount of the self-employment income for such taxable year; and

(4) in the case of any taxable year beginning after December 31, 1967, the tax shall be equal to 6.9 percent of the amount of the self-employment income for such taxable year.

TAX ON EMPLOYEES

(b) Section 3101 of such Code (relating to rate of tax on employees under the Federal Insurance Contributions Act) is amended to read as follows:

SEC. 3101. RATE OF TAX.

In addition to other taxes, there is hereby imposed on the income of every individual a tax equal to the following percentages of the wages (as defined in section 3121(a)) received by him with respect to employment (as defined in section 3121(b))—

(1) with respect to wages received during the calendar year 1962, the rate shall be 3⅛ percent;

(2) with respect to wages received during the calendar years 1963 to 1965, both inclusive, the rate shall be 3⅝ percent;

(3) with respect to wages received during the calendar years 1966 to 1967, both inclusive, the rate shall be 4⅛ percent; and

(4) with respect to wages received after December 31, 1967, the rate shall be 4⅝ percent.

TAX ON EMPLOYERS

(c) Section 3111 of such Code (relating to rate of tax on employers under the Federal Insurance Contributions Act) is amended to read as follows:

SEC. 3111. RATE OF TAX.

In addition to other taxes, there is hereby imposed on every employer an excise tax, with respect to having individuals in his employ, equal to the following percentages of the wages (as defined in section 3121(a)) paid by him with respect to employment (as defined in section 3121(b))—

(1) with respect to wages paid during the calendar year 1962, the rate shall be 3⅛ percent;

(2) with respect to wages paid during the calendar years 1963 to 1965, both inclusive, the rate shall be 3⅝ percent;

(3) with respect to wages paid during the calendar years 1966 to 1967, both inclusive, the rate shall be 4⅛ percent; and

(4) with respect to wages paid after December 31, 1967, the rate shall be 4⅝ percent.

EFFECTIVE DATES

(d) The amendment made by subsection (a) shall apply with respect to taxable years beginning after December 31, 1961. The amendments made by subsections (b) and (c) shall apply with respect to remuneration paid after December 31, 1961.

EXTENSION OF TIME TO ELECT COVERAGE ON BEHALF OF MINISTERS

SEC. 202. (a) Section 1402(e) of the Internal Revenue Code of 1954 is amended by adding at the end thereof the following new paragraph:

(6) CERTIFICATE FILED BY FIDUCIARIES OR SURVIVORS ON OR BEFORE APRIL 15, 1962.—In any case where an individual, whose death has occurred after September 12, 1960, and before April 16, 1962, derived earnings from the performance of services described in subsection (c)(4), or in subsection (c)(5) insofar as it relates to the performance of service by an individual in the exercise of his profession as a Christian Science practitioner, a certificate may be filed after the date of enactment of this paragraph, and

on or before April 15, 1962, by a fiduciary acting for such individual's estate or by such individual's survivor within the meaning of section 205(c)(1)(C) of the Social Security Act. Such certificate shall be effective for the period prescribed in paragraph (3)(A) as if filed by the individual on the day of his death.

(b) The amendment made by subsection (a) shall take effect on the date of enactment of this Act; except that no monthly benefits under title II of the Social Security Act for the month in which this Act is enacted or any prior month shall be payable or increased by reason of such amendment, and no lump-sum death payment under such title shall be payable or increased by reason of such amendment in the case of any individual who died prior to the date of enactment of this Act.

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Approved June 30, 1961, 10:45 a.m.

PUBLIC LAW 87-72
EIGHTY-SEVENTH CONGRESS, JUNE 30, 1961
H.R. 7446 [5]

An Act to provide a one-year extension of the existing corporate normal-tax rate and of certain excise-tax rates.

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 "Tax Rate Extension Act of 1961".

SEC. 2. ONE-YEAR EXTENSION OF CORPORATE NORMAL-TAX RATE.

Section 11(b) (relating to corporate normal tax), section 821(a)(1)(A) (relating to mutual insurance companies other than interinsurers), and section 821(b)(1) (relating to interinsurers) of the Internal Revenue Code of 1954 are amended as follows:

(1) By striking out "July 1, 1961" each place it appears and inserting in lieu thereof "July 1, 1962";

(2) By striking out "July 1, 1961" each place it appears and inserting in lieu thereof "July 1, 1962";

(3) By striking out "June 30, 1961" each place it appears and inserting in lieu thereof "June 30, 1962";

(4) By striking out "June 30, 1961" each place it appears and inserting in lieu thereof "June 30, 1962".

SEC. 3. ONE-YEAR EXTENSION OF CERTAIN EXCISE-TAX RATES.

(a) EXTENSION OF RATES.—The following provisions of the Internal Revenue Code of 1954 are amended by striking out "July 1, 1961" each place it appears and inserting in lieu thereof "July 1, 1962"—

(1) section 4061 (relating to motor vehicles);

(2) section 4251(b)(2) (relating to termination of tax on general telephone service);

(3) section 4261 (relating to tax on transportation of persons);

(4) section 5001(a)(1) (relating to distilled spirits);

(5) section 5001(a)(3) (relating to imported perfumes containing distilled spirits);

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[5] House Report No. 450, page 384, this Bulletin; since Senate Report No. 371 is substantially the same as the House report, it is not published herein.

(6) section 5022 (relating to cordials and liqueurs containing wine);

(7) section 5041(b) (relating to wines);

(8) section 5051(a) (relating to beer); and

(9) section 5701(c)(1) (relating to cigarettes).

(b) TECHNICAL AMENDMENTS.—The following provisions of the Internal Revenue Code of 1954 are amended as follows:

(1) Section 5063 (relating to floor stocks refunds on distilled spirits, wines, cordials, and beer) is amended by striking out "July 1, 1961" each place it appears and inserting in lieu thereof "July 1, 1962", and by striking out "October 1, 1961" and inserting in lieu thereof "October 1, 1962".

(2) Subsections (a) and (b) of section 5707 (relating to floor stocks refunds on cigarettes) are amended by striking out "July 1, 1961" each place it appears and inserting in lieu thereof "July 1, 1962", and by striking out "October 1, 1961" and inserting in lieu thereof "October 1, 1962".

(3) Section 6412(a)(1) (relating to floor stocks refunds on automobiles) is amended by striking out "July 1, 1961" each place it appears and inserting in lieu thereof "July 1, 1962", by striking out "October 1, 1961" and inserting in lieu thereof "October 1, 1962", and by striking out "November 10, 1961" each place it appears and inserting in lieu thereof "November 10, 1962".

Section 497 of the Revenue Act of 1951 (relating to refunds on articles from foreign trade zones) as amended, is amended by striking out "July 1, 1961" each place it appears and inserting in lieu thereof "July 1, 1962".

Approved June 30, 1961.

PUBLIC LAW 87-109
EIGHTY-SEVENTH CONGRESS, JULY 26, 1961
H.R. 929 [6]

An Act to amend the Internal Revenue Code of 1954 to permit the prepaid dues income of certain membership organizations to be included in gross income for the taxable years to which the dues relate.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That (a) subpart B of part II of subchapter E of chapter 1 of the Internal Revenue Code of 1954 (relating to taxable years for which items of gross income are included) is amended by adding at the end thereof the following new section:

SEC. 456. PREPAID DUES INCOME OF CERTAIN MEMBERSHIP ORGANIZATIONS.

(a) YEAR IN WHICH INCLUDED.—Prepaid dues income to which this section applies shall be included in gross income for the taxable years during which the liability described in subsection (e)(2) exists.

(b) WHERE TAXPAYER'S LIABILITY CEASES.—In the case of any prepaid dues income to which this section applies—

(1) If the liability described in subsection (e)(2) ends, then so much of such income as was not includible in gross income under subsection (a) for

[6] House Report No. 381, page 390, this Bulletin; since Senate Report 543 is substantially the same as the House Report, it is not published herein.

preceding taxable years shall be included in gross income for the taxable year in which the liability ends.

(2) If the taxpayer ceases to exist, then so much of such income as was not includible in gross income under subsection (a) for preceding taxable years shall be included in gross income for the taxable year in which such cessation of existence occurs.

(c) PREPAID DUES INCOME TO WHICH THIS SECTION APPLIES.—

(1) ELECTION OF BENEFITS.—This section shall apply to prepaid dues income if and only if the taxpayer makes an election under this section with respect to the trade or business in connection with which such income is received. The election shall be made in such manner as the Secretary or his delegate may by regulations prescribe. No election may be made with respect to a trade or business if in computing taxable income the cash receipts and disbursements method of accounting is used with respect to such trade or business.

(2) SCOPE OF ELECTION.—An election made under this section shall apply to all prepaid dues income received in connection with the trade or business with respect to which the taxpayer has made the election; except that the taxpayer may, to the extent permitted under regulations prescribed by the Secretary or his delegate, include in gross income for the taxable year of receipt the entire amount of any prepaid dues income if the liability from which it arose is to end within 12 months after the date of receipt. Except as provided in subsection (d), an election made under this section shall not apply to any prepaid dues income received before the first taxable year for which the election is made.

(3) WHEN ELECTION MAY BE MADE.—

(A) WITH CONSENT.—A taxpayer may, with the consent of the Secretary or his delegate, make an election under this section at any time.

(B) WITHOUT CONSENT.—A taxpayer may, without the consent of the Secretary or his delegate, make an election under this section for its first taxable year (i) which begins after December 31, 1960, and (ii) in which it receives prepaid dues income in the trade or business. Such election shall be made not later than the time prescribed by law for filing the return for the taxable year (including extensions thereof) with respect to which such election is made.

(4) PERIOD TO WHICH ELECTION APPLIES.—An election under this section shall be effective for the taxable year with respect to which it is first made and for all subsequent taxable years, unless the taxpayer secures the consent of the Secretary or his delegate to the revocation of such election. For purposes of this title, the computation of taxable income under an election made under this section shall be treated as a method of accounting.

(d) TRANSITIONAL RULE.—

(1) AMOUNT INCLUDIBLE IN GROSS INCOME FOR ELECTION YEARS.—If a taxpayer makes an election under this section with respect to prepaid dues income, such taxpayers shall include in gross income, for each taxable year to which such election applies, not only that portion of prepaid dues income received in such year otherwise includible in gross income for such year under this section, but shall also include in gross income for such year an additional amount equal to the amount of prepaid dues income received in the 3 taxable years preceding the first taxable year to which such election applies which would have been included in gross income in the taxable year had the election been effective 3 years earlier.

(2) DEDUCTIONS OF AMOUNTS INCLUDED IN INCOME MORE THAN ONCE.—A taxpayer who makes an election with respect to prepaid dues income, and who includes in gross income for any taxable year to which the election applies an additional amount computed under paragraph (1), shall be permitted to deduct, for such taxable year and for each of the 4 succeeding taxable years, an amount equal to one-fifth of such additional amount, but only to the extent that such additional amount was also included in the taxpayer's gross income during any of the 3 taxable years preceding the first taxable year to which such election applies.

(e) DEFINITIONS.—For purposes of this section—

(1) PREPAID DUES INCOME.—The term "prepaid dues income" means any amount (includible in gross income) which is received by a membership organization in connection with, and is directly attributable to, a liability to render services or make available membership privileges over a period of

time which extends beyond the close of the taxable year in which such amount is received.

(2) LIABILITY.—The term "liability" means a liability to render services or make available membership privileges over a period of time which does not exceed 36 months, which liability shall be deemed to exist ratably over the period of time that such services are required to be rendered, or that such membership privileges are required to be made available.

(3) MEMBERSHIP ORGANIZATION.—The term "membership organization" means a corporation, association, federation, or other organization—

(A) organized without capital stock of any kind, and

(B) no part of the net earnings of which is distributable to any member.

(4) RECEIPT OF PREPAID DUES INCOME.—Prepaid dues income shall be treated as received during the taxable year for which it is includible in gross income under section 451 (without regard to this section).

(b) The table of sections for such subpart B is amended by adding at the end thereof the following:

Sec. 456. Prepaid dues income of certain membership organizations.

SEC. 2. The amendments made by this Act shall apply with respect to taxable years beginning after December 31, 1960.

Approved July 26, 1961.

PUBLIC LAW 87-205
EIGHTY-SEVENTH CONGRESS, SEPTEMBER 6, 1961
H.R. 5964 [7]

An Act to authorize the use of funds arising from a judgment in favor of the Potawatomi Nation of Indians, 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 funds on deposit in the Treasury of the United States to the credit of the Potawatomi Nation of Indians that were appropriated by the Act of September 8, 1960 (74 Stat. 830), to pay a judgment by the Indian Claims Commission dated February 26, 1959, and the interest thereon, be divided on the basis of 780/2,180ths to the Prairie Band of Potawatomi Indians of Kansas, and 1,400/2,180ths to the Citizen Band of Potawatomi Indians of Oklahoma, and the funds so divided, including the interest accruing thereon, after payment of attorney fees and expenses, may be advanced or expended for any purpose that is authorized by the respective tribal governing bodies and approved by the Secretary of the Interior. Any part of such funds that may be distributed per capita to the members of the bands shall not be subject to Federal or State income tax.

Approved September 6, 1961.

PUBLIC LAW 87-235
EIGHTY-SEVENTH CONGRESS, SEPTEMBER 14, 1961
S. 1518 [8]

An Act providing for the disposition of judgment funds of the Omaha Tribe of Indians.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That the Secretary

[7] House Report No. 732, and Senate Report No. 782, are not published herein.
[8] House Report No. 1004 and Senate Report No. 598 are not published herein.

of the Interior is authorized and directed, pursuant to such regulations as may be issued by him, to prepare a roll of Omaha Indians whose names appear on the Omaha allotment rolls finally approved pursuant to the Acts of Congress of August 7, 1882 (22 Stat. 341) and March 3, 1893 (27 Stat. 612), and who are living on the date of this Act, and the descendants of such allottees who are born and living on the date of this Act and who possess Omaha blood of the degree of one-fourth or more regardless of whether such allottees are living or deceased: *Provided*, That no person who is enrolled with any other tribe of Indians or who has received an allotment of land on any other reservation shall be enrolled under the provisions of this Act unless the application for enrollment by such person is approved by a two-thirds vote of the governing body of the Omaha Tribe of Nebraska. Applications for enrollment must be filed with the area director of the Bureau of Indian Affairs, Aberdeen, South Dakota, within four months after the date of this Act. For a period of three months thereafter, the Secretary shall permit the examination of the applications by the governing body of the Omaha Tribe of Nebraska for the purpose of lodging protests against any application. The determination of the Secretary regarding the eligibility of an applicant shall be final.

SEC. 2. The roll prepared pursuant to section 1 of this Act shall constitute the membership roll of the Omaha Tribe of Nebraska as of the date of this Act, notwithstanding the provisions of article II, section 1 of the tribal constitution, and children who are born after the date of this Act may be enrolled if they meet the requirements of section 1(b) of article II of the tribal constitution, applicable to children born after the date that amendment I to said constitution was approved, or any amendment thereof.

SEC. 3. Of the funds on deposit in the Treasury of the United States to the credit of the Omaha Tribe of Nebraska that were appropriated to pay a judgment by the Indian Claims Commission dated February 11, 1960, and the interest thereon, after payment of attorneys' fees and expenses, the Secretary of the Interior shall make a per capita distribution of a sum up to a maximum of $750, to the extent available, to each person whose name appears on the roll prepared pursuant to section 1 of this Act; and the balance of such funds after making payment of or provision for such per capita distribution and accrued and accruing interest, if any, may be advanced or expended for any purpose that is authorized by the tribal governing body and approved in writing by the Secretary. The funds so distributed shall not be subject to Federal or State income taxes.

SEC. 4. (a) Except as provided in subsection (b) of this section, the Secretary shall distribute a per capita share payable to a living enrollee directly to such enrollee, and the Secretary shall distribute a per capita share payable to a deceased enrollee directly to his next of kin or legatees as determined by the laws of the place of domicile of the decedent upon proof of death and inheritance satisfactory to the Secretary, whose findings upon such proof shall be final and conclusive.

(b) A share payable to a person under twenty-one years of age or to a person under a legal disability shall be paid in accordance with

such procedures as the Secretary determines will adequately protect the best interests of such persons.

SEC. 5. No part of any of the funds which may be so distributed shall be subject to any lien, debt, or claim of any nature whatsoever against the tribe or individual Indians except delinquent debts owed by the tribe to the United States or owed by individual Indians to the tribe or to the United States.

SEC. 6. All costs incurred by the Secretary in the preparation of the roll and in the payment of the per capita shares in accordance with provisions of this Act shall be paid by appropriate withdrawals from the judgment fund.

SEC. 7. The Secretary is authorized to prescribe rules and regulations to carry out the provisions of this Act.

Approved September 14, 1961.

PUBLIC LAW 87-256
EIGHTY-SEVENTH CONGRESS, SEPTEMBER 21, 1961
H.R. 8666 [9]

An Act to provide for the improvement and strengthening of the international relations of the United States by promoting better mutual understanding among the peoples of the world through educational and cultural exchanges.

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 "Mutual Educational and Cultural Exchange Act of 1961".

SEC. 101. STATEMENT OF PURPOSE.—The purpose of this Act is to enable the Government of the United States to increase mutual understanding between the people of the United States and the people of other countries by means of educational and cultural exchange; to strengthen the ties which unite us with other nations by demonstrating the educational and cultural interests, developments, and achievements of the people of the United States and other nations, and the contributions being made toward a peaceful and more fruitful life for people throughout the world; to promote international cooperation for educational and cultural advancement; and thus to assist in the development of friendly, sympathetic, and peaceful relations between the United States and the other countries of the world.

SEC. 102. (a) The President is authorized, when he considers that it would strengthen international cooperative relations, to provide, by grant, contract, or otherwise, for—

(1) educational exchanges, (i) by financing studies, research, instruction, and other educational activities—

(A) of or for American citizens and nationals in foreign countries, and

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[9] Senate Report No. 372, page 395, this Bulletin; Conference Report No. 1197, page 411, this Bulletin; House Report No. 1094 is not published herein.

(B) of or for citizens and nationals of foreign countries in American schools and institutions of learning located in or outside the United States;

and (ii) by financing visits and interchanges between the United States and other countries of students, trainees, teachers, instructors, and professors;

(2) cultural exchanges, by financing—

(i) visits and interchanges between the United States and other countries of leaders, experts in fields of specialized knowledge or skill, and other influential or distinguished persons;

(ii) tours in countries abroad by creative and performing artists and athletes from the United States, individually and in groups, representing any field of the arts, sports, or any other form of cultural attainment;

(iii) United States representation in international artistic, dramatic, musical, sports, and other cultural festivals, competitions, meetings, and like exhibitions and assemblies;

(iv) participation by groups and individuals from other countries in nonprofit activities in the United States similar to those described in subparagraphs (ii) and (iii) of this paragraph, when the President determines that such participation is in the national interest.

(3) United States participation in international fairs and expositions, including trade and industrial fairs and other public or private demonstrations of United States economic accomplishments and cultural attainments.

(b) In furtherance of the purposes of this Act, the President is further authorized to provide for—

(1) interchanges between the United States and other countries of handicrafts, scientific, technical, and scholarly books, books of literature, periodicals, and Government publications, and the reproduction and translation of such writings, and the preparation, distribution, and interchange of other educational and research materials, including laboratory and technical equipment for education and research;

(2) establishing and operating in the United States and abroad centers for cultural and technical interchanges to promote better relations and understanding between the United States and other nations through cooperative study, training, and research;

(3) assistance in the establishment, expansion, maintenance, and operation of schools and institutions of learning abroad, founded, operated, or sponsored by citizens or nonprofit institutions of the United States, including such schools and institutions serving as demonstration centers for methods and practices employed in the United States;

(4) fostering and supporting American studies in foreign countries through professorships, lectureships, institutes, seminars, and courses in such subjects as American history, government, economics, language and literature, and other subjects related to American civilization and culture, including financing the attendance at such studies by persons from other countries;

(5) promoting and supporting medical, scientific, cultural, and educational research and development;

(6) promoting modern foreign language training and area studies in United States schools, colleges, and universities by supporting visits and study in foreign countries by teachers and prospective teachers in such schools, colleges, and universities for the purpose of improving their skill in languages and their knowledge of the culture of the people of those countries, and by financing visits by teachers from those countries to the United States for the purpose of participating in foreign language training and area studies in United States schools, colleges, and universities;

(7) United States representation at international nongovernmental educational, scientific, and technical meetings;

(8) participation by groups and individuals from other countries in educational, scientific, and technical meetings held under American auspices in or outside the United States;

(9) encouraging independent research into the problems of educational and cultural exchange.

SEC. 103. (a) The President is authorized to enter into agreements with foreign governments and international organizations, in furtherance of the purposes of this Act. In such agreements the President is authorized, when he deems it in the public interest, to seek the agreement of the other governments concerned to cooperate and assist, including making use of funds placed in special accounts pursuant to agreements concluded in accordance with section 115(b)(6) of the Economic Cooperation Act of 1948, or any similar agreements, in providing for the activities authorized in section 102, and particularly those authorized in subsection 102(a)(1), of this Act with respect to the expenses of international transportation of their own citizens and nationals and of activities in furtherance of the purposes of this Act carried on within the borders of such other nations.

(b) Such agreements may also provide for the creation or continuation of binational or multinational educational and cultural foundations and commissions for the purpose of administering programs in furtherance of the purposes of this Act.

(c) In such agreements with international organizations, the President may provide for equitable United States participation in and support for, including a reasonable share of the cost of, educational and cultural programs to be administered by such organizations.

SEC. 104. (a) The President may delegate, to such officers of the Government as he determines to be appropriate, any of the powers conferred upon him by this Act to the extent that he finds such delegation to be in the interest of the purposes expressed in this Act and the efficient administration of the programs undertaken pursuant to this Act: *Provided*, That where the President has delegated any of such powers to any officer, before the President implements any proposal for the delegation of any of such powers to another officer, that proposal shall be submitted to the Speaker of the House of Representatives and to the Committee on Foreign Relations of the Senate, and thereafter a period of not less than sixty days shall have elapsed while Congress is in session. In computing such sixty days, there shall be excluded the days on which either House is not in session because of an adjournment of more than three days.

(b) The President is authorized to employ such other personnel as he deems necessary to carry out the provisions and purposes of this Act, and of such personnel not to exceed ten may be compensated without regard to the provisions of the Classification Act of 1949, as amended, and of these not to exceed five may be compensated at a rate in excess of the highest rate provided for grades of the general schedule established by the Classification Act of 1949, as amended, but not in excess of $1,000 per annum more than such highest rate. Such positions shall be in addition to the number authorized by section 505 of the Classification Act of 1949, as amended.

(c) For the purpose of performing functions under this Act outside the United States, including participation in binational or multinational foundations or commissions, the Secretary of State may employ or assign or authorize the employment or assignment for the duration of operations under this Act of persons in or to the Foreign Service Reserve or Foreign Service Staff and alien clerks and employees in accordance with applicable provisions of the Foreign Service Act of 1946, as amended (22 U.S.C. 801).

(d) For the purpose of performing functions under this Act outside the United States, the President is authorized to provide that any person employed or assigned by a United States Government agency shall be entitled, except to the extent that the President may specify otherwise in cases in which the period of employment or assignment exceeds thirty months, to the same benefits as are provided by section 528 of the Foreign Service Act of 1946, as amended (22 U.S.C. 928), for persons appointed to the Foreign Service Reserve and, except for policymaking officials, the provisions of section 1005 of the Foreign Service Act of 1949, as amended (22 U.S.C. 807), shall apply in the case of such persons.

(e) (1) In providing for the activities and interchanges authorized by section 102 of this Act, grants may be made to or for individuals, either directly or through foundations or educational or other institutions, which foundations or institutions are public or private nonprofit, and may include funds for tuition and other necessary incidental expenses, for travel expenses from their places of residence and return for themselves, and, whenever it would further the purposes of this Act, for the dependent members of their immediate families, for health and accident insurance premiums, emergency medical expenses, costs of preparing and transporting to their former homes the remains of any of such persons who may die while away from their homes as participants or dependents of participants in any program under this Act, and for per diem in lieu of subsistence at rates prescribed by the President, for all such persons, and for such other expenses as are necessary for the successful accomplishment of the purposes of this Act.

(2) Funds available for programs under this Act may be used (i) to provide for orientation courses, language training, or other appropriate services and materials for persons traveling out of the countries of their residence for educational and cultural purposes which further the purposes of this Act, whether or not they are receiving other financial support from the Government, and (ii) to provide or continue services to increase the effectiveness of such programs following the return of such persons to the countries of their residence.

(3) For the purpose of assisting foreign students in making the best use of their opportunities while attending colleges and universities in the United States, and assisting such students in directing their talents and initiative into channels which will make them more effective leaders upon return to their native lands, the President may make suitable arrangements, by contract or otherwise, for the establishment and maintenance at colleges and universities in the United States attended by foreign students of an adequate counseling service.

(4) The President is authorized to provide for publicity and promotion (including representation) abroad of activities of the type provided for in this Act.

(f) All persons employed or assigned to duties under this Act shall be investigated with respect to loyalty and suitability in accordance with standards and procedures established by the President.

SEC. 105. (a) Appropriations to carry out the purposes of this Act, to remain available until expended, are hereby authorized, and this authorization includes the authority to grant, in any appropriation Act, the authority to enter into contracts, within the amounts so authorized, creating obligations in advance of appropriations.

(b) Funds appropriated for programs under this Act may, without regard to section 3651 of the Revised Statutes (31 U.S.C. 543), be used for the acquisition from any source of foreign currencies in such amounts as may be necessary for current expenditures and for grants, including grants to foundations and commissions in accordance with international agreements providing for the accomplishment of the purposes of this Act.

(c) Moneys appropriated to any department or agency of the Government in furtherance of the purposes of this Act for research, technical aid, and educational and cultural programs, may be transferred by the President to any other appropriation available for like purposes, but no appropriation authorized by this Act shall be increased or decreased by more than 10 per centum by reason of transfers pursuant to this paragraph.

(d) The President is authorized—

(1) to reserve in such amounts and for such periods as he shall determine to be necessary to provide for the programs authorized by subsections 102(a)(1) and 102(a)(2)(i), and

(2) notwithstanding the provisions of any other law, to use in such amounts as may from time to time be specified in appropriation Acts, to the extent that such use is not restricted by agreement with the foreign nations concerned, for any programs authorized by this Act,

any currencies of foreign nations received or to be received by the United States or any agency thereof—

(i) under agreements disposing of surplus property or settling lend-lease and other war accounts concluded after World War II;

(ii) as the proceeds of sales or loan repayments, including interest, for transactions heretofore or hereafter effected under the Agricultural Trade Development and Assistance Act of 1954, as amended;

(iii) in repayment of principal or interest on any other credit extended or loan heretofore or hereafter made by the United States or any agency thereof; or

(iv) as deposits to the account of the United States pursuant to section 115(b)(6) or section 115(h) of the Economic Cooperation Act of 1948, as amended, or any similar provision of any other law.

(e) The President is further authorized to reserve and use for educational and cultural exchange programs and other activities authorized in subsections 102 (a) and (b) of this Act, in relation to Finland and the people of Finland, all sums due or paid on and after August 24, 1949, by the Republic of Finland to the United States as interest on or in retirement of the principal of the debt incurred under the Act of February 25, 1919, as refunded by the agreement dated May 1, 1923, pursuant to the authority contained in the Act of February 9, 1922, or of any other indebtedness incurred by that Republic and owing to the United States as a result of World War I.

(f) Foreign governments, international organizations and private individuals, firms, associations, agencies, and other groups shall be encouraged to participate to the maximum extent feasible in carrying out this Act and to make contributions of funds, property, and services which the President is hereby authorized to accept, to be utilized to carry out the purposes of this Act. Funds made available for the purposes of this Act may be used to contribute toward meeting the expenses of activities carried out through normal private channels, by private means, and through foreign governments and international organizations.

SEC. 106. (a)(1) For the purpose of selecting students, scholars, teachers, trainees, and other persons to participate in the programs authorized under section 102(a)(1) of this Act, and of supervising such programs and the programs authorized under section 102(b)(4) and (6), there is hereby continued the authority of the President to appoint a Board of Foreign Scholarships (hereinafter referred to as the "Board") consisting of twelve members. In connection with appointments to such Board, due consideration shall be given to the selection of distinguished representatives of cultural, educational, student advisory, and war veterans groups, and representatives of the United States Office of Education, the United States Veterans' Administration, public and private nonprofit educational institutions.

(2) In the selection of American citizens for participation in programs under this Act, preference shall be given to those who have served in the Armed Forces of the United States, and due consideration shall be given to applicants from all geographical areas of the United States.

(b)(1) The United States Advisory Commission on International Educational and Cultural Affairs (hereinafter referred to as the "Commission") is hereby established to replace the United States Advisory Commission on Educational Exchange. The Commission shall formulate and recommend to the President policies for exercising his authority under this Act and shall appraise the effectiveness of programs carried out pursuant to it. The Commission shall make a special study of the effectiveness of past programs with emphasis on the activities of a reasonably representative cross section of past recipients of aid and shall submit a report to the Congress not later than December 31, 1962.

(2) The Commission shall consist of nine members, who shall be appointed by the President, by and with the advice and consent of the Senate. Members of the Commission shall be appointed on a nonpartisan basis.

(3) The members of the Commission shall represent the public interest and shall be selected from a cross section of educational, cultural, scientific, technical, and public service backgrounds.

(4) The term of each member shall be three years except that, of the first nine appointments, three shall be for a term of one year and three shall be for a term of two years. Any member appointed to fill a vacancy occurring prior to the expiration of the term for which his predecessor is appointed shall be appointed for the remainder of such term. Upon the expiration of his term of office any member may continue to serve until his successor is appointed and has qualified.

(5) The President shall designate a Chairman from among members of the Commission.

(6) The Commission is authorized to adopt such rules and regulations as it may deem necessary to carry out the authority conferred upon it by this Act.

(c) (1) There is hereby continued the Advisory Committee on the Arts (hereinafter referred to as the "Committee") created under section 10 of the International Cultural Exchange and Trade Fair Participation Act of 1956, consisting of a Chairman and nine other members of whom at least one shall be a member of the Commission. Appointment of all members and selection of the Chairman of this Committee shall hereafter be made by the Secretary of State. In making such appointments due consideration shall be given to the recommendations for nomination submitted by leading national organizations in the major art fields.

(2) The members of the Committee shall be individuals whose knowledge of or experience in, or whose profound interest in, one or more of the arts will enable them to assist the Commission, the President, and other officers of the Government in performing the functions described in paragraph (3) of this subsection.

(3) The Committee shall, in connection with activities authorized under subsection 102(a)(2) of this Act—

(A) advise and assist the Commission in the discharge of its responsibilities in the field of international educational exchange and cultural presentations with special reference to the role of the arts in such fields;

(B) advise other interested officers of the Government in the discharge of their responsibilities in connection with such activities and in connection with other international activities concerned with the arts;

(C) provide such other advice and assistance as may be necessary or appropriate.

(4) The term of office of each of the members of the Committee shall be three years.

(d) The President is authorized to create such interagency and other advisory committees as in his judgment may be of assistance in carrying out the purposes of this Act, and from time to time to convene conferences of persons interested in educational and cultural affairs to consider matters relating to the purposes of this Act.

(e) The provisions of section 214 of the Act of May 3, 1945 (59 Stat. 134; 31 U.S.C. 691), shall be applicable to any interagency committee created pursuant to the provisions of this Act. Members of the Board, the Commission, the Committee, and other committees provided for in this section shall be entitled (i) to transportation expenses and per diem in lieu of subsistence at the rate prescribed by or established pursuant to section 5 of the Administrative Expense Act of 1946, as amended (5 U.S.C. 73b–2), while away from home in connection with attendance at meetings or in consultation with officials of the Government or otherwise carrying out duties as authorized, and (ii) if not otherwise in the employ of the United States Government, to compensation at rates not in excess of $50 per diem while performing services for such Board, Commission, Committee, or other committee.

(f) The President is authorized to provide for necessary secretarial and staff assistance for the Board, the Commission, the Committee, and such other committees as may be created under this section.

SEC. 107. The Board, the Commission, and the Committee shall submit annual reports to the Congress and such other reports to the Congress as they deem appropriate, and shall make reports to the public in the United States and abroad to develop a better understanding of and support for the programs authorized by this Act.

SEC. 108. (a) Whenever the President determines it to be in furtherance of this Act, the functions authorized in section 102(a) (2) and (3) may be performed without regard to such provisions of law or limitations of authority regulating or relating to the making, performance, amendment, or modification of contracts, the acquisition and disposition of property, and the expenditure of Government funds, as he may specify.

(b) The President shall submit annual reports to the Congress of activities carried on and expenditures made in furtherance of the purposes of this Act. Each such report shall include the texts of agreements made with other nations during the period covered by the report, a full description of the program and the funds expended with respect to each country in which activities have been carried on in furtherance of the purposes of this Act.

(c) In connection with activities authorized by section 102(a) (2) and (3) of this Act, the President is authorized to provide for all necessary expenditures involved in the selection, purchase, rental, construction, or other acquisition of exhibits and materials and equipment therefor, and the actual display thereof, including but not limited to costs of transportation, insurance, installation, safekeeping and storage, maintenance and operation, rental of space, and dismantling.

(d) The President is authorized to utilize the provisions of title VIII of the United States Information and Educational Exchange Act of 1948, as amended, to the extent he deems necessary in carrying out the provisions and purposes of this Act.

SEC. 109. The Immigration and Nationality Act, as amended, is hereby amended as follows:

(a) In section 101(a)(15)(F) insert "(i)" at the beginning thereof, strike out the semicolon at the end thereof, and add the following: ", and (ii) the alien spouse and minor children of any such alien if accompanying him or following to join him;"

(b) In section 101(a)(15)(I) change the period to a semicolon at the end thereof and add the following:

(J) an alien having a residence in a foreign country which he has no intention of abandoning who is a bona fide student, scholar, trainee, teacher, professor, research assistant, specialist, or leader in a field of specialized knowledge or skill, or other person of similar description, who is coming temporarily to the United States as a participant in a program designated by the Secretary of State, for the purpose of teaching, instructing or lecturing, studying, observing, conducting research, consulting, demonstrating special skills, or receiving training, and the alien spouse and minor children of any such alien if accompanying him or following to join him.

(c) In section 212 redesignate subsection "(e)" to read "(f)" and add a new subsection "(e)" to read:

(e) No person admitted under section 101(a)(15)(J) or acquiring such status after admission shall be eligible to apply for an immigrant visa, or for permanent residence, or for a nonimmigrant visa under section 101(a)(15)(H) until it is established that such person has resided and been physically present in the country of his nationality or his last residence, or in another foreign country for an aggregate of at least two years following departure from the United States: *Provided,* That such residence in another foreign country shall be considered to have satisfied the requirements of this subsection if the Secretary of State determines that it has served the purpose and the intent of the Mutual Educational and Cultural Exchange Act of 1961: *Provided further,* That upon the favorable recommendation of the Secretary of State, pursuant to the request of an interested United States Government agency, or of the Commissioner of Immigration and Naturalization after he has determined that departure from the United States would impose exceptional hardship upon the alien's spouse or child (if such spouse or child is a citizen of the United States or a lawfully resident alien), the Attorney General may waive the requirement of such two-year foreign residence abroad in the case of any alien whose admission to the United States is found by the Attorney General to be in the public interest: *and provided further,* That the provisions of this paragraph shall apply also to those persons who acquired exchange visitor status under the United States Information and Educational Exchange Act of 1948, as amended; and

(d) In section 248, after the language "paragraph (15)(C)" in both instances, add "or (J)".

SEC. 110. (a) Section 117(b)(2)(A) of the Internal Revenue Code of 1954 (relating to the conditions for exclusion of scholarships and fellowship grants in the case of individuals who are not candidates for degrees is amended to read as follows:

(A) CONDITIONS FOR EXCLUSION.—The grantor of the scholarship or fellowship grant is—

(i) an organization described in section 501(c)(3) which is exempt from tax under section 501(a),

(ii) a foreign government,

(iii) an international organization, or a binational or multinational educational and cultural foundation or commission created or continued pursuant to the Mutual Educational and Cultural Exchange Act of 1961, or

(iv) the United States, or an instrumentality or agency thereof, or a State, a territory, or a possession of the United States, or any political subdivision thereof, or the District of Columbia.

(b) Section 871 of the Internal Revenue Code of 1954 (relating to tax on nonresident alien individuals) is amended by redesignating subsection (d) as subsection (e) and by inserting after subsection (c) the following new subsection:

(d) PARTICIPANTS IN CERTAIN EXCHANGE OR TRAINING PROGRAMS.—For purposes of this section, a nonresident alien individual who (without regard to

this subsection) is not engaged in trade or business within the United States and who is temporarily present in the United States as a nonimmigrant under subparagraph (F) or (J) of section 101(a)(15) of the Immigration and Nationality Act, as amended, shall be treated as a nonresident alien individual engaged in trade or business within the United States.

(c) Section 872(b) of the Internal Revenue Code of 1954 (relating to exclusions from gross income of nonresident alien individuals) is amended by adding at the end thereof the following new paragraph:

(3) COMPENSATION OF PARTICIPANTS IN CERTAIN EXCHANGE OR TRAINING PROGRAMS.—Compensation paid by a foreign employer to a nonresident alien individual for the period he is temporarily present in the United States as a nonimmigrant under subparagraph (F) or (J) of section 101(a)(15) of the Immigration and Nationality Act, as amended. For purposes of this paragraph, the term "foreign employer" means—

(A) a nonresident alien individual, foreign partnership, or foreign corporation, or

(B) an office or place of business maintained in a foreign country or in a possession of the United States by a domestic corporation.

(d)(1) Section 1441(a) of the Internal Revenue Code of 1954 (relating to withholding of tax on nonresident aliens) is amended by inserting before the period at the end thereof the following: ", except that in the case of any item of income specified in the second sentence of subsection (b), the tax shall be equal to 18 percent of such item".

(2) Section 1441(b) of such Code (relating to income items subject to withholding) is amended by adding at the end thereof the following new sentence: "The items of income referred to in subsection (a) from which tax shall be deducted and withheld at the rate of 18 percent are—

"(1) that portion of any scholarship or fellowship grant which is recevied by a nonresident alien individual who is temporarily present in the United States as a nonimmigrant under subparagraph (F) or (J) of section 101(a)(15) of the Immigration and Nationality Act, as amended, and which is not excluded from gross income under section 117(a)(1) solely by reason of section 117(b)(2)(B); and

"(2) amounts described in subparagraphs (A), (B), (C), and (D) of section 117(a)(2) which are received by any such nonresident alien individual and which are incident to a scholarship or fellowship grant to which section 117(a)(1) applies, but only to the extent such amounts are includible in gross income."

(3) Section 1441(c)(4) of the Internal Revenue Code of 1954 (relating to exceptions to withholding of tax on nonresident aliens) is amended to read as follows:

(4) COMPENSATION OF CERTAIN ALIENS.—Under regulations prescribed by the Secretary or his delegate, there may be exempted from deduction and withholding under subsection (a) the compensation for personal services of—

(A) nonresident alien individuals who enter and leave the United States at frequent intervals, and

(B) a nonresident alien individual for the period he is temporarily present in the United States as a nonimmigrant under subparagraph (F) or (J) of section 101(a)(15) of the Immigration and Nationality Act, as amended.

(e)(1) Section 3121(b) of the Internal Revenue Code of 1954 (relating to the definition of employment for purposes of the Federal Insurance Contributions Act) is amended—

(A) by striking out "or" at the end of paragraph (17);

(B) by striking out the period at the end of paragraph (18) and inserting in lieu thereof "; or"; and

(C) by adding at the end thereof the following new paragraph:

(19) Service which is performed by a nonresident alien individual for the period he is temporarily present in the United States as a nonimmigrant under subparagraph (F) or (J) of section 101(a)(15) of the Immigration and Nationality Act, as amended, and which is performed to carry out the purpose specified in subparagraph (F) or (J), as the case may be.

(2) Section 210(a) of the Social Security Act, as amended, is amended—

(A) by striking out "or" at the end of paragraph (17);

(B) by striking out the period at the end of paragraph (18) and inserting in lieu thereof "; or"; and

(C) by adding at the end thereof the following new paragraph:

(19) Service which is performed by a nonresident alien individual for the period he is temporarily present in the United States as a nonimmigrant under subparagraph (F) or (J) of section 101(a)(15) of the Immigration and Nationality Act, as amended, and which is performed to carry out the purpose specified in subparagraph (F) or (J), as the case may be.

(f) Section 3306(c) of the Internal Revenue Code of 1954 (relating to the definition of employment for purposes of the Federal Unemployment Tax Act) is amended—

(1) by striking out "or" at the end of paragraph (16);

(2) by striking out the period at the end of paragraph (17) and inserting in lieu thereof "; or"; and

(3) by adding at the end thereof the following new paragraph:

(18) Service which is performed by a nonresident alien individual for the period he is temporarily present in the United States as a nonimmigrant under subparagraph (F) or (J) of section 101(a)(15) of the Immigration and Nationality Act, as amended, and which is performed to carry out the purpose specified in subparagraph (F) or (J), as the case may be.

(g)(1) Section 3401(a)(6) of the Internal Revenue Code of 1954 (relating to the definition of wages for purposes of withholding of income tax at source) is amended by adding at the end thereof the following new subparagraph:

(C) an individual who is temporarily present in the United States as a nonimmigrant under subparagraph (F) or (J) of section 101(a)(15) of the Immigration and Nationality Act, as amended, if such remuneration is exempt, under section 1441(c)(4)(B), from deduction and withholding under section 1441(a), and is not exempt from taxation under section 872(b)(3), or.

(2) Section 3402(f) of such Code (relating to withholding exemptions) is amended by adding at the end thereof the following new paragraph:

(6) EXEMPTION OF CERTAIN NONRESIDENT ALIENS.—Notwithstanding the provisions of paragraph (1), a nonresident alien individual (other than an individual described in section 3401(a)(6) (A) or (B)) shall be entitled to only one withholding exemption.

(h)(1) The amendments made by subsections (a), (b), and (c) of this section shall apply to taxable years beginning after December 31, 1961.

(2) The amendments made by subsection (d) of this section shall apply with respect to payments made after December 31, 1961.

(3) The amendments made by subsections (e) and (f) of this section shall apply with respect to service performed after December 31, 1961.

(4) The amendments made by subsection (g) of this section shall apply with respect to wages paid after December 31, 1961.

SEC. 111. (a) There are hereby repealed—

(1) Section 32(b)(2) of the Surplus Property Act of 1944, as amended (60 Stat. 754, 50 U.S.C. App. Sec. 1641);

(2) Sections 2(2), 201, 203 insofar as it relates to schools, 601, 602 and 603 insofar as they relate to the Advisory Commission on Educational Exchange, 1001 insofar as it relates to persons employed or assigned to duties under this Act, and 1008 and 1009 insofar as they relate to educational exchange activities, of the United States Information and Educational Exchange Act of 1948, as amended (62 Stat. 6; 22 U.S.C. sections 1431(2); 1434, 1439, 1440, 1446, 1448, 1466, 1467, and 1468);

(3) The International Cultural Exchange and Trade Fair Participation Act of 1956 (70 Stat. 778; 22 U.S.C. 1991–2001);

(4) The joint resolution of August 24, 1949, authorizing the use of Finnish World War I debt payments available for educational and technical instruction, and so forth (63 Stat. 630; 20 U.S.C. 222–224).

(b) All Executive orders, agreements, determinations, regulations, contracts, appointments, and other actions issued, concluded, or taken under authority of any provisions of law repealed by subsection (a) of this section shall continue in full force and effect, and shall be applicable to the appropriate provisions of this Act until modified or superseded by appropriate authority.

(c) Any reference in any other Act to the provisions of law listed in subsection (a) shall hereafter be considered to be references to the appropriate provisions of this Act.

Approved September 21, 1961.

PUBLIC LAW 87-262
EIGHTY-SEVENTH CONGRESS, SEPTEMBER 21, 1961
H.R. 6302 [10]

An Act to establish a teaching hospital for Howard University, to transfer Freedmen's Hospital to the University, and for other purposes.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,

TRANSFER OF FREEDMEN'S HOSPITAL

SECTION 1. (a) For the purpose of assisting in the provision of teaching hospital resources for Howard University, thereby assisting the university in the training of medical and allied personnel and in providing hospital services for the community, the Secretary of Health, Education, and Welfare shall, pursuant to agreement with

[10] Senate Report No. 876, page 416, this Bulletin; since House Report No. 741 is substantially the same as the Senate Report, it is not published herein.

the board of trustees of Howard University, transfer to Howard University, without reimbursement, all right, title, and interest of the United States in certain lands in the District of Columbia, together with the buildings and improvements thereon and the personal property used in connection therewith (as determined by the Secretary), commonly known as Freedmen's Hospital.

(b) It is the intent of Congress (1) that the transfer of Freedmen's Hospital to Howard University be effected as soon as practicable, (2) to assure the well-being of patients at Freedmen's Hospital during the period of transition, and (3) that the transfer be effected with minimum dislocation of the present hospital staff and maximum consideration of their interests as employees.

(c) The Secretary of Health, Education, and Welfare shall report to the Congress the terms of the agreement for such transfer.

PROVISION FOR EMPLOYEES OF HOSPITAL

SEC. 2. (a) The agreement for transfer of Freedmen's Hospital referred to in section 1 shall include provisions to assure that—

(1) all individuals who are career or career-conditional employees of the hospital on the day preceding the effective date of the transfer of the hospital, except those in positions with respect to which they have been notified not less than six months prior to the effective date of such transfer that their positions are to be abolished, will be offered an opportunity to transfer to Howard University;

(2) Howard University—

(A) will not reduce the salary levels for such employees who transfer,

(B) will deposit currently (i) in the civil service retirement and disability fund created by the Act of May 22, 1920, the employee deductions and agency contributions required by the Civil Service Retirement Act, and (ii) in the fund created by section 5(c) of the Federal Employees' Group Life Insurance Act of 1954 the employee deductions and agency contributions required by the Federal Employees' Group Life Insurance Act of 1954,

(C) will provide other benefits for such employees as nearly equivalent as may be practicable to those generally applicable, on the effective date of the transfer of the hospital, to civilian employees of the United States, and

(D) in determining the seniority rights of its employees, Howard University will credit service with Freedmen's Hospital performed by such employees who transfer, on the same basis as it would credit such service had it been performed for such University;

(3) the transfer will become effective not later than the beginning of the second month which begins after construction of the new hospital facilities authorized by section 3 is commenced.

(b) The Department of Health, Education, and Welfare shall make every reasonable effort to place in other comparable Federal positions all individuals who are career or career-conditional employees of Freedmen's Hospital on the date of enactment of this Act and who do not transfer to Howard University.

(c) Each individual who is an employee of Freedmen's Hospital on the date of enactment of this Act and who transfers to Howard University shall, so long as he is continuously in the employ of Howard University, be regarded as continuing in the employ of the United States for the purposes of the Civil Service Retirement Act, the Federal Employees' Group Life Insurance Act of 1954. For purposes of section 3121(b) of the Internal Revenue Code of 1954 and section 210 of the Social Security Act, service performed by such individual during the period of his employment at Howard University shall be regarded as though performed in the employ of the United States.

AUTHORIZATION OF CONSTRUCTION OF HOSPITAL FACILITIES

SEC. 3. For the purpose specified in section 1, there are hereby authorized to be appropriated such sums as may be necessary for the construction of a building or buildings and facilities, including equipment, and for remodeling of existing buildings (including repair and replacement of equipment) which are to be combined with the building or buildings and facilities so constructed, to provide a hospital with a capacity of not to exceed five hundred beds.

CONTINUED OPERATION OF FACILITIES

SEC. 4. If, within twenty years after the completion of construction (as determined by the Secretary of Health, Education, and Welfare) of the new hospital facilities authorized by section 3, any of such facilities, or of the facilities transferred pursuant to section 1 and combined with such new facilities, are transferred by Howard University to any other person or entity (except a transfer to the United States) or cease to be operated by the university as teaching hospital facilities, the United States shall be entitled to recover from the transferee or the university, in the case of a transfer, or from the university, if there is no transfer, an amount equal to the then value of such facilities (or so much thereof as is involved in the transfer, as the case may be), such value to be determined by agreement of the parties or by action brought in the United States District Court for the District of Columbia.

AUTHORIZATION OF APPROPRIATIONS FOR OPERATION

SEC. 5. In order to facilitate operation of teaching hospital facilities at Howard University, there are authorized to be appropriated annually to the university such sums as the Congress may determine, for the partial support of the operation of such facilities giving consideration to the cost imposed by the provisions of section 2 and the portion of the agreement under this Act relating to such provisions. The cost of operating such facilities, the appropriations pursuant to this section, and any other income derived from such operation or available for such purpose shall be identified and accounted for separately in the accounts of the university.

FINANCIAL POLICY

SEC. 6. It is hereby declared to be the policy of the Congress that, to the extent consistent with good medical teaching practice, the Howard University Hospital facilities shall become progressively more self-supporting. In order to further this policy, the President shall

submit to the Congress a report, based on a study of the financing of the operation of the hospital, containing his recommendations on the rate at which, consistent with the above policy, Federal financial participation in such cost of operation shall be reduced. Such report shall be submitted not later than the end of the second calendar year following the year in which the construction of the new hospital facilities, authorized by section 3, is completed.

REPEAL OF LAWS

SEC. 7. All laws heretofore applicable specifically to Freedmen's Hospital are, to the extent of such applicability, repealed, effective with the transfer of Freedmen's Hospital pursuant to section 1.

TRANSFER OF FUNDS

SEC. 8. All unexpended balances of appropriations, allocations, and other funds, available or to be made available, of Freedmen's Hospital are, effective with the transfer of Freedmen's Hospital pursuant to section 1, transferred to Howard University for use in the operation of the Howard University Hospital facilities, except to the extent (determined by the Director of the Bureau of the Budget) required to meet obligations already incurred and not assumed by the university.

Approved September 21, 1961.

PUBLIC LAW 87-293
EIGHTY-SEVENTH CONGRESS, SEPTEMBER 22, 1961
H.R. 7500 [11]

An Act to provide for a Peace Corps to help the peoples of interested countries and areas in meeting their needs for skilled manpower.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,

TITLE I—THE PEACE CORPS

SHORT TITLE

SECTION 1. This Act may be cited as the "Peace Corps Act".

DECLARATION OF PURPOSE

SEC. 2. The Congress of the United States declares that it is the policy of the United States and the purpose of this Act to promote world peace and friendship through a Peace Corps, which shall make available to interested countries and areas men and women of the United States qualified for service abroad and willing to serve, under conditions of hardship if necessary, to help the peoples of such countries and areas in meeting their needs for trained manpower, and to help promote a better understanding of the American people on the part of the peoples served and a better understanding of other peoples on the part of the American people.

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[11] This publication of the law is restricted to excerpts involving internal revenue matters; House Report No. 1115, page 419, this Bulletin; Senate Report No. 706, and Conference Report No. 1239, are not published herein.

TITLE II—AMENDMENT OF INTERNAL REVENUE CODE AND SOCIAL SECURITY ACT

TAXATION OF ALLOWANCES

SEC. 201. (a) Section 912 of the Internal Revenue Code of 1954 (relating to exemption from gross income for certain allowances) is amended by adding at the end thereof the following new paragraph:

> (3) PEACE CORPS ALLOWANCES.—In the case of an individual who is a volunteer or volunteer leader within the meaning of the Peace Corps Act and members of his family, amounts received as allowances under section 5 or 6 of the Peace Corps Act other than amounts received as—
>
> (A) termination payments under section 5(c) or section 6(1) of such Act,
>
> (B) leave allowances,
>
> (C) if such individual is a volunteer leader training in the United States, allowances to members of his family, and
>
> (D) such portion of living allowances as the President may determine under the Peace Corps Act as constituting basic compensation.

(b) Section 1303(b) of the Internal Revenue Code of 1954 (relating to definition of back pay) is amended by adding at the end thereof the following new paragraph:

> (4) Termination payments under section 5(c) or section 6(1) of the Peace Corps Act which are received or accrued by an individual during the taxable year on account of any period of service, as a volunteer or volunteer leader under the Peace Corps Act, occurring prior to the taxable year.

(c) Section 3401(a) of the Internal Revenue Code of 1954 (relating to the definition of wages for purposes of the collection of income tax at source on wages) is amended by striking out the period at the end of paragraph (12) and inserting in lieu thereof "; or", and by adding at the end thereof the following new paragraph:

> (13) pursuant to any provision of law other than section 5(c) or 6(1) of the Peace Corps Act, for service performed as a volunteer or volunteer leader within the meaning of such Act.

(d) The amendments made by subsections (a) and (b) of this section shall apply with respect to taxable years ending after March 1, 1961. The amendment made by subsection (c) shall apply with respect to remuneration paid after the date of the enactment of this Act.

SOCIAL SECURITY COVERAGE

SEC. 202. (a)(1) Section 3121(i) of the Internal Revenue Code of 1954 (relating to computation of wages for purposes of the Federal Insurance Contributions Act) is amended by adding at the end thereof the following new paragraph:

> (3) PEACE CORPS VOLUNTEER SERVICE.—For purposes of this chapter, in the case of an individual performing service, as a volunteer or volunteer leader within the meaning of the Peace Corps Act, to which the provisions of section 3121(p) are applicable, the term "wages" shall, subject to the provisions of subsection (a)(1) of this section, include as such individual's remuneration for such service only amounts paid pursuant to section 5(c) or 6(1) of the Peace Corps Act.

(2) Section 3121 of such Code is amended by adding at the end thereof the following new subsection:

> (p) PEACE CORPS VOLUNTEER SERVICE.—For purposes of this chapter, the term "employment" shall, notwithstanding the provisions of subsection (b) of this section, include service performed by an individual as a volunteer or volunteer leader within the meaning of the Peace Corps Act.

(3) The first sentence of section 3122 of such Code (relating to Federal service) is amended by inserting after "section 3121(m)(1) are applicable," the following: "and including service, performed as a volunteer or volunteer leader within the meaning of the Peace Corps Act, to which the provisions of section 3121(p) are applicable,".

(4) Section 6051(a) of such Code (relating to receipts for employees) is amended by adding at the end thereof the following new sentence: "In the case of compensation paid for service as a volunteer or volunteer leader within the meaning of the Peace Corps Act, the statement shall show, in lieu of the amount required to be shown by paragraph (5), the total amount of wages as defined in section 3121(a), computed in accordance with such section and section 3121(i)(3)."

(b)(1) Section 210 of the Social Security Act (42 U.S.C. 410) is amended by adding at the end thereof the following new subsection:

Peace Corps Volunteer Service

(o) The term "employment" shall, notwithstanding the provisions of subsection (a), include service performed by an individual as a volunteer or volunteer leader within the meaning of the Peace Corps Act.

(2) Section 209 of such Act (42 U.S.C. 409) is amended by adding at the end thereof the following new paragraph:

For purposes of this title, in the case of an individual performing service, as a volunteer or volunteer leader within the meaning of the Peace Corps Act, to which the provisions of section 210(o) are applicable, (1) the term "wages" shall, subject to the provisions of subsection (a) of this section, include as such individual's remuneration for such service only amounts certified as payable pursuant to section 5(c) or 6(1) of the Peace Corps Act, and (2) any such amount shall be deemed to have been paid to such individual at the time the service, with respect to which it is paid, is performed.

(3) The first sentence of section 205(p)(1) of such Act (42 U.S.C. 405(p)(1)) is amended by inserting after "are applicable," the following: "and including service, performed as a volunteer or volunteer leader within the meaning of the Peace Corps Act, to which the provisions of section 210(o) are applicable,".

(c) The amendments made by subsections (a) and (b) of this section shall apply with respect to service performed after the date of the enactment of this Act. In the case of any individual who is enrolled as a volunteer or volunteer leader under section 16(a) of this Act, such amendments shall apply with respect to service performed on or after the effective date of such enrollment.

Approved September 22, 1961.

PUBLIC LAW 87-298
EIGHTY-SEVENTH CONGRESS, SEPTEMBER 26, 1961
H.R. 8236 [12]

An Act to authorize the use of funds arising from judgments in favor of any of the Confederated Tribes of the Colville Reservation.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That the funds on

[12] House Report No. 1000 and Senate Report No. 1068 are not published herein.

deposit in the Treasury of the United States to the credit of the Colville Tribe, San Poeils-Nespelem Tribe, Okanogan Tribe, Methow Tribe, and Lake Tribe (certain constituent groups of the Confederated Tribes of the Colville Reservation) that were appropriated to pay a judgment of the Indian Claims Commission dated March 1, 1960, in docket numbered 181, and the funds which may be deposited in the Treasury of the United States to the credit of the said constituent groups or any other constituent groups of the Confederated Tribes of the Colville Reservation to pay any judgments arising out of proceedings presently pending before the Indian Claims Commission in dockets numbered 161, 179, 181–A, 181–B, 181–C, 222, and 224, and the interest on said judgments, after payment of attorney fees and expenses, shall be credited to the account of the Confederated Tribes of the Colville Reservation, and may be advanced or expended for any purpose that is authorized by the tribal governing body of the Confederated Tribes of the Colville Reservation and approved by the Secretary of the Interior. Any part of such funds that may be distributed per capita to the members of the tribes shall not be subject to Federal or State income tax.

Approved September 26, 1961.

PUBLIC LAW 87–312
EIGHTY-SEVENTH CONGRESS, SEPTEMBER 26, 1961
H.R. 7057 [13]

An Act relating to the determination of gross income from the property for taxable years prior to 1961 in the case of certain clays and shale which were used in the manufacture of certain clay products.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That (a) ELECTION FOR PAST YEARS.—In the case of brick and tile clay, fire clay, or shale used by the mineowner or operator in the manufacture of building or paving brick, drainage and roofing tile, sewer pipe, flower pots, and kindred products (without regard to the applicable rate of percentage depletion), if an election is made under subsection (c), for the purpose of applying section 613(c) of the Internal Revenue Code of 1954 (and corresponding provision of the Internal Revenue Code of 1939) for each of the taxable years with respect to which the election is effective—

(1) gross income from the property shall be 50 per centum of the amount for which the manufactured products are sold during the taxable year except that with respect to such manufactured products, gross income from the property shall not exceed an amount equal to $12.50 multiplied by the number of short tons used in the manufactured products sold during the taxable year, and

(2) for purposes of computing the 50 per centum limitation under section 613(a) of the Internal Revenue Code of 1954 (or

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[13] House Report No. 939, page 425, this Bulletin; Senate Report No. 903, page 429, this Bulletin.

the corresponding provision of the Internal Revenue Code of 1939), the taxable income from the property (computed without allowance for depletion) shall be 50 per centum of the taxable income from the manufactured products sold during the taxable year (computed without allowance for depletion).

(b) YEARS TO WHICH APPLICABLE.—An election made under subsection (c) to have the provisions of this section apply shall be effective for all taxable years beginning before January 1, 1961, in respect of which—

(1) the assessment of a deficiency,

(2) the refund or credit of an overpayment, or

(3) the commencement of a suit for recovery of a refund under section 7405 of the Internal Revenue Code of 1954,

is not prevented on the date of the enactment of this Act by the operation of any law or rule of law. Such election shall also be effective for any taxable year beginning before January 1, 1961, in respect of which an assessment of a deficiency has been made but not collected on or before the date of the enactment of this Act.

(c) TIME AND MANNER OF ELECTION.—An election to have the provisions of this section apply shall be made by the taxpayer on or before the sixtieth day after the date of publication in the Federal Register of final regulations issued under authority of subsection (f), and shall be made in such form and manner as the Secretary of the Treasury or his delegate shall prescribe by regulations. Such election, if made, may not be revoked.

(d) STATUTES OF LIMITATION.—Notwithstanding any other law, the period within which an assessment of a deficiency attributable to the election under subsection (c) may be made with respect to any taxable year for which such election is effective, and the period within which a claim for refund or credit of an overpayment attributable to the election under such subsection may be made with respect to any such taxable year, shall not expire prior to one year after the last day for making an election under subsection (c). An election by a taxpayer under subsection (c) shall be considered as a consent to the application of the provisions of this subsection.

(e) TERMS; APPLICABILITY OF OTHER LAWS.—Except where otherwise distinctly expressed or manifestly intended, terms used in this section shall have the same meaning as when used in the Internal Revenue Code of 1954 (or corresponding provisions of the Internal Revenue Code of 1939) and all provisions of law shall apply with respect to this section as if this section were a part of such Code (or corresponding provisions of the Internal Revenue Code of 1939).

(f) REGULATIONS.—The Secretary of the Treasury or his delegate shall prescribe such regulations as may be necessary to carry out the provisions of this section.

Approved September 26, 1961.

PUBLIC LAW 87-321
EIGHTY-SEVENTH CONGRESS, SEPTEMBER 26, 1961
H.R. 2585 [14]

An Act relating to the credits against the employment tax in the case of certain successor employers and to provide an election for past taxable years with respect to the determination of gross income from mining in the case of quartzite and clay used in the production of refractory products.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That (a) section 3302 of the Internal Revenue Code of 1954 (relating to credits against tax imposed by Federal Unemployment Tax Act) is amended by adding at the end thereof the following new subsection:

(e) SUCCESSOR EMPLOYER.—Subject to the limits provided by subsection (c), if—

(1) an employer acquires during any calendar year substantially all the property used in the trade or business of another person, or used in a separate unit of a trade or business of such other person, and immediately after the acquisition employs in his trade or business one or more individuals who immediately prior to the acquisition were employed in the trade or business of such other person, and

(2) such other person is not an employer for the calendar year in which the acquisition takes place,

then, for the calendar year in which the acquisition takes place, in addition to the credits allowed under subsections (a) and (b), such employer may credit against the tax imposed by section 3301 for such year an amount equal to the credits which (without regard to subsection (c)) would have been allowable to such other person under subsections (a) and (b) and this subsection for such year, if such other person had been an employer, with respect to remuneration subject to contributions under the unemployment compensation law of a State paid by such other person to the individual or individuals described in paragraph (1).

(b) The amendment made by subsection (a) shall apply with respect to the calendar year 1961 and each calendar year thereafter.

SEC. 2. ELECTION FOR QUARTZITE AND CLAY USED IN THE PRODUCTION OF REFRACTORY PRODUCTS.

(a) ELECTION FOR PAST YEARS.—If an election is made under subsection (c), in the case of quartzite and clay used by the mine owner or operator in the production of refractory products, for the purpose of applying section 613(c) of the Internal Revenue Code of 1954 (and corresponding provisions of the Internal Revenue Code of 1939) for each of the taxable years with respect to which the election is effective—

(1) the term "ordinary treatment processes" shall include crushing, grinding, and separating the mineral from waste, but shall not include any subsequent process; and

(2) the gross income from mining for each short ton of such quartzite or clay used in the production of all refractory products sold during the taxable year shall be equal to 87½ percent of the lesser of—

(A) the average lowest published or advertised price, or

(B) the average lowest actual selling price,

at which, during the taxable year, the mine owner or operator offered to sell, or sold, such quartzite or clay (in the form and

[14] Senate Report No. 692, page 444, this Bulletin; Senate Report No. 868, page 447, this Bulletin; House Report No. 425, page 442, this Bulletin.

condition of such products after the application of only the processes described in paragraph (1) and before transportation from the plant in which such processes were applied). For purposes of this paragraph, exceptional, unusual, or nominal sales or selling prices shall be disregarded. If the mine owner or operator makes no sales of, or makes only exceptional, unusual, or nominal sales of, such quartzite or clay after application of only the processes described in paragraph (1), then in lieu of the price provided for in subparagraph (A) or (B) there shall be used the average lowest recognized selling price for the taxable year for such quartzite or clay in the marketing area of the mine owner or operator published in a trade journal or other industry publication.

(b) YEARS TO WHICH APPLICABLE.—An election made under subsection (c) to have the provisions of this section apply shall be effective on and after January 1, 1951, for all taxable years beginning before January 1, 1961, in respect of which—

(1) the assessment of a deficiency,

(2) the refund or credit of an overpayment, or

(3) the commencement of a suit for recovery of a refund under section 7405 of the Internal Revenue Code of 1954,

is not prevented on the date of the enactment of this Act by the operation of any law or rule of law. Such election shall also be effective on and after January 1, 1951, for any taxable year beginning before January 1, 1961, in respect of which an assessment of a deficiency has been made but not collected on or before the date of the enactment of this Act.

(c) TIME AND MANNER OF ELECTION.—An election to have the provisions of this section apply shall be made by the taxpayer on or before the 60th day after the date of publication in the Federal Register of final regulations issued under authority of subsection (f), and shall be made in such form and manner as the Secretary of the Treasury or his delegate shall prescribe by regulations. Such election, if made, may not be revoked.

(d) STATUTES OF LIMITATIONS.—Notwithstanding any other law, the period within which an assessment of a deficiency attributable to the election under subsection (c) may be made with respect to any taxable year for which such election is effective, and the period within which a claim for refund or credit of an overpayment attributable to the election under such subsection may be made with respect to any such taxable year, shall not expire prior to one year after the last day for making an election under subsection (c). An election by a taxpayer under subsection (c) shall be considered as a consent to the application of the provisions of this subsection.

(e) TERMS; APPLICABILITY OF OTHER LAWS.—Except where otherwise distinctly expressed or manifestly intended, terms used in this section shall have the same meaning as when used in the Internal Revenue Code of 1954 (or corresponding provisions of the Internal Revenue Code of 1939) and all provisions of law shall apply with respect to this section as if this section were a part of such Code (or corresponding provisions of the Internal Revenue Code of 1939).

(f) REGULATIONS.—The Secretary of the Treasury or his delegate shall prescribe such regulations as may be necessary to carry out the provisions of this section.

Approved September 26, 1961.

PUBLIC LAW 87-345
EIGHTY-SEVENTH CONGRESS, OCTOBER 3, 1961
H.R. 2010 [15]

AN ACT to amend title V of the Agricultural Act of 1949, as amended, 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 502(2) of the Agricultural Act of 1949, as amended, is amended to read as follows:

(2) to reimburse the United States for essential expenses incurred by it under this title, except salaries and expenses of personnel engaged in compliance activities, in amounts not to exceed $15 per worker; and.

SEC. 2. Clause (3) of section 503 of such Act is amended to read as follows: "(3) reasonable efforts have been made to attract domestic workers for such employment at wages, standard hours of work, and working conditions comparable to those offered to foreign workers".

SEC. 3. Sections 504 through 509 of such Act are renumbered sections "505" through "510" respectively; the reference to "section 507" in section 508, renumbered as section "509", is changed to section "508"; and the following new section "504" is inserted after section 503:

SEC. 504. No workers recruited under this title shall be made available to any employer or permitted to remain in the employ of any employer—

(1) for employment in other than temporary or seasonal occupations, except in specific cases when found by the Secretary of Labor necessary to avoid undue hardship; or

(2) for employment to operate or maintain power-driven self-propelled harvesting, planting, or cultivating machinery, except in specific cases when found by the Secretary of Labor necessary for a temporary period to avoid undue hardship.

SEC. 4. Section 505 of such Act, as amended, renumbered as section "506", is amended by adding at the end thereof the following:

(d) Workers recruited under the provisions of this title shall not be subject to any Federal or State tax levied to provide illness or disability benefits for them.

SEC. 5. Paragraph (1) of section 507 of such Act, renumbered as section "508", is amended by changing the comma after the words "Internal Revenue Code, as amended" to a period and deleting the remainder of the paragraph.

SEC. 6. Section 509 of such Act, as amended, renumbered as section "510", is amended by striking "December 31, 1961" and inserting "December 31, 1963".

Approved October 3, 1961.

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[15] Senate Report No. 619, page 452, this Bulletin; Conference Report No. 1198, page 457, this Bulletin; since the relevant portions of House Report No. 274 are substantially the same as those contained in the Senate Report, the House Report is not published herein.

PUBLIC LAW 87-370
EIGHTY-SEVENTH CONGRESS, OCTOBER 4, 1961
H.R. 4317 [16]

An Act to amend the Internal Revenue Code of 1954 and incorporate therein provisions for the payment of annuities to widows and certain dependents of the judges of the Tax Court of the United States, and for other purposes.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That subchapter C of chapter 76 of the Internal Revenue Code of 1954 (relating to the Tax Court of the United States) is hereby amended by adding immediately following section 7447 the following new section:

SEC. 7448. ANNUITIES TO WIDOWS AND DEPENDENT CHILDREN OF JUDGES.

(a) DEFINITIONS.—For purposes of this section—

(1) The term "Tax Court" means the Tax Court of the United States.

(2) The term "judge" means the chief judge or a judge of the Tax Court, including any individual receiving retired pay (or compensation in lieu of retired pay) under section 7447 or under section 1106 of the Internal Revenue Code of 1939 whether or not performing judicial duties pursuant to section 7447(c) or pursuant to section 1106(d) of the Internal Revenue Code of 1939.

(3) The term "chief judge" means the chief judge of the Tax Court.

(4) The term "judge's salary" means the salary of a judge received under section 7443(c), retired pay received under section 7447(d), and compensation (in lieu of retired pay) received under section 7447(c).

(5) The term "survivors annuity fund" means the Tax Court judges survivors annuity fund established by this section.

(6) The term "widow" means a surviving wife of an individual, who either (A) shall have been married to such individual for at least 2 years immediately preceding his death or (B) is the mother of issue by such marriage, and who has not remarried.

(7) The term "dependent child" means an unmarried child, including a dependent stepchild or an adopted child, who is under the age of 18 years or who because of physical or mental disability is incapable of self-support.

(b) ELECTION.—Any judge may by written election filed with the chief judge within 6 months after the date on which he takes office after appointment or any reappointment, or within 6 months after the date upon which he first becomes eligible for retirement under section 7447(b), or within 6 months after the enactment of this section, bring himself within the purview of this section, except that, in the case of such an election by the chief judge, the election shall be filed as prescribed by the Tax Court subject to the preceding requirements as to the time of filing.

(c) SALARY DEDUCTIONS.—There shall be deducted and withheld from the salary of each judge electing under subsection (b) a sum equal to 3 percent of such judge's salary. The amounts so deducted and withheld from such judge's salary shall, in accordance with such procedure as may be prescribed by the Comptroller General of the United States, be deposited in the Treasury of the United States to the credit of a fund to be known as the "Tax Court judges survivors annuity fund" and said fund is appropriated for the payment of annuities, refunds, and allowances as provided by this section. Each judge electing under subsection (b) shall be deemed thereby to consent and agree to the deductions from his salary as provided in this subsection, and payment less such deductions shall be a full and complete discharge and acquittance of all claims and demands whatsoever for all judicial services rendered by such judge during the period covered by such payment, except the right to the benefits to which he or his survivors shall be entitled under the provisions of this section.

(d) DEPOSITS IN SURVIVORS ANNUITY FUND.—Each judge electing under subsection (b) shall deposit, with interest at 4 percent per annum to December 31, 1947, and 3 percent per annum thereafter, compounded on December 31 of each year, to the credit of the survivors annuity fund, a sum equal to 3 percent of his judge's salary and of his basic salary, pay, or compensation for service as a

[16] House Report No. 361, page 460, this Bulletin; Senate Report No. 730, page 466, this Bulletin; Conference Report No. 1199, page 474, this Bulletin.

Senator, Representative, Delegate, or Resident Commissioner in Congress, and for any other civilian service within the purview of section 3 of the Civil Service Retirement Act (5 U.S.C. 2253). Each such judge may elect to make such deposits in installments during the continuance of his service as a judge in such amount and under such conditions as may be determined in each instance by the chief judge. Notwithstanding the failure of a judge to make such deposit, credit shall be allowed for the service rendered, but the annuity of the widow of such judge shall be reduced by an amount equal to 10 percent of the amount of such deposit, computed as of the date of the death of such judge, unless such widow shall elect to eliminate such service entirely from credit under subsection (n), except that no deposit shall be required from a judge for any year with respect to which deductions from his salary were actually made under the Civil Service Retirement Act and no deposit shall be required for any honorable service in the Army, Navy, Air Force, Marine Corps, or Coast Guard of the United States.

(e) INVESTMENT OF SURVIVORS ANNUITY FUND.—The Secretary of the Treasury shall invest from time to time, in interest-bearing securities of the United States or Federal farm loan bonds, such portions of the survivors annuity fund as in his judgment may not be immediately required for the payment of the annuities, refunds, and allowances as provided in this section. The income derived from such investments shall constitute a part of said fund for the purpose of paying annuities and of carrying out the provisions of subsections (g), (h), and (j).

(f) CREDITING OF DEPOSITS.—The amount deposited by or deducted and withheld from the salary of each judge electing to bring himself within the purview of this section for credit to the survivors annuity fund shall be credited to an individual account of such judge.

(g) TERMINATION OF SERVICE.—If the service of any judge electing under subsection (b) terminates other than pursuant to the provisions of section 7447 or other than pursuant to section 1106 of the Internal Revenue Code of 1939, the amount credited to his individual account, together with interest at 4 percent per annum to December 31, 1947, and 3 percent per annum thereafter, compounded on December 31 of each year, to the date of his relinquishment of office, shall be returned to him. For the purpose of this section, the service of any judge electing under subsection (b) who is not reappointed following expiration of his term but who, at the time of such expiration, is eligible for and elects to receive retired pay under section 7447 shall be deemed to have terminated pursuant to said section.

(h) ENTITLEMENT TO ANNUITY.—In case any judge electing under subsection (b) shall die while a judge after having rendered at least 5 years of civilian service computed as prescribed in subsection (n), for the last 5 years of which the salary deductions provided for by subsection (c) or the deposits required by subsection (d) have actually been made or the salary deductions required by the Civil Service Retirement Act have actually been made—

(1) if such judge is survived by a widow but not by a dependent child, there shall be paid to such widow an annuity beginning with the day of the death of the judge or following the widow's attainment of the age of 50 years, whichever is the later, in an amount computed as provided in subsection (m); or

(2) if such judge is survived by a widow and a dependent child or children, there shall be paid to such widow an immediate annuity in an amount computed as provided in subsection (m), and there shall also be paid to or on behalf of each such child an immediate annuity equal to one-half the amount of the annuity of such widow, but not to exceed $900 per year divided by the number of such children or $360 per year, whichever is lesser; or

(3) if such judge leaves no surviving widow or widower but leaves a surviving dependent child or children, there shall be paid to or on behalf of each such child an immediate annuity equal to the amount of the annuity to which such widow would have been entitled under paragraph (2) of this subsection had she survived, but not to exceed $480 per year.

The annuity payable to a widow under this subsection shall be terminable upon such widow's death or remarriage. The annuity payable to a child under this subsection shall be terminable upon (A) his attaining the age of 18 years, (B) his marriage, or (C) his death, whichever first occurs, except that if such child is incapable of self-support by reason of mental or physical disability his

annuity shall be terminable only upon death, marriage, or recovery from such disability. In case of the death of a widow of a judge leaving a dependent child or children of the judge surviving her, the annuity of such child or children shall be recomputed and paid as provided in paragraph (3) of this subsection. In any case in which the annuity of a dependent child is terminated under this subsection, the annuities of any remaining dependent child or children, based upon the service of the same judge, shall be recomputed and paid as though the child whose annuity was so terminated had not survived such judge.

(i) DETERMINATION OF DEPENDENCY AND DISABILITY.—Questions of dependency and disability arising under this section shall be determined by the chief judge subject to review only by the Tax Court, the decision of which shall be final and conclusive. The chief judge may order or direct at any time such medical or other examinations as he shall deem necessary to determine the facts relative to the nature and degree of disability of any dependent child who is an annuitant or applicant for annuity under this section, and may suspend or deny any such annuity for failure to submit to any examination so ordered or directed.

(j) PAYMENTS IN CERTAIN CASES.—

(1) In any case in which—

(A) a judge electing under subsection (b) shall die while in office (whether in regular active service or retired from such service under section 7447), before having rendered 5 years of civilian service computed as prescribed in subsection (n), or after having rendered 5 years of such civilian service but without a survivor or survivors entitled to annuity benefits provided by subsection (h), or

(B) the right of all persons entitled to annuity under subsection (h) based on the service of such judge shall terminate before a valid claim therefor shall have been established,

the total amount credited to the individual account of such judge, with interest at 4 percent per annum to December 31, 1947, and 3 percent per annum thereafter, compounded on December 31 of each year, to the date of the death of such judge, shall be paid, upon the establishment of a valid claim therefor, to the person or persons surviving at the date title to the payment arises, in the following order of precedence, and such payment shall be a bar to recovery by any other person:

(i) to the beneficiary or beneficiaries whom the judge may have designated by a writing filed prior to his death with the chief judge, except that in the case of the chief judge such designation shall be by a writing filed by him, prior to his death, as prescribed by the Tax Court;

(ii) if there be no such beneficiary, to the widow of such judge;

(iii) if none of the above, to the child or children of such judge and the descendants of any deceased children by representation;

(iv) if none of the above, to the parents of such judge or the survivor of them;

(v) if none of the above, to the duly appointed executor or administrator of the estate of such judge; and

(vi) if none of the above, to such other next of kin of such judge as may be determined by the chief judge to be entitled under the laws of the domicile of such judge at the time of his death.

Determination as to the widow, child, or parent of a judge for the purposes of this paragraph shall be made by the chief judge without regard to the definitions in subsections (a) (6) and (7).

(2) In any case in which the annuities of all persons entitled to annuity based upon the service of a judge shall terminate before the aggregate amount of annuity paid equals the total amount credited to the individual account of such judge, with interest at 4 percent per annum to December 31, 1947, and 3 percent per annum thereafter, compounded on December 31 of each year, to the date of the death of such judge, the difference shall be paid, upon establishment of a valid claim therefor, in the order of precedence prescribed in paragraph (1).

(3) Any accrued annuity remaining unpaid upon the termination (other than by death) of the annuity of any person based upon the service of a judge shall be paid to such person. Any accrued annuity remaining unpaid upon the death of any person receiving annuity based upon the service of a judge shall be paid, upon the establishment of a valid claim therefor, in the following order of precedence:

(A) to the duly appointed executor or administrator of the estate of such person;

(B) if there is no such executor or administrator payment may be made, after the expiration of thirty days from the date of the death of such person, to such individual or individuals as may appear in the judgment of the chief judge to be legally entitled thereto, and such payment shall be a bar to recovery by any other individual.

(k) PAYMENTS TO PERSONS UNDER LEGAL DISABILITY.—Where any payment under this section is to be made to a minor, or to a person mentally incompetent or under other legal disability adjudged by a court of competent jurisdiction, such payment may be made to the person who is constituted guardian or other fiduciary by the law of the State of residence of such claimant or is otherwise legally vested with the care of the claimant or his estate. Where no guardian or other fiduciary of the person under legal disability has been appointed under the laws of the State of residence of the claimant, the chief judge shall determine the person who is otherwise legally vested with the care of the claimant or his estate.

(l) METHOD OF PAYMENT OF ANNUITIES.—Annuities granted under the terms of this section shall accrue monthly and shall be due and payable in monthly installments on the first business day of the month following the month or other period for which the annuity shall have accrued. None of the moneys mentioned in this section shall be as signable, either in law or in equity, or subject to execution, levy, attachment, garnishment, or other legal process.

(m) COMPUTATION OF ANNUITIES.—The annuity of the widow of a judge electing under subsection (b) shall be an amount equal to the sum of (1) 1¼ percent of the average annual salary received by such judge for judicial service and any other prior allowable service during the last 5 years of such service prior to his death, or prior to his receiving retired pay under section 7447(d), whichever first occurs, multiplied by the sum of his years of judicial service, his years of prior allowable service as a Senator, Representative, Delegate, or Resident Commissioner in Congress, his years of prior allowable service performed as a member of the Armed Forces of the United States, and his years, not exceeding 15, of prior allowable service performed as a congressional employee (as defined in section 1(c) of the Civil Service Retirement Act (5 U.S.C. 2251(c)), and (2) three-fourths of 1 percent of such average salary multiplied by his years of any other prior allowable service, but such annuity shall not exceed 37½ percent of such average annual salary and shall be further reduced in accordance with subsection (d), if applicable.

(n) INCLUDIBLE SERVICE.—Subject to the provisions of subsection (d), the years of service of a judge which are allowable as the basis for calculating the amount of the annuity of his widow shall include his years of service as a member of the United States Board of Tax Appeals and as a judge of the Tax Court, his years of service as a Senator, Representative, Delegate, or Resident Commissioner in Congress, his years of active service as a member of the Armed Forces of the United States not exceeding 5 years in the aggregate and not including any such service for which credit is allowed for the purposes of retirement or retired pay under any other provision of law, and his years of any other civilian service within the purview of section 3 of the Civil Service Retirement Act (5 U.S.C. 2253).

(o) SIMULTANEOUS ENTITLEMENT.—Nothing contained in this section shall be construed to prevent a widow eligible therefor from simultaneously receiving an annuity under this section and any annuity to which she would otherwise be entitled under any other law without regard to this section, but in computing such other annuity service used in the computaton of her annuity under this section shall not be credited.

(p) ESTIMATES OF EXPENDITURES.—The chief judge shall submit to the Bureau of the Budget annual estimates of the expenditures and appropriations necessary for the maintenance and operation of the survivors annuity fund, and such supplemental and deficiency estimates as may be required from time to time for the same purposes, according to law. The chief judge shall cause periodic examinations of the survivors annuity fund to be made by an actuary, who may be an actuary employed by another department of the Government temporarily assigned for the purpose, and whose findings and recommendations shall be transmitted by the chief judge to the Tax Court.

(q) TRANSITIONAL PROVISION.—In the case of a judge who dies within 6 months after the date of enactment of this section after having rendered at least 5 years of civilian service computed as prescribed in subsection (n), but without having

made an election as provided in subsection (b), an annuity shall be paid to his widow and surviving dependents as is provided in this section, as if such judge had elected on the day of his death to bring himself within the purview of this section but had not made the deposit provided for by subsection (d). An annuity shall be payable under this section computed upon the basis of the actual length of serving as a judge and other allowable service of the judge and subject to the reduction required by subsection (d) even though no deposit has been made, as required by subsection (h) with respect to any of such service.

(r) WAIVER OF CIVIL SERVICE BENEFITS.—Any judge electing under subsection (b) shall, at the time of such election, waive all benefits under the Civil Service Retirement Act. Such a waiver shall be made in the same manner and shall have the same force and effect as a waiver filed under section 7447(g)(3).

(s) AUTHORIZATION OF APPROPRIATION.—Funds necessary to carry out the provisions of this section may be appropriated out of any money in the Treasury not otherwise appropriated.

SEC. 2. The table of sections for part I of subchapter C of chapter 76 of the Internal Revenue Code of 1954 is amended by adding at the end thereof the following:

Sec. 7448. Annuities to widows and dependent children of judges.

SEC. 3. (a) Section 403(b) of the Internal Revenue Code of 1954 (relating to taxability of beneficiaries under annuities purchased by section 501(c)(3) organizations) is amended—

(1) by striking out subparagraph (A) of paragraph (1) and inserting in lieu thereof the following:

(A) an annuity contract is purchased—
(i) for an employee by an employer described in section 501(c)(3) which is exempt from tax under section 501(a), or
(ii) for an employee (other than an employee described in clause (i)), who performs services for an educational institution (as defined in section 151(e)(4)), by an employer which is a State, a political subdivision of a State, or an agency or instrumentality of any one or more of the foregoing;

(2) by striking out "the employer described in section 501(c)(3) and exempt from tax under section 501(a)," in paragraph (3) and inserting in lieu thereof the following: "the employer described in paragraph (1)(A),"; and

(3) by inserting before the period in the heading of such subsection the following: "OR PUBLIC SCHOOL".

(b) The amendments made by subsection (a) shall apply with respect to taxable years beginning after December 31, 1957.

Approved October 4, 1961.

PUBLIC LAW 87-397
EIGHTY-SEVENTH CONGRESS, OCTOBER 5, 1961
H.R. 8876 [17]

An Act to amend the Internal Revenue Code of 1954 to permit the use of identifying numbers.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,

(a) IDENTIFYING NUMBERS.—Subchapter B of chapter 61 of the Internal Revenue Code of 1954 (miscellaneous provisions relating to

[17] Senate Report No. 1102, page 475, this Bulletin; since House Report No. 1103 is substantially the same as the Senate Report, it is not published herein.

information and returns) is amended by renumbering section 6109 as section 6110 and inserting after section 6108 the following new section:

SEC. 6109. IDENTIFYING NUMBERS.

(a) SUPPLYING OF IDENTIFYING NUMBERS.—When required by regulations prescribed by the Secretary or his delegate:

(1) INCLUSION IN RETURNS.—Any person required under the authority of this title to make a return, statement, or other document shall include in such return, statement, or other document such identifying number as may be prescribed for securing proper identification of such person.

(2) FURNISHING NUMBER TO OTHER PERSONS.—Any person with respect to whom a return, statement, or other document is required under the authority of this title to be made by another person shall furnish to such other person such identifying number as may be prescribed for securing his proper identification.

(3) FURNISHING NUMBER OF ANOTHER PERSON.—Any person required under the authority of this title to make a return, statement, or other document with respect to another person shall request from such other person, and shall include in any such return, statement, or other document, such identifying number as may be prescribed for securing proper identification of such other person.

(b) LIMITATION.—

(1) Except as provided in paragraph (2), a return of any person with respect to his liability for tax, or any statement or other document in support thereof, shall not be considered for purposes of paragraphs (2) and (3) of subsection (a) as a return, statement, or other document with respect to another person.

(2) For purposes of paragraphs (2) and (3) of subsection (a), a return of an estate or trust with respect to its liability for tax, and any statement or other document in support thereof, shall be considered as a return, statement, or other document with respect to each beneficiary of such estate or trust.

(c) REQUIREMENT OF INFORMATION.—For purposes of this section, the Secretary or his delegate is authorized to require such information as may be necessary to assign an identifying number to any person.

(b) PENALTY FOR FAILURE TO SUPPLY IDENTIFYING NUMBER.—Subchapter B of chapter 68 of such Code (relating to assessable penalties) is amended by adding at the end thereof the following new section:

SEC. 6676. FAILURE TO SUPPLY IDENTIFYING NUMBERS.

(a) CIVIL PENALTY.—If any person is required by regulations prescribed under section 6109—

(1) to include his identifying number in any return, statement, or other document,

(2) to furnish his identifying number to another person, or

(3) to include in any return, statement, or other document made with respect to another person the identifying number of such other person,

fails to comply with such requirement at the time prescribed by such regulations, such person shall pay a penalty of $5 for each such failure, unless it is shown that such failure is due to reasonable cause.

(b) DEFICIENCY PROCEDURES NOT TO APPLY.—Subchapter B of chapter 63 (relating to deficiency procedures for income, estate, and gift taxes) shall not apply in respect of the assessment or collection of any penalty imposed by subsection (a).

(c) TECHNICAL AMENDMENTS.—

(1) The table of sections for subchapter B of chapter 61 of such Code is amended by striking out the last line and inserting in lieu thereof the following:

Sec. 6109. Identifying numbers.
Sec. 6110. Cross references.

(2) The table of sections for subchapter B of chapter 68 of such Code is amended by adding at the end thereof the following:

Sec. 6676. Failure to supply identifying numbers.

(d) EFFECTIVE DATE.—Paragraph (1) of section 6109(a) of the Internal Revenue Code of 1954, as added by subsection (a) of this section, shall apply only in respect of returns, statements, and other documents relating to periods commencing after December 31, 1961. Paragraphs (2) and (3) of such section 6109(a) shall apply only in respect of returns, statements, or other documents relating to periods commencing after December 31, 1962.

Approved October 5, 1961.

SUBPART C.—COMMITTEE REPORTS

[H.R. 5189] [1]

AMENDING THE INTERNAL REVENUE CODE OF 1954 TO EXEMPT FROM TAX INCOME DERIVED BY A FOREIGN CENTRAL BANK OF ISSUE FROM OBLIGATIONS OF THE UNITED STATES

[Senate Report No. 163, Eighty-seventh Congress, First Session, Calendar No. 143]

[April 13, 1961]

MR. BYRD of Virginia, from the Committee on Finance, submitted the following report to accompany H.R. 5189

The Committee on Finance, to whom was referred the bill (H.R. 5189) to amend the Internal Revenue Code of 1954 to exempt from tax income derived by a foreign central bank of issue from obligations of the United States, having considered the same, report favorably thereon with amendments and recommend that the bill as amended do pass.

PURPOSE OF BILL

The House-passed bill provides an exemption from tax for income derived by a foreign contral bank of issue from U.S. Government obligations, but only if the obligations are not held for, or used in connection with, commercial banking functions or other commercial activities. This exemption is to be effective with respect to income received in taxable years beginning after 1960.

This exemption will accord foreign central banks of issue which are separately incorported the same exemption with respect to holdings of U.S. Government obligations as now exists where these obligations are held directly by the foreign government itself. Interest on U.S. bank deposits held by persons not engaged in trade or business in the United States already are free of tax as also are bankers' acceptances held by foreign central banks of issue.

The President of the United States has requested this legislation as one of various desirable steps intended to improve this country's ability to defend its gold reserves. A similar proposal was made by the administration last year but there was not sufficient time for its consideration by Congress. It is anticipated that the bill will have a negligible effect on revenues.

PURPOSE OF COMMITTEE AMENDMENTS

The Committee on Finance added to the House-passed bill an amendment to extend to May 15, 1961, the period in which the spouse of a shareholder in a small business corporation may consent to an election not to be taxed as a corporation. The title of the bill was appropriately amended also.

Under subchapter S, certain small business corporations were permitted to elect not to be taxed as a corporation. The Treasury Department has taken the position that in the case of an election under this section in a community property State, both husband and wife must make the election. In many situations in community property States, the husband operating as a small business corporation made the election but did not have his wife sign the document. Such elections the Treasury now holds are invalid, and as the elections had to be signed within a specified time, the period has expired in which the wife and the husband may now perfect the election. The amendment adopted by the Committee on Finance permits the spouse not signing the election additional time to sign the election. The extended date for perfecting such election is May 15, 1961.

If this amendment is not adopted, many small businessmen in community property States will not be able to take advantage of subchapter S, permitting certain small business corporations not to be taxable as corporations. The amendment only applies where a timely election in the first instance was made by one of the spouses.

[1] Public Law 87-29, page 307, this Bulletin.

GENERAL STATEMENT ON BILL

Under present law (sec. 881 of the Internal Revenue Code) foreign corporations not engaged in a trade or business in the United States generally are subject to a flat 30-percent tax (collected by withholding at the source) on amounts received from sources within the United States in the form of interest, dividends, rents, salaries, and other fixed or determinable amounts. There are, however, several exceptions to this general rule. The principal ones with respect to interest are specified below. First, there is no tax on interest on bank deposits. Also, there is no tax on interest received from resident alien individuals, resident foreign corporations, or domestic corporations where less than 20 percent of the recipient's gross income for the past 3-year period is derived from sources within the United States. Other exceptions to the rules specified above exist in many of the tax treaties the United States has entered into with 21 different foreign countries. Five of these treaties on a reciprocal basis provide for reduced rates of taxation on interest and 10 provide for outright exemption of interest. Of the five providing for reduced rates, a rate of 15 percent is specified in four cases and a rate of 5 percent in the other case.

Still another exception to the general rule described above exists in the case of foreign governments and international organizations of which the United States is a member. Present law (sec. 892) provides that these governments or organizations are completely exempt from tax in the case of income earned from sources within the United States. In addition, present law exempts from tax income derived from bankers' acceptances but only in the case of holdings by foreign central banks of issue. A "foreign central bank of issue" is defined under existing regulations as a bank which is by law or government sanction the principal authority, other than the government itself, issuing instruments intended to circulate as currency. Such a bank is generally the custodian of the banking reserve of the country.

This bill is concerned with the tax treatment of interest on U.S. Government obligations received by these foreign central banks of issue where these banks are not a part of the foreign government itself but instead are separately incorporated and in some cases are not wholly owned by the government. Many of them, for example, organize their central banking somewhat along the lines of our Federal Reserve System. Foreign central banks have increasingly acquired dollar assets as a part of their monetary reserves. These usually take the form of bank deposits, bankers' acceptances, or Treasury bills. As noted above, the United States imposes no tax on this bank deposit interest or on income from bankers' acceptances held by foreign central banks of issue. However, a tax may be imposed with respect to holdings of Treasury bills or other U.S. obligations if the central bank of issue is not a part of the foreign government itself.

Prior to 1946 the Internal Revenue Service held that a foreign corporation which was wholly owned by a foreign government was exempt from tax on income from sources within the United States under the provision exempting foreign governments (sec. 892 of present law). In 1946 the Service reversed its position (I.T. 3789) and held that the tax exemption for a foreign government did not apply to a separate corporation. This reversal of position was based upon the disapproval by the Joint Committee on Internal Revenue Taxation of a tax refund to a corporation incorporated under the laws of the State of New York, the stock of which was wholly owned by a foreign government and which was engaged in commercial activities in this country. The joint committee believed that the exemption from tax for foreign governments did not extend to separate corporations, which may be engaging in commercial activities, even though they are wholly owned by a foreign government. In 1955 the Internal Revenue Service held that the Commonwealth Bank of Australia was entitled to tax exemption as a part of the Australian Government. It was wholly owned by that Government and similar in its functions to our Federal Reserve banks. Upon review of the bank's claim for refund the staff of the Joint Committee on Internal Revenue Taxation disagreed with the position of the Service and recommended that the claim be rejected on the theory that the bank was a separate entity from the Australian Government. It took the position that an entity with the attributes of an ordinary domestic corporation should not be considered a part of a foreign government. As a result, the Service revoked its ruling. However, because of fiscal repercussions anticipated in connection with a shift in U.S. investments of foreign central banks, the revocation of the ruling was suspended after consultations between the staff of the joint committee and

representatives of the Treasury Department to the extent such a bank is not engaged in commercial activities.

This bill settles the problem described above by providing an exemption from income tax for income derived by foreign central banks of issue from obligations of the United States unless the obligations are held for, or used in connection with, the conduct of commercial banking functions or any other commercial activity. It applies to income received in taxable years beginning after December 31, 1960, and thus removes any doubt on this problem as to the future.

Your committee believes that this change is desirable because it will provide uniform tax treatment for investments of the reserve funds of various countries in the case of investments in U.S. obligations. It will remove the present distinction which turns on whether or not the central bank operations are carried on through a separate corporation or directly by the foreign government. Thus, countries which organize their foreign central banks as a separate corporation will no longer be subject to U.S. tax with respect to the return on their holdings of U.S. Government obligations.

Also, in the case of these foreign central banks, this bill is desirable because it will remove a distinction between the treatment provided for income from bank deposits and bankers' acceptances on the one hand and U.S. Government obligations on the other. Thus, no longer will a preference be provided these foreign central banks for their holdings of deposits or bankers' acceptances on the grounds that the return is free of U.S. tax, while the return from Treasury bills or other U.S. Government obligations may be subject to tax.

Of particular importance at the present time is the improved effect that this change can be expected to have on the gold reserves of the United States. This is illustrated by the events of the last year when large volumes of funds seeking short-term investments flowed out of the United States because of temporary higher interest rates in foreign countries. Under these conditions the foreign governments where the funds were invested tended to acquire dollar assets as a result of these investments in order to maintain the strength of the dollar as required by their International Monetary Fund commitments. Once these dollar balances are acquired, they can be converted by the foreign banking authority into gold or into other dollar assets such as bank accounts, bankers' acceptances, or Treasury bills. Conversion of these balances into gold, of course, increases the drain upon the gold reserves of the United States. On the other hand, deposits in U.S. banks, purchases of bankers' acceptances, or purchases of the U.S. Treasury bills do not have this adverse effect. The present tax which may be imposed upon investments in U.S. obligations, however, tends to discourage the purchase of Treasury bills and, therefore, increases the likelihood of conversion into gold.

The exemption provided by the bill will not discriminate against domestic private enterprise because it is limited to U.S. Government obligations held by foreign banks in connection with their central banking functions and is not available in the case of balances held for commercial banking activities or any other commercial activities.

The revenue effect of this proposal is expected to be negligible. It is believed that this will be true because foreign central banks of issue, where the tax is presently applicable, now tend not to hold their reserves in U.S. Government obligations but instead to hold them in gold or in dollar assets, income from which is exempt, such as bank accounts or bankers' acceptances.

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[H.R. 1877] [2]

PLUMBERS UNION LOCAL NO. 12 PENSION FUND

[Senate Report No. 280, Eighty-seventh Congress, First Session, Calendar No. 251]

[May 19, 1961]

MR. BYRD of Virginia, from the committee on Finance, submitted the following report to accompany H.R. 1877.

The Committee on Finance, to whom was referred the bill (H.R. 1877) relating to the effective date of the qualification of Plumbers Union Local No. 12

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[2] This publication of the Committee Report is restricted to excerpts involving internal revenue matters; Public Law 87-59, page 308, this Bulletin.

Pension Fund as a qualified trust under section 401(a) of the Internal Revenue Code of 1954, having considered the same, report favorably thereon with amendments and recommend that the bill as amended do pass.

A. SUMMARY OF HOUSE BILL

The Plumbers Union Local No. 12 Pension Fund, Boston, Mass., for years ending on or after June 3, 1959, has been held to be a qualified trust (under code sec. 401(a)) and to be exempt from taxation (under sec. 501(a)). H.R. 1877 as passed by the House and as approved by your committee provides that this trust also is to be considered a qualified and exempt trust from the time of its establishment in 1954 up until June 3, 1959, but only if it is shown to the satisfaction of the Secretary of the Treasury or his delegate that the trust was not operated in this period in a manner which would jeopardize the interests of its beneficiaries. The effect of this will be to permit employers deductions for their contributions to this trust during this period and to grant the trust an exemption from income tax for income earned in this period.

The Treasury Department has no objection to this provision but if a significant number of additional cases should arise it may prefer general legislation on this problem.

B. SUMMARY OF COMMITTEE AMENDMENTS

1. The first amendment extends for 2 years, 1960 and 1961, the period within which certain stock life insurance companies may make deductible distributions to shareholders (in acquisition of their stock) in pursuance of a plan of mutualization adopted prior to January 1, 1958.

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C. EXPLANATION OF HOUSE BILL

Under present law, a pension trust is qualified for income tax exemption only if it meets certain requirements relating to coverage of employees and nondiscrimination of contributions or benefits. Where the pension trust is properly qualified, not only is it exempt from Federal taxation with respect to its income, but also contributions paid to it by an employer on behalf of his employees are deductible for Federal income tax purposes.

Occasionally it is difficult for a pension trust to achieve qualified status before employer contributions are received by it. This is particularly true in the case of pension plans, such as that of the Plumbers Union Local No. 12, negotiated under collective-bargaining agreements with many employers, both large and small. Often, considerable time is required to obtain sufficient factual data to establish the actuarial soundness of the plan. Sometimes, also, a technicality may prevent initial compliance with the requirements.

Where a pension plan operates for a period as a nonqualified plan before meeting all of the necessary requirements under the Internal Revenue Code, any income it may earn during this period is subject to income tax and any employer contributions made during the period are not deductible.

Last year Congress in seven similar cases (Public Laws 86-779 [C.B. 1960-2, 709] and 86-781 [C.B. 1960-2, 726]) concluded that this loss of exemption for the fund and the denial of deduction for the employer for a past period was too severe a penalty where it was the intention of both the employers and the employees to qualify the fund, but they failed to do so through inadvertence or for technical reasons, and they in fact operated in the same manner as if they had been qualified trusts. Therefore, last year Congress provided in the case of these seven funds that they were to be considered as qualified, and as exempt funds, in the intervening period between their inception and the time they actually qualified for this treatment, but only if the Secretary of the Treasury or his delegate found that they in the interval had not been operated in a manner to jeopardize the interests of the beneficiaries.

This bill provides the same treatment for the Plumbers Union Local No. 12 Pension Fund, Boston, Mass., for the period beginning on September 1, 1954, and ending on June 3, 1959. September 1, 1954, was the date the fund was established by a collective-bargaining agreement and for years ending on or after June 3, 1959, it was held to be a qualified fund. For the specified period from 1954 to 1959, the fund is to be held and considered to have been a qualified

trust under section 401(a) and to have been exempt from taxation under section 501(a), but only if it is shown to the satisfaction of the Secretary or his delegate that the trust did not, during the period referred to, operate in a manner which would jeopardize the interests of the beneficiaries.

D. EXPLANATION OF AMENDMENT RELATING TO CERTAIN MUTUALIZATION DISTRIBUTIONS

Under the Life Insurance Company Income Tax Act of 1959 [P.L. 86-69, C.B. 1959-2, 654], it was provided that in the case of certain stock companies which had adopted a plan of mutualization before January 1, 1958, a special deduction was to be allowed in computing gain from operations (for purposes of the so-called phase 2 tax) of amounts paid by the company to its stockholders in acquisition of their stock under the mutualization plan. A problem was presented by some of the mutualized companies where they did not have funds to spare—over and above funds needed to protect policyholders—to redeem all the stock outstanding at the time they adopted the plan of mutualization. Consequently, these companies had been redeeming their stock gradually out of annual earnings since adoption of their mutualization plan. The purpose of the 1959 act was to make it plain that those stock companies which had adopted a plan of mutualization before January 1, 1958, would be permitted to continue to acquire their stock out of annual earnings and to receive a deduction for amounts so used but only for the 2 years—1958 and 1959. It has developed that at least one of such mutualized companies was unable to complete its mutualization by the end of 1959 and your committee believes it advisable to allow 2 additional years—that is, 1960 and 1961—to complete the plan of mutualization. The amendment is limited to funds actually paid to the shareholders in 1960 and 1961 and does not include accruals paid in subsequent years. The special deduction is also limited to the amount of phase 2 income and is not to be available to any extent to an underwriting loss which may reduce phase 1 income subject to tax.

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[H.R. 6713] [3]

FEDERAL-AID HIGHWAY ACT OF 1961 AND INTERNAL REVENUE CODE AND HIGHWAY TRUST FUND AMENDMENTS

[House of Representatives Report No. 326, Eighty-seventh Congress, First Session]

[May 1, 1961]

MR. FALLON, from the Committee on Public Works, submitted the following report to accompany H.R. 6713.

The Committee on Public Works to whom was referred the bill (H.R. 6713) to amend certain laws relating to Federal-aid highways, to make certain adjustments in the Federal-aid highway program, and for other purposes, having considered the same, report favorably thereon without amendment and recommend that the bill do pass.

INTRODUCTORY STATEMENT

H.R. 6713, which is favorably reported by the committee, contains in title I certain necessary provisions for the continuation of the Federal-aid highway program. Title II of H.R. 6713 contains the recommendations of the Committee on Ways and Means to the Committee on Public Works to provide necessary tax revenues to finance the highway program.

The Committee on Public Works held public hearings on H.R. 5200, which is superseded by title I of the reported bill, on March 21 and 23, 1961, and carefully considered the legislation in executive sessions.

The Committee on Ways and Means recommended material to the Committee on Public Works for inclusion in this legislation as title II which would amend

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[3] This publication of the Committee Report is restricted to excerpts involving internal revenue matters; Public Law 87-61, page 309, this Bulletin.

the Internal Revenue Code of 1954 and the Highway Revenue Acts of 1956 and 1959 to provide additional revenue to make the program self-financing.

The provisions of these two titles have been incorporated in H.R. 6713, after having been approved by the respective committees having jurisdiction over the subject matter in order to permit the simultaneous and orderly consideration of the highway program by Congress.

TITLE I. THE NATIONAL SYSTEM OF INTERSTATE AND DEFENSE HIGHWAYS

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TITLE II. INTERNAL REVENUE CODE AND HIGHWAY TRUST FUND AMENDMENTS

The Committee on Public Works has received the following letter from the Committee on Ways and Means:

COMMITTEE ON WAYS AND MEANS,
HOUSE OF REPRESENTATIVES,
Washington, D.C., May 1, 1961.

HON. CHARLES A. BUCKLEY,
Chairman, Committee on Public Works,
U.S. House of Representatives.

MY DEAR MR. CHAIRMAN: In accordance with the agreement which has been worked out between the Committee on Ways and Means and the Committee on Public Works, I am enclosing the material relative to title II of H.R. 6713, for inclusion in the committee report which your committee will make on that bill to the House of Representatives.

As you know, since the financing provisions of title II are within the jurisdiction of the Committee on Ways and Means, it was agreed that our committee would make the policy decisions on these provisions and draft language carrying out these decisions. This language is embodied in title II of H.R. 6713. The attached material constitutes the report of the Committee on Ways and Means on title II, as well as the minority views with regard to this title.

With kind personal regards, I am,

Sincerely yours,

WILBUR D. MILLS, *Chairman.*

The explanation furnished to the Committee on Public Works by the Committee on Ways and Means is set forth below.

A. SUMMARY

Title II contains the financing provisions for the Federal-aid highway program.

A cost study presented to Congress by the Bureau of Public Roads, Department of Commerce, January 1, 1961, indicated that a total of $37 billion is required to finance to completion the Federal share of the National System of Interstate and Defense Highways now provided by law so as to complete construction in 1972. Present law, after making provision for the A–B–C (primary, secondary, and urban) road program at an annual level of $925 million, provides $27,758 million toward this objective. The additional revenues provided by title II make possible the full financing of the $37 billion Federal share of the Interstate System as well as permitting a gradual increase in the apportionments for the A–B–C program to a level of $1 billion a year. This is accomplished by bringing into the trust fund $9,825 million in revenues in addition to transferring back to the general fund $2,492 million in revenues attributable to passenger car and auto part taxes.

The changes from present law in revenue sources provided by title II are as follows:

(1) The gasoline, special motor fuels, and diesel fuel taxes are continued at the present rate of 4 cents a gallon. These, under present law, are scheduled to revert to 3 cents a gallon as of July 1, 1961.

(2) The taxes on tires for highway-type vehicles and inner tubes are increased to 10 cents a pound while the tax on tread rubber is increased to 5 cents a pound. Presently, the rates of these taxes are 8 cents, 9 cents, and 3 cents, respectively.

(3) The tax on highway vehicles weighing over 26,000 pounds is increased from $1.50 to $3 per 1,000 pounds.

(4) Five additional percentage points of the manufacturers' tax on trucks, buses, and trailers are dedicated to the highway trust fund. This presently is a general fund revenue. The first 5 percentage points of this tax already is a highway trust fund revenue source.

(5) The highway trust fund is continued for an additional 3 months beyond June 30, 1972, and all taxes now dedicated to the fund are continued as highway trust fund revenues at the proposed tax rate levels for the additional 3 months.

(6) The provisions of present law, which would for the 3 fiscal years 1962, 1963, and 1964 divert 5 percentage points of the manufacturers' taxes on passenger cars, etc., and on automobile parts and accessories to the highway trust fund, are repealed. Thus, these taxes in their entirety will remain general fund revenues.

(7) Provision is made in the bill for paying the use tax on highway motor vehicles weighing over 26,000 pounds on a quarterly basis and for the exemption of gasoline from tax where it is sold for nonfuel purposes in the manufacture of another article.

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C. GENERAL EXPLANATION OF THE HIGHWAY FINANCING PROVIDED BY THE BILL

1. *Fuel taxes*

Title II of this bill continues the taxes on gasoline, special motor fuel and diesel fuel in the case of highway use at the present tax of 4 cents a gallon. Without this action these taxes would revert to 3 cents a gallon as of July 1, 1961. Under the bill the 4-cent rate will continue to apply until October 1, 1972.

Table 2 shows estimated revenues to the highway trust fund under existing legislation and the additional revenues provided by this bill. It indicates that revenue collections from these motor fuel taxes under existing legislation over the period from 1957 to 1972 will amount to almost $32 billion. It also shows that the new motor fuel taxes added by this bill are expected to raise revenues of the fund by $8.3 billion, over the period up to October 1, 1972. This represents an annual increase of between $600 and $700 million. This will raise aggregate collections from the fuel taxes over the period 1957 to 1972 to $40.3 billion.

2. *Taxes on tires, tubes, and tread rubber*

The bill also provides an increase in the taxes on tires, tubes, and tread rubber. The present tax on tires of the type used on highway vehicles is 8 cents a pound. The bill raises this rate to 10 cents a pound. The tax on innertubes for tires now is 9 cents a pound and this also is raised by the bill to 10 cents a pound. The present tax on tread rubber is 3 cents a pound. The bill raises this rate to 5 cents a pound. All of these increases are made effective for the period from July 1, 1961, to October 1, 1972.

Table 2 shows that the increases in the taxes on tires, tubes, and tread rubber are expected to increase revenues for the highway trust fund for the period up to 1972 by $1.1 billion. Present law revenues from these taxes for the period 1957 to 1972 will amount to $5.1 billion. Thus, aggregate revenues from these taxes can be expected to amount to about $6.2 billion over the entire period of the trust fund. The additional annual revenues provided by these taxes can be expected to range from $75 to $98 million.

3. *Use tax on motor vehicles*

The third source of new revenue provided by the bill is the increase made in the tax on the use of motor vehicles weighing more than 26,000 pounds. At present this use tax is imposed at the rate of $1.50 per year. The bill raises this to $3 a year effective for the fiscal year beginning July 1, 1961, and continues it at this level until October 1, 1972. The bill also provides for the payment of this use tax in quarterly installments. This installment procedure is described in greater detail in section D below.

Table 2 shows that for the period from 1957 to 1972 the changes made by the Committee on Ways and Means in the motor vehicle use tax will increase revenues by $1,091 million. The tax of $1.50 provided by present law over the period from 1957 to 1972 is shown as resulting in revenue for the fund of $853 million. Although the tax provided by the bill is a 100 percent increase in the

TABLE 2.—*Estimated highway trust fund revenues under present law and revenues added by bill*

Fiscal year	Revenues under present law									Revenues added by bill									Total present and new revenues available under bill
	Gasoline [1] and other motor fuels, 3 cents per gallon	Manufacturers' taxes on—						Truck use tax vehicles over 26,000 pounds $1.50 per 1,000 pounds	Interest	Total revenues available under present law	Gasoline [2] and other motor fuels, 1 cent per gallon	Manufacturers' taxes on—						Truck use tax vehicles over 26,000 pounds $1.50 per 1,000 pounds	Net total revenues added by bill	
		Trucks, buses, and trailers, 5 percent	Tread rubber 3 cents per pound	Tires 8 cents or 5 cents per pound	Inner-tubes, 9 cents per pound	Automobiles 5 percent	Parts and accessories 5 percent					Trucks, buses, and trailers, 5 percent	Tread rubber 2 cents per pound	Tires 2 cents per pound	Inner-tubes, 1 cent per pound	Automobiles less 5 percent	Parts and accessories less 5 percent			
1957	1,326	34	11	82	-------	-------	-------	26	3	1,482	-------	-------	-------	-------	-------	-------	-------	-------	-------	1,482
1958	1,608	111	13	244	17	-------	-------	33	18	2,044	-------	-------	-------	-------	-------	-------	-------	-------	-------	2,044
1959	1,657	107	14	247	15	-------	-------	34	13	2,087	-------	-------	-------	-------	-------	-------	-------	-------	-------	2,087
1960	2,044	142	15	281	19	-------	-------	38	−3	2,536	-------	-------	-------	-------	-------	-------	-------	-------	-------	2,536
1961	2,362	142	15	279	16	-------	-------	45	−2	2,857	-------	-------	-------	-------	-------	-------	-------	-------	-------	2,857
1962	1,894	143	15	286	16	679	131	50	2	3,216	524	143	9	64	2	−679	−131	79	11	3,227
1963	1,869	146	16	291	16	692	137	53	3	3,223	615	146	11	67	2	−692	−137	84	96	3,319
1964	1,917	149	17	296	16	709	144	56	4	3,308	635	149	12	68	2	−709	−144	88	101	3,409
1965	1,965	153	19	301	16	-------	-------	59	4	2,517	649	153	13	69	2	-------	-------	92	978	3,495
1966	2,010	156	19	307	16	-------	-------	61	4	2,573	665	156	14	71	2	-------	-------	95	1,003	3,576
1967	2,054	159	20	313	16	-------	-------	63	4	2,629	679	159	14	72	2	-------	-------	99	1,025	3,654
1968	2,097	162	21	318	16	-------	-------	65	4	2,683	695	162	14	73	2	-------	-------	102	1,048	3,731
1969	2,142	164	22	325	16	-------	-------	66	4	2,739	710	164	14	75	2	-------	-------	103	1,068	3,807
1970	2,191	166	22	331	16	-------	-------	67	4	2,797	727	166	15	76	2	-------	-------	104	1,090	3,887
1971	2,242	169	23	339	16	-------	-------	68	4	2,861	744	169	15	78	2	-------	-------	107	1,115	3,976
1972	2,298	172	24	347	16	-------	-------	69	4	2,930	762	172	16	80	2	-------	-------	108	1,140	4,070
1973 [3]	319	-------	-------	2	-------	-------	-------	-------	-------	321	931	64	11	110	4	-------	-------	30	1,150	1,471
Total	31,995	2,275	286	4,589	243	2,080	412	853	70	42,803	8,336	1,803	158	903	26	−2,080	−412	1,091	9,825	52,628

[1] Tax receipts less refunds. Temporary 4 cent rate, Oct. 1, 1959, through June 30, 1961.
[2] Tax receipts less refunds.
[3] From liabilities accrued prior to July 1, 1972, less floor stock refunds where applicable, under present law; from collections and liabilities accrued prior to Oct. 1, 1972, less floor stock refunds where applicable, under bill.

Source: U.S. Department of Commerce, Bureau of Public Roads.

rate, it will be noted that the revenue increase of $1,091 million is considerably above that which would normally be provided by a 100-percent increase. This is due to the fact that under present law a substantial proportion of tax due in in this case apparently is not now being collected. The Committee on Ways and Means has requested the Treasury Department to report back by the end of this year on practical means of better enforcement for this tax, as well as asking it to consider various other possible modifications governing the liability of taxpayers for this tax. Based upon preliminary discussions which have already occurred with Treasury officials on this problem, the committee believes that it will be possible in the future to obtain substantially greater compliance with this tax and as a result in its estimates it has assumed the tax is collected in full. Also, the weight classifications for trucks now provided in the regulations are to be reviewed and this also may result in changes in the classification which will raise the revenue collected from this tax.

4. *Extension of life of highway trust fund*

The fourth source of revenue provided by the bill is a 3-month extension of the life of the highway trust fund beyond June 30, 1972. Thus, the revenues provided by present law, as well as the new revenues provided under the bill, will continue to be devoted to the highway trust fund until October 1, 1972. This also means that those taxes which otherwise were scheduled to revert to a lower rate or to expire as of June 30, 1972, under the bill will continue at present or proposed rates until October 1, 1972. Thus, the 4-cent tax on gasoline, special motor fuels, and diesel fuel will revert to 1½ cents as of this date. Also, the 10-cent tax on tires of the type used on highway vehicles and on inner tubes will revert to 5 and 9 cents a pound, respectively, as of that date. In addition, as of that date the 5-cent tax on tread rubber will expire as also will the use tax on highway vehicles weighing over 26,000 pounds.

The effect of continuing the highway trust fund for these additional 3 months will be to increase revenues of the highway trust fund by $1,150 million. Thus, as is shown in table 2, all of the $1,471 million expected to be collected in the fiscal year 1973, except the $321 million (shown as revenues under present law) attributable to liability incurred before July 1, 1972, represents new highway trust fund revenue resulting from this extension.

5. *Dedication of truck, etc., tax to fund*

The fifth source of revenue provided by the bill is the dedication of the remaining 5 percentage points of the manufacturers' tax on trucks, buses, and trailers to the highway trust fund. Five percentage points of this tax has been dedicated to this fund since 1957. The bill dedicates the remaining 5 percentage points to the highway trust fund. As indicated in table 2, the highway trust fund is expected to derive $1.8 billion in additional revenue as a result of this additional tax. This, together with the $2.3 billion derived from this source under existing law (over a longer period of time), means that the highway trust fund will derive approximately $4.1 billion from this revenue source over the life of the highway trust fund.

6. *Repeal of provision dedicating auto and parts taxes to fund*

The bill prevents the diversion from the general fund to the highway trust fund of 5 percentage points of the taxes on passenger cars, etc., and on auto parts and accessories. Under present law, as a result of the action taken by Congress in 1959, these taxes (to the extent indicated) would have been dedicated to the highway trust fund for the period beginning July 1, 1961, and ending June 30, 1964. Under the bill these revenues will remain in the general fund. The manufacturers' tax on automobiles would have raised highway trust fund revenues by between $679 and $709 million in each of the 3 years involved. Similarly, the revenue from the manufacturers' tax on auto parts and accessories would have increased highway fund revenues in each of these 3 years in an amount varying from $131 to $144 million. For the 3-year period these taxes would have increased highway trust fund revenues by about $2.5 billion. This loss of revenue to the highway trust fund is more than compensated for by continuing the tax on gasoline at 4 cents and by the other revenue increases referred to above.

7. Effect of changes on apportionments and expenditures

Tables 3 and 4 show the apportionments and expenditures which can be made with the existing and proposed financing for the highway trust fund. The aggregate revenues available for the trust fund under existing legislation for the entire period it is in existence, as shown on table 3, is expected to be $42.8 billion. The estimated total revenue over the life of the highway trust fund after the changes made by the bill is $52.6 billion. This indicates that the bill will increase the revenues of the highway trust fund by $9.8 billion over the period from July 1, 1961, to October 1, 1972, or, on the average, by approximately $875 million in each of these 11¼ years.

Cost estimates submitted to Congress this last January pursuant to provisions of section 104(b)(5) of title 23, United States Code (H. Doc. 49, 87th Cong., 1st sess.), indicate that additional interstate authorizations totaling $11.56 billion are needed for completion of the $37 billion interstate highway program. The President in his message on the highway program also requested that the apportionment for the regular A–B–C systems of primary, secondary, and urban roads now fixed at an annual level of $925 million be increased by $25 million a year every 2 years beginning in 1964 until the $1 billion level is reached and then that these apportionments be maintained at that level. The additional funds required in future years for the step-up in A–B–C expenditures and for emergency relief and special funds are $418 million (the difference between the A–B–C expenditures shown on table 3 and those shown on table 4). This $418 million, plus the $11,560 million of additional funds required by the Interstate System indicates a need for $11,978 million in additional expenditures. This amount is provided under the bill by the trust fund balance (see table 3) of $2,318 million plus new revenues of $9,825 million (see table 4). These sources provide $12,143 million for additional expenditures or $165 million more than the requirement of $11,978 million.

TABLE 3.—*Estimated status of highway trust fund under existing legislation*

[In millions of dollars]

Fiscal year	Apportionments		Expenditures		Revenues	Balance in the fund on June 30
	Interstate	Primary, secondary, and urban [1]	Interstate	Primary, secondary, and urban [1]		
From before 1957	140	965				
1957	1,175	829	208	758	1,482	516
1958	1,700	859	675	836	2,044	1,049
1959	2,200	1,381	1,501	1,112	2,088	524
1960	2,500	906	1,861	1,079	2,535	119
1961	1,800	883	1,901	967	2,857	108
1962	2,200	884	2,078	913	3,216	333
1963	2,000	935	2,278	912	3,223	366
1964	1,500	935	2,141	928	3,308	605
1965	1,500	935	1,838	940	2,517	344
1966	1,600	935	1,670	941	2,573	306
1967	1,700	935	1,673	944	2,629	318
1968	1,900	935	1,705	943	2,683	353
1969	1,900	935	1,795	943	2,739	354
1970	1,625	935	1,746	943	2,797	462
1971		935	1,746	943	2,861	634
1972		935	624	943	2,930	1,997
After 1972					[2] 321	2,318
Total	25,440	16,057	25,440	15,045	42,803	

[1] Includes emergency relief as well as special funds totaling $502,000,000 apportioned for 1959.
[2] Receipts on tax liabilities accrued prior to July 1, 1972.

TABLE 4.—*Estimated status of highway trust fund under proposed legislation*

[In millions of dollars]

Fiscal year	Apportionments		Expenditures		Revenues			Balance in the fund on June 30
	Interstate	Primary, secondary, and urban [1]	Interstate	Primary, secondary, and urban [1]	Present sources	Additional	Total	
From before 1957	140	965						
1957	1,175	829	208	758	1,482		1,482	516
1958	1,700	859	675	836	2,044		2,044	1,049
1959	2,200	1,381	1,501	1,112	2,087		2,087	523
1960	2,500	906	1,861	1,079	2,536		2,536	119
1961	1,800	883	1,901	967	2,857		2,857	108
1962	2,200	884	2,139	913	3,216	11	3,227	283
1963	2,400	930	2,326	898	3,223	96	3,319	378
1964	2,600	955	2,451	927	3,308	101	3,409	409
1965	2,700	955	2,552	923	2,517	978	3,495	429
1966	2,800	980	2,645	932	2,573	1,003	3,576	428
1967	2,900	980	2,739	949	2,629	1,025	3,654	394
1968	3,000	1,005	2,838	958	2,683	1,048	3,731	329
1969	3,000	1,005	2,886	972	2,739	1,068	3,807	298
1970	3,000	1,005	2,901	977	2,797	1,090	3,887	307
1971	2,885	1,005	2,992	979	2,861	1,115	3,976	312
1972		1,005	3,104	966	2,930	1,140	4,070	312
Through Sept. 30, 1972			1,301	317	321	[2] 1,150	1,471	165
Total	37,000	16,532	37,000	15,463	42,803	9,825	52,628	

[1] Includes emergency relief program, as well as special funds totaling $502,000,000 apportioned for 1959.
[2] Includes receipts on tax liabilities accrued prior to Sept. 30, 1972.

D. INSTALLMENT PAYMENTS OF TAX ON THE USE OF HIGHWAY VEHICLES

The bill adds a new provision to the Internal Revenue Code (sec. 6156) providing that those subject to the tax on the use of highway motor vehicles weighing over 26,000 pounds may elect to pay this tax in installments. This provision has been added to title II of the bill because it was recognized that, in the case of truckers operating on quite limited funds, the requirement that this entire tax be paid in one payment works a real financial hardship.

This tax, like other similar taxes imposed by the Federal Government, is imposed on a fiscal year basis beginning July 1. If liability for the tax is first incurred in July, August, or September, the bill permits the tax to be paid in four equal installments. If the liability is first incurred in October, November, or December, it may be paid in three equal installments, and if the liability is first incurred in January, February, or March, it may be paid in two equal installments. If the liability is first incurred in April, May, or June, the installment privilege for payment of the tax is not available.

Under existing regulations, any person incurring liability for this use tax is required to file a return on or before the last day of the next month after that in which the first use of any motor vehicle occurs. (Under this, of course, a taxpayer may be required to file more than one return during the year and under the new provision a separate election to pay an installment may be made with each such return unless the return is filed in the last 3 months of the fiscal year.) Under the bill the first installment of tax is due at the same time the return must be filed. The second installment is due on or before the last day of the third month following the calendar quarter in which liability was incurred. The third installment, if any is due, must be paid on or before the last day of the sixth month following the calendar quarter in which liability was incurred, and the fourth installment, if any is due, must be paid on or before the last day of the ninth month following the calendar quarter in which liability was incurred. The tabulation presented below has been worked out to show the installment due dates described by the bill based on the presently prescribed date for filing the return. This table of payments, it will be noted,

presents a plan for regularizing all payments after the initial payment which, of course, is determined by the month in which liability is first incurred.

If the liability was incurred in—	1st installment is due on or before the last day of—	2d installment is due on or before the last day of—	3d installment is due on or before the last day of—	4th installment is due on or before the last day of—
July	August	December	March	June.
August	September	December	March	June.
September	October	December	March	June.
October	November	March	June	
November	December	March	June	
December	January	March	June	
January	February	June		
February	March	June		
March	April	June		

Where a vehicle subject to this tax is sold during the year, it is possible for two persons to become liable for this tax. However, provision is made to prevent doubling up of tax payments in such cases. The person in whose name the vehicle is registered at the time of the first taxable use incurs liability for the total tax at the time of such first use of the vehicle. This liability is for the total tax even though he elects to pay the tax in installments, and sells the vehicle to another person before the end of the taxable year. Although the first owner of the vehicle is liable for the full payment of the tax (even for installments due after selling the vehicle), if he fails to pay either the total tax or any installment when due, the second owner may be required to pay any tax remaining due. His liability begins in the month in which he is notified of it by the District Director of Internal Revenue. He may then pay the tax in installments if more than 3 months remain in the fiscal year.

Technical provisions added in connection with this installment privilege are similar to those applicable in other cases where taxes are paid in installments. Thus, where any part of a tax is omitted from a return filed by a taxpayer who has elected the installment privilege, this additional tax is prorated equally to all installments, whether paid or unpaid, for which the election has been made. The additional tax prorated to the installments already due must be paid upon notice and demand from the Secretary of the Treasury or his delegate. Also, where a taxpayer fails to pay an installment on or before the date prescribed for payment, the bill provides that the entire unpaid tax must be paid upon notice and demand from the Secretary of the Treasury or his delegate.

Interest on underpayments of installments runs from the due date for the installment. However, where the installment privilege has been terminated, and the time for payment of remaining installments accelerated by the issuance of a notice and demand, interest on these installments runs from the date of the notice and demand. Interest on additional tax prorated as described above is to run from the date prescribed for the payment of the first installment.

E. GASOLINE SOLD FOR USE FOR NONFUEL PURPOSES AS MATERIAL IN MANUFACTURE OF ANOTHER ARTICLE

At the present time petroleum products, other than gasoline, such as methane, pentane, and propane are widely used as raw feed stock by chemical companies in the manufacture of plastics and petrochemicals. Under present law these products when sold for use or used by any person for the propulsion of a motor vehicle, motor boat or airplane are subject to the same 4-cent tax as gasoline. However, when these products are sold to chemical companies for uses such as those referred to above, no tax is applicable. Gasoline, on the other hand, under present law is subject to a 4-cent tax, except that where it is used for nonhighway purposes a 2-cent refund may be claimed.

The chemical companies have found that natural gasoline also is capable of being used in the manufacture of plastics and other petrochemicals. It has been reported to the Committee on Ways and Means that it is an excellent charging stock for petrochemical manufacturing, being suitable to supplement existing chemical raw feed stocks. Pilot plant experiments in the use of casing-head and natural gasoline in the manufacture of plastics and other petrochemicals also have proved successful. However, gasoline has not been used in this manner commercially primarily because of the net 2-cent-a-gallon tax which must be paid.

The Committee on Ways and Means believes that it is unfortunate to in effect prevent the use of gasoline in the manufacture of other nonfuel articles. This is contrary to the policy the committee has followed in generally not taxing articles which are used in the manufacture of other articles.

As a result of these considerations, title II of the bill provides an exemption from the gasoline tax in the case of gasoline sold for use by the purchaser (or his purchaser) for nonfuel purposes as a material in the manufacture of another article to be produced by the purchaser (or second purchaser).

For the exemption to apply, the gasoline must be sold for use as an ingredient of the article being manufactured or produced, as would be the case where it is used as an ingredient in plastics or petrochemicals. The exemption does not apply if the gasoline is consumed in the manufacturing process rather than being an ingredient in the finished product. Thus, for example, gasoline used to power machinery at a plant would not be considered as used as a material in the manufacture or production of an article being manufactured or produced at such a plant.

The phrase "for nonfuel purposes" is intended to make it clear that this exemption does not apply even though the gasoline becomes a component part, or is used as a material in, another article if the gasoline serves as a fuel either by itself, or as a fuel additive to another product. No change in present law is intended in this respect.

The bill also amends the code (sec. 4218) to permit a similar exemption from tax where the producer or importer of the gasoline himself makes a nonfuel use of the gasoline as a material in the manufacture or production of another article. In addition the bill amends the code (sec. 6416(b)(3)) to permit a credit or refund of the tax paid on gasoline where the purchaser uses it for nonfuel purposes as a material in the manufacture or production of another article.

Since gasoline presently is not being used for the purposes described above, and since it appears unlikely that it will be so used so long as the present tax applies, it is believed that this exemption will not result in any loss of revenue. This exemption, or credit, or refund, in the case of gasoline used by a person other than the producer or importer is to apply with respect to gasoline sold on or after October 1, 1961, and in the case of gasoline used by the producer or importer himself is to apply to gasoline used on or after that date.

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[H.R. 6713] [4]

FEDERAL-AID HIGHWAY ACT OF 1961

TITLE II—INTERNAL REVENUE CODE AND HIGHWAY TRUST FUND AMENDMENTS

[Senate Report No. 367, Eighty-seventh Congress, First Session, Calendar No. 335]

[June 12, 1961]

MR. BYRD of Virginia, from the Committee on Finance, submitted the following report . . . to accompany title II of H.R. 6713.

The Committee on Finance, to whom was referred the bill (H.R. 6713) to amend certain laws relating to Federal-aid highways, to make certain adjustments in the Federal-aid highway program, and for other purposes, for consideration of title II thereof, having considered the same, report favorably thereon with amendments and recommended that the bill, as amended, do pass.

I. SUMMARY

Title II contains the financing provisions for the Federal-aid highway program.

A cost study presented to Congress by the Bureau of Public Roads, Department of Commerce, January 12, 1961, indicated that a total of $37 billion is required to finance to completion the Federal share of the National System of

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[4] This publication of the Committee Report is restricted to excerpts involving internal revenue matters; Public Law 87-61, page 309, this Bulletin.

Interstate and Defense Highways now provided by law to complete construction in 1972. Present law, after making provision for the A–B–C (primary, secondary, and urban) road program at an annual level of $925 million, provides $27,758 million toward this objective. The additional revenues provided by title II of the bill as amended by your committee make possible substantially all of the financing of the $37 billion Federal share of the Interstate System as well as permitting a gradual increase in the apportionments for the A–B–C program to a level of $1 billion a year. This is accomplished by bringing into the trust fund $9,367 million in revenues in addition to transferring back to the general fund $2,492 million in revenues attributable to passenger car and auto part taxes.

The changes from present law in revenue sources provided by title II are as follows:

(1) The gasoline, special motor fuels, and diesel fuel taxes under both the House and your committee's versions of the bill are continued at the present rate of 4 cents a gallon. These, under present law, are scheduled to revert to 3 cents a gallon as of July 1, 1961.

(2) The taxes on tires for highway-type vehicles and inner tubes under both versions of the bill are increased to 10 cents a pound. The tax on tread rubber is increased to 5 cents a pound under the House bill and to 4 cents a pound under your committee's amendments. Presently, the rates of these taxes are 8 cents, 9 cents, and 3 cents, respectively.

(3) The tax on highway vehicles weighing over 26,000 pounds in both versions is increased from $1.50 to $3 per 1,000 pounds.

(4) Five additional percentage points of the manufacturers' tax on trucks, buses, and trailers under both versions are dedicated to the highway trust fund. However, under the House bill this dedication begins on July 1, 1961, and under your committee's amendments on July 1, 1962. This presently is a general fund revenue. The first 5 percentage points of this tax already are a highway trust fund revenue source.

(5) The highway trust fund in both versions is continued for an additional 3 months beyond June 30, 1972, and all taxes now dedicated to the fund are continued as highway trust fund revenues at the proposed tax rate levels for the additional 3 months.

(6) The provisions of present law, which would for the 3 fiscal years 1962, 1963, and 1964 divert 5 percentage points of the manufacturers' taxes on passenger cars, etc., and on automobile parts and accessories to the highway trust fund, under both bills are repealed. Thus, these taxes in their entirety will remain general fund revenues.

(7) Provision is made in the bill for paying the use tax on highway motor vehicles weighing over 26,000 pounds on a quarterly basis and for the exemption of gasoline from tax where it is sold for nonfuel purposes in the manufacture of another article.

(8) Your committee has also added an amendment granting to retail dealers of gasoline an allowance equal to 1 percent of the tax paid on gasoline as an allowance for shrinkage or evaporation of the gasoline in their hands.

II. REASONS FOR THE HIGHWAY FINANCING PROVIDED BY THE BILL

1. *Background of problem*

In 1956 Congress enacted a greatly expanded program of Federal aid for interstate highways. At that time Congress decided that this Interstate System, as well as the other Federal-aid highway programs (the so-called A–B–C program), should be separately financed through a special highway trust fund in order to maintain these programs on an independent basis. Such a highway trust fund was established for the 16-year period from June 30, 1956, to July 1, 1972. Into this trust fund were deposited certain highway user excise taxes; namely, all of the taxes on gasoline, diesel fuel, special motor fuel, tread rubber, tires, and inner tubes, and the use tax on highway vehicles. In addition, half of the 10-percent manufacturers' tax on trucks, buses, and trailers was placed in the fund.

A special provision in the Highway Revenue Act of 1956, the so-called Byrd amendment, was designed to give assurance on a year-by-year basis that no deficit would develop in the highway trust fund. This provision requires that before apportionments of Federal-aid highway funds can be made to the States

for the Interstate System, estimates must be made of the revenues expected to be in the fund at the time the expenditures arising from the apportionments can be expected to occur. To the extent that these estimates show that there will be any deficiency in the fund, the Secretary of Commerce is required to reduce the apportionments to the States.

By 1959 it had become apparent that the revenues devoted to the trust fund were insufficient to finance the Interstate System in addition to the regular A–B–C program. The original 1955 estimate of the cost of the Federal share of the Interstate System was $25 billion. This by 1959 had been increased to an estimate of $36 billion. For the most part this increase in cost was due to the fact that the 1955 estimate, because of the hurried manner in which it had to be made, was of necessity a preliminary estimate based upon an incomplete analysis of the cost of the Interstate System. In 1959 Congress was also faced with an immediate deficit in the trust fund for the fiscal year 1960 of $490 million which would have grown to $1,305 million by the end of the fiscal year 1961 if the apportionments already made or planned for those years were to be carried out.

In view of the pressing nature of the immediate financing problems, Congress in 1959 attempted only a temporary solution to the highway financing problems. At that time it provided a 1-cent increase in the gasoline, special motor fuel, and diesel fuel taxes for the period from September 1, 1959, to June 30, 1961. This was expected to provide an increase in trust fund revenues of $1,035 million for this 22-month period. For the fiscal years 1962 through 1964 the bill provided that 5 percentage points of the manufacturers' taxes on passenger cars and automobile parts and accessories were to be dedicated to the trust fund. These funds, which presently are general fund revenues, would have increased highway trust fund revenues by about $2.5 billion and decreased general fund revenues by the same amount.

In addition to the above reasons for concentrating its major effort in 1959 on the short-run financial problem, Congress also was faced with differing points of view as to the proper distribution of the cost of the highway program among various beneficiaries of the program both among various classes of highway users and between highway and nonhighway users. Moreover, at that time relatively little statistical information was available to aid Congress in evaluating the conflicting claims of relative benefit. Congress previously had requested the Bureau of Public Roads to submit to it a study on highway cost allocations, but this study was not then completed. The purpose of this study was to determine what taxes should properly be imposed, and in what amounts, in order to assure, insofar as practicable, an equitable distribution of the tax burden among the various classes of persons using the Federal-aid highways or otherwise deriving benefits from these highways.

The study on highway cost allocations required by section 210 of the Highway Revenue Act of 1956 and also a report on revised costs of completing the highway program now are available. In addition, the President has recommended a new plan for revising the financing of the highway program. In this he has stressed his desire that the passenger car and auto parts and accessories taxes not be diverted from the general fund as is provided by present law for the fiscal years 1962, 1963, and 1964. Instead, he has proposed the continuation to 1972 of the 4-cent tax on gasoline and the increasing of a series of taxes which would be borne primarily by the trucking industry for the period up to June 30, 1972.

2. *Committee amendments*

The bill as amended by your committee for the most part is the same as the House-passed bill. However, it does depart from this bill in three respects. First, it defers for 1 year the transfer of half of the 10-percentage-point tax on the manufacturers sale price of trucks, buses and trailers. Five percentage points of this tax already represents a highway revenue source and the House-passed bill would have transferred the remaining 5 percentage points of this tax to the highway trust fund for the period from July 1, 1961, through September 30, 1972. Your committee's bill provides such a transfer for the period beginning July 1, 1962, and ending on the same date as the House bill. This 1-year delay in the transfer of this tax revenue to the highway trust fund will preserve $143 million of revenues for the general fund for the fiscal year 1962. Thus, for the current budget this will mean that revenues in this respect will be maintained for the general fund at the level planned by the President in his budget message to Congress.

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The transfer for subsequent years of the remaining half of this manufacturers' tax on trucks, etc., to the trust fund can be taken into account in plans for the various budgets as they are prepared in the future. Your committee has been assured that this will not affect apportionments before the fiscal year 1964 and then, of course, only to a minor extent.

The second change made by your committee in the House bill is concerned with the tax on tread rubber. As previously indicated, the House bill would increase this tax from 3 cents a pound to 5 cents a pound. Your committee's amendments provide for a tax of 4 cents a pound. Your committee modified the House bill in this respect because it believed an increase of 33⅓ percent was as large an increase as should be provided in a tax of this type where most of the producers involved are small businesses. It is estimated that this change will decrease the revenues which otherwise would have been provided under the House bill by $4 to $8 million a year.

The third change made by your committee provides that a retail dealer in gasoline is to be compensated for the tax paid on gasoline which is lost by shrinkage or evaporation and other causes to the extent of 1 percent of the tax paid on the gasoline he sells. Since the gasoline tax usually is based on the volume of gasoline the retail dealer purchases, he not only pays tax on the volume of gasoline he resells but also on the gasoline he loses through shrinkage, evaporation, etc. This is a discrimination which many States have recognized and removed by granting retail dealers special shrinkage and evaporation allowances. The allowances provided by various States are shown in table 1. Your committee's bill corrects the present discrimination in the Federal tax base in a similar manner. It is estimated that this will result in a revenue loss of $18 million a year.

TABLE 1.—*States which have adopted refund laws for retailers of gasoline*

	Percent		*Percent*
Georgia	2.0	North Dakota	1.0
Florida	2.0	Utah	1.0
Minnesota	1.0	Wisconsin	.5
Michigan	1.0	Tennessee	.5
New Hampshire	1.0	Colorado	1.0
Idaho	1.0	Texas	.5
Ohio	1.0		

3. *Comparison with President's proposals*

Title II of this bill, as amended by your committee, like the House bill, accepts much of the President's plan for financing the highway program. It stops the transfer of the passenger car and auto parts taxes from the general fund. It continues to 1972 the 4-cent tax on gasoline, special motor fuel, and diesel fuel. It increases the taxes on tires of the type used on highway vehicles and inner tubes to 10 cents a pound. It increases the tax on tread rubber to 4 cents a pound (the House bill would have increased this to 5 cents) and the use tax on trucks weighing over 26,000 pounds to $3 per 1,000 pounds. All of these increases either are the same as recommended by the President or are steps in the direction of his recommendations. A more detailed comparison of the bill as amended by your committee with the President's recommendations and the changes which would be made by the House bill is shown in the next section of this report.

The major difference between both the House and your committee's bills on one hand and the President's recommendations on the other hand is that although the bills increase substantially taxes on truckers, it was not considered appropriate to make the full increase recommended by the administration. In part this conclusion was reached because it believed it would be unfortunate to make so substantial an increase in the costs of the truckers. As is shown in table 2, even with the modest increase made in costs by your committee's bill, the total of existing and proposed road-user taxes will be around 5 percent of total operating costs and may well in many cases exceed the profit margins. In addition, the truckers are faced with substantial State roaduser taxes which, as indicated by table 2, are approximately 1⅓ times the proposed Federal taxload. In addition, restricting the increases in truck taxes is also justified upon analyzing the various means of allocating costs among various classes of highway users. A subsequent section of this report compares the allocation of highway costs provided by this bill with the two principal methods for allocating highway costs among the various classes of highway users; namely, the "incremental" and the "differential benefit" methods.

The nonhighway user benefits which will be derived from the highway program also are impressive. It is believed that these costs justify the dedication of a limited amount of general fund revenues for use of the highway trust fund. The revenues dedicated in this manner by title II of the bill are those derived from the manufacturers' tax on trucks, buses, and trailers, which, of course, is itself a highway user tax. Presently, one-half of this tax already is assigned to the highway trust fund. The bill dedicates the other half to the trust fund as well, although as noted above, this dedication under your committee's amendments is deferred for 1 year.

The highway user cost study suggests that approximately 8 percent of the highway costs are properly attributable to nonhighway users. This represents the portion of the nonhighway use readily subject to measurement. As is indicated in the study, other types of nonhighway benefits are obtained from the highway system which are not capable of measurement.

It is sometimes suggested that this 8-percent charge against nonhighway users already has been recognized by the fact that a substantial amount of revenues were taken from the general fund when the highway trust fund was established. These revenues, shown in table 3 for the period of 1957 to 1961, have amounted to about $6.4 billion. However, the cost of the A–B–C program previously was a charge upon the general fund, and if these revenues are to be considered a "diversion" from the general fund when the A–B–C expenditures should likewise be considered a "diversion" from the general fund. Table 2 shows that these A–B–C expenditures from the trust fund since its inception have amounted to nearly $4.8 billion. Thus, the revenues dedicated to the trust fund exceed this figure only by $1.6 billion. Moreover, the general fund revenues which have been dedicated to the highway trust fund are almost entirely taxes imposed with respect to the highway use and on that basis it can be claimed that they properly are allocable to any road program carried on by the Federal Government. In this connection it should be noted that three highway-user taxes will remain among the general fund revenues. The principal taxes of this type are the 10-percent passenger car tax and the tax on auto parts and accessories. Also, there is the tax on lubricating oil, perhaps half of which is attributable to oils used by motor vehicles.

TABLE 2.—*Estimated operating costs and taxes of selected motor vehicles under committee bill*

[Cents per mile]

Vehicle type	Operating costs excluding road-user taxes	State road-user taxes	Federal motor vehicle taxes [1]		
			Present [2] law	Increase made by committee bill	Combined effect of present law and committee bill
Automobile	8.59	0.62	0.55	0.01	0.56
Single-unit trucks:					
2-axle, 4-tire	22.05	.71	.52	.01	.53
2-axle, 6-tire	24.83	1.24	.89	.02	.91
Combinations with semitrailers:					
3-axle (40,000 pounds gross vehicle weight):					
Gasoline-powered	33.60	2.10	1.37	.17	1.54
Diesel-powered	32.45	1.87	1.21	.17	1.38
4-axle (55,000 pounds gross vehicle weight):					
Gasoline-powered	35.80	2.40	1.63	.18	1.81
Diesel-powered	34.65	2.03	1.37	.18	1.55
5-axle (72,000 pounds gross vehicle weight):					
Gasoline-powered	42.27	3.24	2.11	.24	2.35
Diesel-powered	41.82	2.72	1.72	.24	1.96

[1] Includes all Federal excise taxes on motor fuel, motor vehicles, tires, parts, and accessories, and other taxes closely associated with motor vehicles or their use, whether or not they are dedicated to the highway trust fund.

[2] Present law as in effect for Oct. 1, 1959–June 30, 1961.

Source: U.S. Department of Commerce, Bureau of Public Roads.

TABLE 3.—*Comparison of revenues which would have been available to general fund* [1] *if the interstate program had not been established with expenditures for primary, secondary, and urban (A–B–C) highways, July 1, 1956, to June 30, 1961*

[Millions of dollars]

Fiscal year	Estimated revenue	A–B–C expenditures	Fiscal year	Estimated revenue	A–B–C expenditures
1957	$878	$758	1961	$1,448	[2] $967
1958	1,300	836			
1959	1,330	1,112	Total	6,371	4,752
1960	1,415	1.079			

[1] Based on the following excise tax rates in effect prior to 1956 act:
Gasoline and special motor fuels: 2 cents per gallon, transferred to highway trust fund beginning July 1, 1956.
Trucks, buses, and trailers: 10 percent, of which 2 percentage points was transferred to highway trust fund for the fiscal year 1957 and 3 additional percentage points for subsequent years.
Tires: 5 cents per pound, transferred to highway trust fund beginning July 1, 1957.
Tubes: 9 cents per pound, transferred to highway trust fund beginning July 1, 1957.
[2] Estimated.

Your committee agrees with the House that the factors outlined above justify a modest diversion from the general fund of an amount equal to the remaining half of the truck tax.

A third significant area in which both the House and your committee's bills differ from the President's proposal is in the case of the diesel fuel tax. Both versions of the bill continue this tax at 4 cents a gallon whereas the President's proposal would raise this tax to 7 cents a gallon. Your committee considered this differential rate for diesel fuel, but concluded that such a change would not be desirable in view of the effect it would have in changing the relative competitive position of diesel- and gasoline-powered trucks.

III. GENERAL EXPLANATION OF THE HIGHWAY FINANCING PROVIDED BY THE BILL

Table 4 shows the estimated revenues to the highway trust fund from the House bill and the modifications which your committee's amendments make in these new revenue sources. Table 5 shows the estimated revenues to the highway trust fund under existing legislation and the additional revenues provided by your committee's bill. Table 6 shows the revenue under your committee's bill in greater detail.

1. *Motor fuel taxes*

As indicated in these tables, the taxes on gasoline, special motor fuel and diesel fuel in the case of highway use at present are imposed at a rate of 4 cents a gallon. Without this action these taxes would revert to 3 cents a gallon as of July 1, 1961. Under the House and your committee's action the 4-cent rate will continue to apply until October 1, 1972. The President proposed the same rate of tax as that provided in the bill with respect to gasoline and special motor fuels. In the case of diesel fuels, however, he recommended an increase of the tax rate to 7 cents a gallon. The bill as amended by your committee also provides a special shrinkage or evaporation allowance for gasoline sold by retail dealers. This is discussed in greater detail in section VII below.

The revenue collections from these motor fuel taxes under existing legislation over the period from 1957 to 1972 will amount to almost $32 billion. The new motor fuel taxes added by both the House and your committee's bill are expected to raise revenues of the fund by $8.3 billion, over the period up to 1972. This represents an annual increase of between $600 and $700 million. This will raise aggregate collections from the fuel taxes over the period 1957 to 1972 to $40.3 billion.

2. *Taxes on tires, inner tubes and tread rubber*

The bill also provides an increase in the taxes on tires, tubes, and tread rubber. The present tax on tires of the type used on the highway vehicles is 8 cents a pound. Both versions of the bill raise this rate to 10 cents a pound. The tax on inner tubes for tires now is 9 cents a pound and this also is raised

TABLE 4.—*Comparison of estimated highway revenues under H.R. 6713 and H.R. 6713, as amended by your committee*

[In millions of dollars]

Fiscal year	Gasoline and other motor fuels, 4 cents per gallon			Manufacturers' taxes on—								Truck use tax on vehicles over 26,000 pounds, $3 per 1,000 pounds (both bills)	Interest	Totals		
				Trucks, buses, and trailers			Tread rubber			Tires, 10 cents per pound (both bills)	Inner-tubes, 10 cents per pound (both bills)					
	House bill	Your committee's bill [1]	Difference	House bill, 10 percent of manufacturers' price	Your committee's bill [2]	Difference	House bill, 5 cents per pound	Your committee's bill, 4 cents per pound	Difference					House bill	Your committee's bill	Difference
1962	2,418	2,418		286	143	−143	24	20	−4	350	18	129	2	3,227	3,080	−147
1963	2,484	2,465	−19	292	292		27	21	−6	358	18	137	3	3,319	3,294	−25
1964	2,552	2,533	−19	298	298		29	23	−6	364	18	144	4	3,409	3,384	−25
1965	2,614	2,594	−20	306	306		32	25	−7	370	18	151	4	3,495	3,468	−27
1966	2,675	2,655	−20	312	312		33	26	−7	378	18	156	4	3,576	3,549	−27
1967	2,733	2,713	−20	318	318		34	27	−7	385	18	162	4	3,654	3,627	−27
1968	2,792	2,771	−21	324	324		35	28	−7	391	18	167	4	3,731	3,703	−28
1969	2,852	2,831	−21	328	328		36	29	−7	400	18	169	4	3,807	3,779	−28
1970	2,918	2,896	−22	332	332		37	30	−7	407	18	171	4	3,887	3,858	−29
1971	2,986	2,964	−22	338	338		38	30	−8	417	18	175	4	3,976	3,946	−30
1972	3,060	3,037	−23	344	344		40	32	−8	427	18	177	4	4,070	4,039	−31
1973 [3]	1,250	1,221	−29	64	64		11	6	−5	112	4	30	4	1,475	1,441	−34
Total	31,334	31,098	−236	3,542	3,399	−143	376	297	−79	4,359	202	1,768	45	41,626	41,168	−458

[1] Tax receipts less refunds. H.R. 6713 does not provide for a loss allowance, but H.R. 6713 as amended provides for a "1-percent loss allowance refund."

[2] Half of 10 percent goes to trust fund in fiscal year 1962, all thereafter.

[3] July through September.

Source: U.S. Department of Commerce, Bureau of Public Roads.

TABLE 5.—*Estimated highway trust fund revenues under present law and revenues added by H.R. 6713 as amended by your committee*

[In millions of dollars]

Fiscal year	Revenues under present law										Revenues added by H.R. 6713 as amended by your committee									Total present and new revenues available under bill
	Gasoline and other motor fuels, 3 cents per gallon [1]	Manufacturer's taxes on—						Truck use tax on vehicles over 26,000 pounds, $1.50 per 1,000 pounds	Interest	Total revenues available under present law	Gasoline and other motor fuels, 1 cent per gallon [2]	Manufacturer's taxes on—						Truck use tax on vehicles over 26,000 pounds, $1.50 per 1,000 pounds	Net total revenues added by bill	
		Trucks, buses, and trailers, 5 percent	Tread rubber, 3 cents per pound	Tires, 8 cents or 5 cents per pound	Inner-tubes, 9 cents per pound	Automobiles, 5 percent	Parts and accessories, 5 percent					Trucks, buses, and trailers, 5 percent	Tread rubber, 1 cent per pound	Tires, 2 cents per pound	Inner-tubes, 1 cent per pound	Automobiles, less percent	Parts and accessories, less percent			
1957	1,326	34	11	82				26	3	1,482										1,482
1958	1,608	111	13	244	17			33	18	2,044										2,044
1959	1,657	107	14	247	15			34	13	2,087										2,087
1960	2,044	142	15	281	19			38	−3	2,536										2,536
1961	2,362	142	15	279	16			45	−2	2,857										2,857
1962	1,894	143	15	286	16	679	131	50	2	3,216	524		5	64	2	−679	−131	79	−136	3,080
1963	1,869	146	16	291	16	692	137	53	3	3,223	596	146	5	67	2	−692	−137	84	71	3,294
1964	1,917	149	17	296	16	709	144	56	4	3,308	616	149	6	68	2	−709	−144	88	76	3,384
1965	1,965	153	19	301	16			59	4	2,517	629	153	6	69	2			92	951	3,468
1966	2,010	156	19	307	16			61	4	2,573	645	156	7	71	2			95	976	3,549
1967	2,054	159	20	313	16			63	4	2,629	659	159	7	72	2			99	998	3,627
1968	2,097	162	21	318	16			65	4	2,683	674	162	7	73	2			102	1,020	3,703
1969	2,142	164	22	325	16			66	4	2,739	689	164	7	75	2			103	1,040	3,779
1970	2,191	166	22	331	16			67	4	2,797	705	166	8	76	2			104	1,061	3,858
1971	2,242	169	23	339	16			68	4	2,861	722	169	7	78	2			107	1,085	3,946
1972	2,298	172	24	347	16			69	4	2,930	739	172	8	80	2			108	1,109	4,039
1973 [3]	319			2						321	902	64	6	110	4			30	1,116	1,437
Total	31,995	2,275	286	4,589	243	2,080	412	853	70	42,803	8,100	1,660	79	903	26	−2,080	−412	1,091	9,367	52,170

[1] Gasoline tax receipts less refunds. Temporary 4-cent rate, Oct. 1, 1959, through June 30, 1961.

[2] Gasoline tax receipts less refunds.

[3] From liabilities accrued prior to July 1, 1972, less floor stock refunds where applicable, under present law; from collections and liabilities accrued prior to Oct. 1, 1972, less floor stock refunds where applicable, under bill.

Source: U.S. Department of Commerce, Bureau of Public Roads.

TABLE 6.—*Estimated revenues to the highway trust fund H.R. 6713 as amended by your committee, July 1, 1962, through Sept. 30, 1972*

[In millions of dollars]

Fiscal year	Motor fuel			Trucks and buses, 10 percent manufacturer's price [2]	Tires, 10 cents per pound	Inner-tubes, 10 cents per pound	Tread rubber, 4 cents per pound	Vehicle use, $3 per 1,000 pounds gross vehicle weight	Total
	Gasoline, 4 cents per gallon [1]	Diesel, 4 cents per gallon	Total						
1962	2,325	93	2,418	143	350	18	20	129	3,078
1963	2,362	103	2,465	292	358	18	21	137	3,291
1964	2,418	115	2,533	298	364	18	23	144	3,380
1965	2,470	124	2,594	306	370	18	25	151	3,464
1966	2,523	132	2,655	312	378	18	26	156	3,545
1967	2,574	139	2,713	318	385	18	27	162	3,623
1968	2,626	145	2,771	324	391	18	28	167	3,699
1969	2,679	152	2,831	328	400	18	29	169	3,775
1970	2,738	158	2,896	332	407	18	30	171	3,854
1971	2,800	164	2,964	338	417	18	30	175	3,942
1972	2,865	172	3,037	344	427	18	32	177	4,035
1973 [3]	1,148	73	1,221	64	112	4	6	30	1,437

[1] Includes aviation gasoline; but all refunds, including 1 percent loss allowance refund, have been deducted.
[2] Half to trust fund, half to general fund in fiscal year 1962; all to trust fund thereafter.
[3] July through September.

Source: U.S. Department of Commerce, Bureau of Public Roads.

by the House and your committee's bill to 10 cents a pound. The President in his message proposed increasing the tax on tires and tubes to the same levels.

The present tax on tread rubber is 3 cents a pound. Your committee's bill raises this rate to 4 cents a pound. All of these increases are made effective for the period from July 1, 1961, to October 1, 1972. The President would have raised the tax on tread rubber to 10 cents a pound.

The increases in the taxes on tires, tubes and tread rubber are expected to increase revenues for the highway trust fund for the period up to 1972 by $1 billion under your committee's bill. Present law revenues from these taxes for the period 1957 to 1972 will amount to $5.1 billion. Thus, aggregate revenues from these taxes can be expected to amount to about $6.1 billion over the entire period of the trust fund. The additional annual revenues provided by these taxes can be expected to range from $71 to $90 million. Your committee's action with respect to these taxes raises from $4 to $8 million a year less than the House bill because of the lower tread-rubber tax. Over the period up to 1972 this is expected to amount to $79 million in aggregate.

3. *Use tax on trucks*

The third source of new revenue provided by the bill is the increase made in the tax on the use of motor vehicles weighing more than 26,000 pounds. Both versions of the bill raise this to $3 a year effective for the fiscal year beginning July 1, 1961, and continues it at this level until October 1, 1972. The President has proposed an increase in this tax to the rate of $5 per 1,000 pounds. The bill also provides for the payment of this use tax in quarterly installments. This installment procedure is described in greater detail in section V below.

For the period from 1957 to 1972 the changes made in the motor vehicle use tax will increase revenues by $1,091 million. The tax of $1.50 provided by present law over the period from 1957 to 1972 is shown as resulting in revenue for the fund of $853 million. Although the tax provided by the bill is a 100-percent increase in the rate, it will be noted that the revenue increase of $1,091 is considerably above a 100-percent increase. This is due to the fact that under present law a substantial portion of tax due in this case apparently is not now being collected. The House Committee on Ways and Means has requested the Treasury Department to report back to it by the end of this year on practical means of better enforcement for this tax, as well as asking it to consider various other possible modifications in the regulations governing the liability of taxpayers for this tax. It is believed that it will be possible in the future to obtain substantially greater compliance with this tax and as a result in your committee's estimates it is assuming the tax is collected in full. Also, the

weight classifications for trucks now provided in the regulations are to be reviewed by the House Committee on Ways and Means and this also may result in changes in the classification which will raise the revenue collected from this tax.

4. *Three months' extension of trust fund*

The fourth source of revenue provided by both versions of the bill is a 3-month extension of the life of the highway trust fund beyond June 30, 1972. Thus, the revenues provided by present law, as well as the new revenues provided under the bill, will continue to be devoted to the highway trust fund until October 1, 1972. This also means that those taxes which otherwise were scheduled to revert to a lower rate or to expire as of June 30, 1972, under the bill will continue at present or proposed rates until October 1, 1972. Thus, the 4-cent tax on gasoline, special motor fuels, and diesel fuel will revert to 1½ cents as of this date. Also, the 10-cent tax on tires of the type used on highway vehicles and on inner tubes will revert to 5 and 9 cents a pound, respectively, as of that date. In addition, as of that date the 5-cent tax on tread rubber will expire as also will the use tax on highway vehicles weighing over 26,000 pounds.

The effect of continuing the highway trust fund for these additional 3 months will be to increase revenues of the highway trust fund by $1,150 million. Thus, as is shown on table 5, all of the $1,471 million expected to be collected in the fiscal year 1973, except the $321 million (shown as revenues under present law) attributable to liability incurred before June 30, 1973, represents new highway trust fund revenue resulting from this extension.

5. *Dedication of manufacturers' tax on trucks, etc., to fund*

The fifth source of revenue provided by the bill is the dedication of the remaining 5 percentage points of the manufacturers' tax on trucks, buses, and trailers to the highway trust fund. Five percentage points of this tax has been dedicated to this fund since 1956. The House bill dedicates the remaining 5 percentage points to the highway trust fund beginning July 1, 1961, and your committee's bill, beginning July 1, 1962. The highway trust fund is expected to derive $1.660 billion in additional revenue as a result of this additional tax under your committee's bill ($143 million less than under the House bill). This, together with the $2.3 billion derived from this source under existing law, means that the highway trust fund will derive approximately $3.9 billion from this revenue source over the life of the highway trust fund.

6. *Repeal of provision dedicating auto and parts taxes to fund*

Both versions of the bill prevent the transfer from the general fund to the highway trust fund of 5 percentage points of the taxes on passenger cars, etc., and on auto parts and accessories. Under present law, as a result of the action taken by Congress in 1959, these taxes (to the extent indicated) would have been dedicated to the highway trust fund for the period beginning July 1, 1961, and ending June 30, 1964. Under the bill these revenues will remain in the general fund. This is in conformity with the recommendation of the President. The manufacturers' tax on automobiles would have raised highway trust fund revenues by between $679 and $709 million in each of the 3 years involved. Similarly, the revenue from the manufacturers' tax on auto parts and accessories would have increased revenues in each of these 3 years in an amount varying from $131 to $144 million. For the 3-year period these taxes would have increased highway trust fund revenues by about $2.5 billion. This loss of revenue to the highway trust fund is more than compensated for by continuing the tax on gasoline at 4 cents and by the other revenue increases referred to above.

7. *Further recommendations of the President*

The President in his message on the highway program also requested two further actions affecting the financing of the highway trust fund. He recommended that Congress transfer the financing of the forest and public land highways to the highway trust fund and also that Congress transfer aviation fuel tax receipts to the general fund instead of retaining them in the highway trust fund as is presently done. This action is not taken in either version of this bill. In the case of the forest and public land highways the question arises as to whether these are more properly a charge on the general fund. Leaving these expenditure programs in the general fund has the effect of reducing expenditures which otherwise would have to be made from the highway trust

fund by an estimated $397 million over the period until 1972, an annual effect of $36 or $37 million.

The President in his recent tax message recommended the imposition of a tax on aviation fuel other than gasoline; namely, jet fuel. He would initially impose this jet fuel tax at the rate of 2 cents a gallon. However, he would then provide annual increments in this rate, and also in the rate of the tax on gasoline used by airplanes, of one-half cent a year until "the portion of the cost of the airways properly allocable to civil aviation is substantially recovered by the tax." The House Committee on Ways and Means decided in the case of the aviation fuel presently dedicated to the highway trust fund that it would be desirable to postpone any action on the President's recommendation with respect to removing this from the trust fund until it could consider this larger problem raised by the President with respect to aviation fuel. Removing the aviation fuel from the highway trust fund would have resulted in a decrease in highway trust fund revenues of $164 million, or an annual revenue loss of from $13 to $23 million.

8. *Effect of changes on apportionments and expenditures*

Tables 7, 8, and 9 show the apportionments and expenditures which can be made with the existing, the House, and your committee's provision for financing the highway trust fund. The aggregate revenues available for the trust fund under existing legislation for the entire period it is in existence, as shown on table 7, is expected to be $42.8 billion. The estimated total revenue over the life of the highway trust fund after the changes made by the House bill is $52.6 billion and after changes made by your committee is $52.17 billion. This indicates that your committee's bill will increase the revenues of the highway trust fund by $9.37 billion over the period from July 1, 1961, to September 30, 1972, or, on the average, by approximately $845 million in each of these 11¼ years.

Cost estimates submitted to Congress this last January pursuant to provisions of section 104(b)(5) of title 23, United States Code (H. Doc. 49, 87th Cong., 1st sess.), indicate that additional interstate authorizations totaling $11.56 billion are needed for completion of the $37 billion interstate highway program. The President in his message on the highway program also requested that the apportionment for the regular A–B–C systems of primary, secondary, and urban roads now fixed at an annual level of $925 million be increased by $25 million a year every 2 years beginning in 1964 until the $1 billion level is reached

TABLE 7.—*Estimated status of highway trust fund under existing legislation*

[In millions of dollars]

Fiscal year	Apportionments		Expenditures		Revenues	Balance in the fund on June 30
	Interstate	Primary, secondary, and urban [1]	Interstate	Primary, secondary, and urban [1]		
From before 1957	140	965				
1957	1,175	829	208	758	1,482	516
1958	1,700	859	675	836	2,044	1,049
1959	2,200	1,381	1,501	1,112	2,088	524
1960	2,500	906	1,861	1,079	2,535	119
1961	1,800	883	1,901	967	2,857	108
1962	2,200	884	2,078	913	3,216	333
1963	2,000	935	2,278	912	3,223	366
1964	1,500	935	2,141	928	3,308	605
1965	1,500	935	1,838	940	2,517	344
1966	1,600	935	1,670	941	2,573	306
1967	1,700	935	1,673	944	2,629	318
1968	1,900	935	1,705	943	2,683	353
1969	1,900	935	1,795	943	2,739	354
1970	1,625	935	1,746	943	2,797	462
1971		935	1,746	943	2,861	634
1972		935	624	943	2,930	1,097
After 1972					[2] 321	2,318
Total	25,440	16,057	25,440	15,045	42,803	

[1] Includes emergency relief as well as special funds totaling $502,000,000 apportioned for 1959.
[2] Receipts on tax liabilities accrued prior to July 1, 1972.

TABLE 8.—*Estimated status of highway trust fund under House bill*

[In millions of dollars]

Fiscal year	Apportionments		Expenditures		Revenues			Balance in the fund on June 30
	Interstate	Primary, secondary, and urban [1]	Interstate	Primary, secondary, and urban [1]	Present sources	Additional	Total	
From before 1957	140	965						
1957	1,175	829	208	758	1,482		1,482	516
1958	1,700	859	675	836	2.044		2,044	1,049
1959	2,200	1,381	1,501	1,112	2,087		2,087	523
1960	2,500	906	1,861	1,079	2,536		2,536	119
1961	1,800	883	1,901	967	2,857		2,857	108
1962	2,200	884	2,139	913	3,216	11	3,227	283
1963	2,400	930	2,326	898	3,223	96	3,319	378
1964	2,600	955	2,451	927	3,308	101	3,409	409
1965	2,700	955	2,552	923	2,517	978	3,495	429
1966	2,800	980	2,645	932	2,573	1,003	3,576	428
1967	2,900	980	2,739	949	2,629	1,025	3,654	394
1968	3,000	1,005	2,838	958	2,683	1,048	3,731	329
1969	3,000	1,005	2,886	972	2,739	1,068	3,807	298
1970	3,000	1,005	2,901	977	2,797	1,090	3,887	307
1971	2,885	1,005	2,992	979	2,861	1,115	3,976	312
1972		1,005	3,104	966	2,930	1,140	4,070	312
Through Sept. 30, 1972			1,301	317	321	[2] 1,150	1,471	165
Total	37,000	16,532	37,000	15,463	42,803	9,825	52,628	

[1] Includes emergency relief program, as well as special funds totaling $502,000,000 apportioned for 1959.
[2] Receipts on tax liabilities accrued prior to Sept. 30, 1972.

TABLE 9.—*Estimated status of highway trust fund under your committee's bill*

[In millions of dollars]

Fiscal year	Apportionments		Expenditures		Revenues			Balance in the fund on June 30
	Interstate	Primary, secondary, and urban [1]	Interstate	Primary, secondary, and urban [1]	Present sources	Additional	Total	
From before 1957	140	965						
1957	1,175	829	208	758	1,482		1,482	516
1958	1,700	859	675	836	2,044		2,044	1,049
1959	2,200	1,381	1,501	1,112	2,087		2,087	523
1960	2,500	906	1,861	1,079	2,536		2,536	119
1961	1,800	883	1,901	967	2,857		2,857	108
1962	2,200	884	2,139	913	3,216	−136	3,080	136
1963	2,400	930	2,315	898	3,223	71	3,294	217
1964	[2] 2,500	955	2,408	927	3,308	76	3,384	266
1965	[2] 2,600	955	2,515	923	2,517	951	3,468	296
1966	[2] 2,700	980	2,579	932	2,573	976	3,549	334
1967	[2] 2,800	980	2,654	949	2,629	998	3,627	358
1968	3,000	1,005	2,754	958	2,683	1,020	3,703	349
1969	[3] 3,100	1,005	2,834	972	2,739	1,040	3,779	322
1970	[3] 3,100	1,005	2,935	977	2,797	1,061	3,858	268
1971	[3] 3,085	1,005	3,075	979	2,861	1,085	3,946	160
1972		1,005	3,233	966	2,930	1,109	4,039	
1973			1,413	317	321	1,116	1,437	[4] −293
Total	37,000	16,532	37,000	15,463	42,803	9,367	52,170	

[1] Includes emergency relief program, as well as special funds totaling $502,000,000 apportioned for 1959.
[2] Apportionment of $100,000,000 of fiscal year authorization deferred pursuant to sec. 209(g) of 1956 act.
[3] Includes apportionment of amounts deferred from prior years.
[4] Amount not available in highway trust fund from revenues provided by Senate Finance Committee bill, assumed to be provided from other sources.

and then that these apportionments be maintained at that level. The additional funds required in future years for the step-up in A–B–C expenditures and for emergency relief and special funds are $418 million (the difference between the A–B–C expenditures shown on table 7 and those shown on table 8). This $418 million, plus the $11,560 million of additional funds required by the Interstate System indicates a need for $11,978 million in additional expenditures. The amount provided under your committee bill is the total of the trust balance (see table 7) of $2,318 million plus the new revenues of $9,367 million (see table 9), which is within $293 million of the amount required.

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V. INSTALLMENT PAYMENTS OF TAX ON THE USE OF HIGHWAY VEHICLES

Both versions of the bill add a new provision to the Internal Revenue Code (sec. 6156) providing that those subject to the tax on the use of highway motor vehicles weighing over 26,000 pounds may elect to pay this tax in installments. This provision has been added to title II of the bill because it was recognized that, in the case of truckers operating on quite limited funds, the requirement that this entire tax be paid in one payment works a real financial hardship.

Under existing regulations, any person incurring liability for this use tax is required to file a return on or before the last day of the next month after that in which the first use of any motor vehicle occurs. (Under this, of course, a taxpayer may be required to file more than one return during the year and under the new provision a separate election to pay an installment may be made with each such return unless the return is filed in the last 3 months of the fiscal year.) Under the bill the first installment of tax is due at the same time the return must be filed. The second installment is due on or before the last day of the third month following the calendar quarter in which liability was incurred. The third installment, if any is due, must be paid on or before the last day of the sixth month following the calendar quarter in which liability was incurred, and the fourth installment, if any is due, must be paid on or before the last day of the ninth month following the calendar quarter in which liability was incurred. The tabulation presented below has been worked out to show the installment due dates described by the bill based on the presently prescribed date for filing the return. This table of payments, it will be noted, presents a plan for regularizing all payments after the initial payment which, of course, is determined by the month in which liability is first incurred.

If the liability was incurred in—	1st installment is due on or before the last day of—	2d installment is due on or before the last day of—	3d installment is due on or before the last day of—	4th installment is due on or before the last day of—
July	August	December	March	June.
August	September	December	March	June.
September	October	December	March	June.
October	November	March	June	
November	December	March	June	
December	January	March	June	
January	February	June		
February	March	June		
March	April	June		

Where a vehicle subject to this tax is sold during the year, it is possible for two persons to become liable for this tax. However, provision is made to prevent doubling up of tax payments in such cases. The person in whose name the vehicle is registered at the time of the first taxable use incurs liability for the total tax at the time of such first use of the vehicle. This liability is for the total tax even though he elects to pay the tax in installments, and sells the vehicle to another person before the end of the taxable year. Although the first owner of the vehicle is liable for the full payment of the tax (even for installments due after selling the vehicle), if he fails to pay either the total tax or any installment when due, the second owner may be required to pay any tax remaining due. His liability begins in the month in which he is notified of it by the District Director of Internal Revenue. He may then pay the tax in installments if more than 3 months remain in the fiscal year.

Technical provisions added in connection with this installment privilege are similar to those applicable in other cases where taxes are paid in installments. Thus, where any part of a tax is omitted from a return filed by a taxpayer who has elected the installment privilege, this additional tax is prorated equally to all installments, whether paid or unpaid, for which the election has been made. The additional tax prorated to the installments already due must be paid upon notice and demand from the Secretary of the Treasury or his delegate. Also, where a taxpayer fails to pay an installment on or before the date prescribed for payment, the bill provides that the entire unpaid tax must be paid upon notice and demand from the Secretary of the Treasury or his delegate.

Interest on underpayments of installments runs from the due date for the installment. However, where the installment privilege has been terminated, and the time for payment of remaining installments accelerated by the issuance of a notice and demand, interest on these installments runs from the date of the notice and demand. Interest on additional tax prorated as described above is to run from the date prescribed for the payment of the first installment.

VI. GASOLINE SOLD FOR USE FOR NONFUEL PURPOSES AS MATERIAL IN MANUFACTURE OF ANOTHER ARTICLE

At the present time petroleum products, other than gasoline, such as methane, pentane, and propane are widely used as raw feed stock by chemical companies in the manufacture of plastics and petrochemicals. Under present law these products when sold for use or used by any person for the propulsion of a motor vehicle, motorboat or airplane are subject to the same 4-cent tax as gasoline. However, when these products are sold to chemical companies for uses such as those referred to above, no tax is applicable. Gasoline, on the other hand, under present law is subject to a 4-cent tax, except that where it is used for nonhighway purposes a 2-cent refund may be claimed.

The chemical companies have found that natural gasoline also is capable of being used in the manufacture of plastics and other petrochemicals. It has been reported that it is an excellent charging stock for petrochemical manufacturing, being suitable to supplement existing chemical raw feed stocks. Pilot plant experiments in the use of casinghead and natural gasoline in the manufacture of plastics and other petrochemicals also have proved successful. However, gasoline has not been used in the manner commercially primarily because of the net 2-cent-a-gallon tax which must be paid.

Your committee believes that it is unfortunate to in effect prevent the use of gasoline in the manufacture of other nonfuel articles. This is contrary to the policy the Congress has followed in generally not taxing articles which are used in the manufacture of other articles.

As a result of these considerations, title II of both versions of the bill provides an exemption from the gasoline tax in the case of gasoline sold for use by the purchaser (or his purchaser) for nonfuel purposes as a material in the manufacture of another article to be produced by the purchaser (or second purchaser).

For the exemption to apply, the gasoline must be sold for use as an ingredient of the article being manufactured or produced, as would be the case where it is used as an ingredient in plastics or petrochemicals. The exemption does not apply if the gasoline is consumed in the manufacturing process rather than being an ingredient in the finshed product. Thus, for example, gasoline used to power machinery at a plant would not be considered as used as a material in the manufacture or production of an article being manufactured or produced at such a plant.

The phrase "for nonfuel purposes" is intended to make it clear that this exemption does not apply even though the gasoline becomes a component part, or is used as a material in, another article if the gasoline serves as a fuel either by itself, or as a fuel additive to another product. No change in present law is intended in this respect.

The bill also amends the code (sec. 4218) to permit a similar exemption from tax where the producer or importer of the gasoline himself makes a nonfuel use of the gasoline as a material in the manufacture or production of another article. In addition, the bill amends the code (sec. 6416(b)(3)) to permit a credit or refund of the tax paid on gasoline where the purchaser uses it for nonfuel purposes as a material in the manufacture or production of another article.

Since gasoline presently is not being used for the purposes described above, and since it appears unlikely that it will be so used so long as the present tax

applies, it is believed that this exemption will not result in any loss of revenue. This exemption, or credit, or refund, in the case of gasoline used by a person other than the producer or importer is to apply with respect to gasoline sold on or after October 1, 1961, and in the case of gasoline used by the producer or importer himself is to apply to gasoline used on or after that date.

VII. PAYMENTS TO RETAILERS FOR GASOLINE TO COMPENSATE FOR TAX LOST BY SHRINKAGE, EVAPORATION, ETC.

Your committee has added an amendment to the bill providing that retail dealers of gasoline are to be compensated for the tax paid on gasoline which is lost by shrinkage, evaporation, or other causes. The payment is to be 1 percent of the gasoline tax on the gasoline sold by the dealer.

Under present law the Federal tax on gasoline is imposed on the producer, importer or wholesale distributor of the gasoline and is payable shortly after he makes his sale. Thus, for the producer, importer, or wholesale distributor losses through shrinkage or evaporation, etc., while the gasoline is in his possession do not result in the payment of tax on a larger amount than that sold. In the case of a retail dealer, however, since the tax is usually imposed on the person from whom he makes the purchase, any amount of gasoline he loses is tax-paid gasoline. In the past, when the tax was imposed only on the producer or importer, Congress recognized that this type of treatment discriminated against wholesale distributors and as a result in 1959 permitted these distributors to buy gasoline on a tax-free basis and pay the tax at the time they made their sale. It is not practical, however, to collect the gasoline tax from each of the many retail gasoline dealers, however, at the time they make their sales. As a result, in order to remove this discrimination in the case of retail dealers, your committee's amendment, in lieu of imposing a tax at the retail level, grants the 1 percent shrinkage allowance to the dealers.

Claims for payment of this allowance are to be filed on an annual basis for the year ending June 30. The claims must be filed within 3 months of the end of such a year.

No allowance is to be paid to any retail dealer for gasoline sold by him if the Treasury Department determines the gasoline was exempt from the gasoline tax, the tax is refundable to any one, or with respect to gasoline used on farms or gasoline used for certain nonhighway purposes of by local transit systems (under sec. 6421). Also, no allowance is to be paid to a retail dealer for gasoline sold by him to another dealer including a wholesale dealer or distributor of gasoline.

This allowance with respect to shrinkage, evaporation, etc., is to be available only with respect to gasoline sold by retail dealers after June 30, 1961.

Since all of the receipts from the gasoline tax are appropriated to the highway trust fund, provision is made for reimbursement of the general fund of the Treasury by the highway trust fund for these allowances paid to retail dealers.

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[H.R. 6713] [5]

FEDERAL-AID HIGHWAY ACT OF 1961

[Conference Report No. 564, Eighty-seventh Congress, First Session]

[June 22, 1961]

MR. FALLON, from the Committee of Conference, submitted the following Conference Report to accompany H.R. 6713.

The committee of conference on the disagreeing votes of the two Houses on the amendments of the Senate to the bill (H.R. 6713) to amend certain laws relating to Federal-aid highways, to make certain adjustments in the Federal-aid highway program, and for other purposes, having met, after full and free conference, have agreed to recommend and do recommend to their respective Houses as follows:

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[5] This publication of the Conference Report is restricted to excerpts involving internal revenue matters; Public Law 87-61, page 309, this Bulletin.

TITLE II

The managers on the part of the House and the managers on the part of the Senate as to title II of the bill having met, after full and free conference, have agreed to recommend and do recommend to their respective Houses as follows:

That the Senate recede from its amendments numbered 4, 5, 6, 8, 12, 15, 16, and 17.

That the House recede from its disagreement to the amendments of the Senate numbered 7, 9, 10, 11, 13, and 14, and agree to the same.

W. D. MILLS,
CECIL R. KING,
THOS. J. O'BRIEN,
N. M. MASON,
JOHN W. BYRNES,
Managers on the Part of the House.
HARRY F. BYRD,
ROBT. S. KERR,
RUSSELL LONG,
JOHN J. WILLIAMS,
FRANK CARLSON,
Managers on the Part of the Senate.

STATEMENT OF THE MANAGERS ON THE PART OF THE HOUSE

The managers on the part of the House at the conference on the disagreeing votes of the two Houses on the amendments of the Senate to the bill (H.R. 6713) to amend certain laws relating to Federal-aid highways, to make certain adjustments in the Federal-aid highway program, and for other purposes, submit the following statement in explanation of the effect of the action agreed upon by the conferees and recommended in the accompanying conference report:

* * * * * * *

TITLE II

The managers on the part of the House as to title II of the bill submit the following statement in explanation of the effect of the action agreed upon by the conferees as to title II of the bill and recommended in the accompanying conference report:

TREAD RUBBER

Amendments Nos. 4 and 8: The House bill increased the tax on tread rubber by 2 cents a pound (from 3 cents a pound to 5 cents a pound). Senate amendment No. 4 limits the increase to 1 cent a pound (that is, the existing tax rate of 3 cents a pound is increased to 4 cents a pound). Senate amendment No. 8 is a related conforming amendment reducing the floor stocks tax on tread rubber held by a dealer on July 1, 1961, from 2 cents a pound to 1 cent a pound. The Senate recedes.

GASOLINE LOST BY SHRINKAGE, ETC.

Amendments Nos. 5, 6, 12, 15, 16, and 17: Senate amendment No. 5 provides for payments to compensate retail dealers of gasoline for tax paid on gasoline lost by shrinkage, evaporation, and so forth. Under the amendment, the retail dealer would be entitled to an amount equal to 1 percent of the tax paid under section 4081 of the 1954 Code on gasoline sold by him. Senate amendments Nos. 6, 12, 15, 16, and 17 are related conforming clerical, technical, and effective date amendments. The Senate recedes.

In connection with the action of the conferees on these amendments the Treasury Department has been requested to conduct, in cooperation with other appropriate agencies of the Federal Government, a scientific study for the purpose of obtaining data on the percentage of the gasoline bought by retail dealers which is lost by shrinkage or evaporation or for other causes. Representatives of the Treasury Department have given assurances that this study will be conducted. The results of this study are to be reported to the Ways and Means Committee of the House of Representatives and to the Committee on Finance of the Senate before January 1, 1962.

INNER TUBES FOR BICYCLE TIRES

Amendments Nos. 7, 9, 10, and 11: Amendment No. 7 provides that the floor stocks tax of 1 cent a pound imposed on inner tubes held by dealers, etc., on July 1, 1961, for sale or use is not to apply to inner tubes for bicycle tires. Similarly, amendment No. 11 provides that the floor stock refund of 1 cent a pound provided for inner tubes held by dealers, etc., on October 1, 1972, for sale or use is not to apply to inner tubes for bicycle tires. Amendments Nos. 9 and 10 are related clerical amendments. The House recedes.

TRANSFERS TO HIGHWAY TRUST FUND

Amendments Nos. 13 and 14: Section 209(c)(1)(C) of the Highway Revenue Act of 1956 at present provides that there shall be transferred to the highway trust fund amounts equivalent to 50 percent of the tax received under section 4061(a)(1) of the 1954 Code (that is, the tax on trucks, buses, etc.). The House bill amended this provision so that, in the case of amounts so received after June 30, 1961, the percentage transferred is to be 100 percent instead of 50 percent. Under Senate amendments Nos. 13 and 14, the change in the percentage from 50 percent to 100 percent is delayed 1 year and applies only to tax received after June 30, 1962. The House recedes.

W. D. MILLS,
CECIL R. KING,
THOS. J. O'BRIEN,
N. M. MASON,
JOHN W. BYRNES,
Managers on the Part of the House.

[H.R. 6027] [6]
SOCIAL SECURITY AMENDMENTS OF 1961

[Senate Report No. 425, Eighty-seventh Congress, First Session]

[June 20, 1961]

MR. BYRD OF VIRGINIA, from the Committee on Finance, submitted the following report to accompany H.R. 6027.

I. SCOPE OF THE BILL

H.R. 6027, as reported by the committee, affects both the old-age, survivors, and disability insurance program and the public assistance program.

As to the insurance program the reported bill is generally the same as that passed by the House of Representatives, which adopted the proposals of the President but reduced them somewhat in scope. Certain other minor provisions have also been added relating to extension of coverage. Passage of the bill will mean that within the first 12 months about 4,420,000 people will get new or increased benefits amounting to $780 million.

As to the public assistance program, the committee increased the Federal matching maximum for old-age assistance, aid to the blind, and aid to the permanently and totally disabled.

The committee also has authorized the expenditure of Federal funds for temporary assistance to certain U.S. nationals who have returned from foreign countries and are without immediately available resources.

II. SUMMARY OF THE PRINCIPAL PROVISIONS OF THE BILL

A. OLD-AGE, SURVIVORS, AND DISABILITY INSURANCE

The committee accepted the provisions of the House approved bill which increases the minimum benefit, provides benefits for men at age 62, liberalizes the insured status requirement, increases the widow's benefit, and relates to the establishment of periods of disability. These liberalizations would be financed

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[6] Public Law 87-64, page 315, this Bulletin.

by an appropriate increase in the tax rates so that the program will continue to be self-supporting and on a sound actuarial basis.

1. Increase in the minimum benefit

The bill would increase from $33 to $40 the minimum monthly retirement benefit payable under the program to persons retiring at or after age 65 and the minimum monthly disability benefit, with proportionate increases in the minimum benefits payable to dependents and survivors. This provision would mean increased benefits for 2,175,000 people, amounting to $170 million, during the first 12 months of operation.

2. Benefits at age 62 for men

The bill would make benefits available for men beginning at age 62, with the benefits payable to men claiming them before age 65 reduced to take account of the longer period over which the benefits will be paid. The effect of this change would be that men electing to retire at age 62 will receive the same total amount of benefits over the remainder of their lives as they would have received had they waited to retire at age 65.

In the first year of operation, about 560,000 people would get benefits amounting to $440 million under this proposed change.

3. Liberalization of the insured status requirements

The bill would liberalize the insured status requirements so that a worker would be fully insured for benefit purposes if he has one quarter of coverage for every year elapsing after 1950 (or after the year in which he attained age 21, if that was later) and up to the year of disability, death, or attainment of age 65 for men (62 for women). Under present law one quarter of coverage is required for every three elapsed calendar quarters.

This change would bring about 160,000 people onto the benefit rolls in the first year for a total of $65 million in benefits.

4. Increase in widow's, widower's, and parent's benefits

The bill would increase aged widow's, widower's and surviving parent's benefit from 75 to 82½ percent of the workers' retirement benefit—a 10-percent increase in benefits for these people.

This provision would increase benefits for 1,525,000 people by $105 million in the first 12 months of operation.

5. Establishing a period of disability

The bill extends for 1 year—to June 30, 1962—the period within which a person may file an application for establishing a period of disability for purposes of determining eligibility for, and the amount of, old-age, survivors, and disability insurance benefits, and have the period begin as early as the time when his disability began.

6. Facilitation of coverage for certain State and local employees, and certain ministers

The committee added a provision to the House-approved bill which modifies the so-called divided system coverage of employees under State and local retirement systems so that (1) New Mexico would be added to the list of States who are permitted this method of coverage and (2) those employees who originally had chosen not to come under the program would be given an additional chance to elect to be in the group which has coverage.

Likewise, the provision in present law which permits ordained ministers to elect coverage before April 16, 1962, would be modified by the committee bill so that, in the case of a minister who died before this date without making such an election, his widow or other survivor beneficiary would be able to make the election within the original time period prescribed.

7. Effective dates

The benefit provisions of the bill will be effective generally for the 1st month that begins on or after the 30th day after the bill is enacted.

8. Increase in tax rates

To meet the increased cost incurred as a result of the improvements in the old-age, survivors, and disability insurance program which would be made by

the bill, provision is made for an increase in the scheduled contribution rates. The bill provides that, beginning in 1962, contribution rates would be raised by one-eighth of 1 percent each for employees and employers and by approximately three-sixteenths of 1 percent for the self-employed. This means that the improvements would be fully financed and the system would remain actuarially sound.

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III. GENERAL DISCUSSION

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*6. Facilitation of coverage for * * * certain ministers.*

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(c) *Giving survivors of certain ministers opportunity to elect coverage.*—The 1960 amendments provided an extension of the time provided for ministers to elect old-age and survivors, and disability insurance coverage up to April 16, 1962. Under a provision added to the bill by the committee, the survivors of ministers (or Christian Science practitioners) who die on or after the date of enactment of the 1960 amendments (September 13, 1960) and before April 16, 1962, would be eligible to take advantage of this extension. Such a survivor, as in the case of the minister himself had he lived, would have the opportunity through April 15, 1962, to file a certificate electing coverage of services performed by the minister before his death. A certificate filed by a survivor would be effective generally to cover the minister's services retroactively for 1 year just as if the certificate had been filed by the minister himself on the date of his death.

Under present law a waiver certificate may not be filed on behalf of a minister after his death. Thus, if a minister dies without electing coverage there is no way for his family to secure old-age, survivors, and disability insurance protection. The committee believes that a minister's family should not be deprived of social security benefits because the minister died before he had a full opportunity to exercise his right to elect coverage under the 1960 legislation.

7. Increase in tax rates

It is essential that the old-age, survivors, and disability insurance program remain soundly financed. The Congress has established the policy that the tax schedule in the law should make the system fully self-supporting and keep it actuarially sound. Consistent with this policy, the increase in the bill for employees and employers would be one-eighth of 1 percent each. The rate for the self-employed was, under the House-approved bill, 1½ times the rate for employees; or, in other words, the rate is increased by three-sixteenths of 1 percent. The fractions resulting from an increase of three-sixteenths of 1 percent will, in the committee's opinion, make it difficult for self-employed people to compute their taxes. Therefore, in the committee bill the rates for the self-employed are expressed in decimals, rounded to the nearest tenth of 1 percent.

The new tax schedule would be as follows:

Years	Rate for employees and employers	Rate for self-employed
	Percent	*Percent*
1962	3⅛	4.7
1963 to 1965	3⅝	5.4
1966 to 1968	4⅛	6.2
1969 and later	4⅝	6.9

* * * * * * *

IV. SECTION-BY-SECTION ANALYSIS

The first section of the bill provides that it may be cited as the "Social Security Amendments of 1961."

The remainder of the bill is divided into three titles and eight sections as follows:

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TITLE II—AMENDMENTS TO THE INTERNAL REVENUE CODE OF 1954

Sec. 201. Changes in tax schedules.
Sec. 202. Extension of time to elect coverage on behalf of ministers.

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TITLE II—AMENDMENTS TO THE INTERNAL REVENUE CODE

SEC. 201. CHANGES IN TAX SCHEDULES

Section 201 of the bill increases the rates of taxes under the Self-Employment Contribution Act of 1954 (ch. 2 of the Internal Revenue Code of 1954) and the Federal Insurance Contributions Act (ch. 21 of such code). Each rate provided by existing law for the employer tax and the employee tax under the Federal Insurance Contributions Act is increased by one-eighth percent, effective with respect to remuneration paid after 1961. Each rate provided by existing law for the self-employment tax is increased by three-sixteenths percent and rounded to the nearest tenth of 1 percent, effective for taxable years beginning after December 31, 1961.

The following tables illustrate the proposed changes in rates:

Self-employment tax rates

	Existing law (percent)	Proposed (percent)
1962	4½	4.7
1963 to 1965, inclusive	5¼	5.4
1966 to 1968, inclusive	6	6.2
1969 and after	6¾	6.9

Employer tax and employee tax rates (each)

	Existing law (percent)	Proposed (percent)
1962	3	3⅛
1963 to 1965, inclusive	3½	3⅝
1966 to 1968, inclusive	4	4⅛
1969 and after	4½	4⅝

SEC. 202. EXTENSION OF TIME TO ELECT COVERAGE ON BEHALF OF MINISTERS

Section 202(a) of the bill amends section 1402(e) of the Internal Revenue Code of 1954 by adding at the end thereof a new paragraph numbered (6). Under the new paragraph in any case where a minister or Christian Science practitioner dies after September 12, 1960, and before April 16, 1962, his survivor or the fiduciary of his estate may file a certificate, on or before April 15, 1962, electing to have the services of the minister or Christian Science practitioner covered under title II of the Social Security Act. Such a certificate would be effective for the period prescribed in existing law as if filed by the minister or Christian Science practitioner on the date of his death.

Section 202(b) of the bill provides the effective date for the amendment contained in section 202(a) of the bill. The amendment is to apply on the date of enactment of the bill but no monthly benefits shall be payable or increased by reason of such amendment for the month in which the bill is enacted or any prior month and no lump-sum death payment shall be payable or increased by reason of such amendment in the case of any individual who died prior to the date of enactment of the bill.

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[H.R. 6027] [7]

SOCIAL SECURITY AMENDMENTS OF 1961

[Conference Report No. 611, Eighty-seventh Congress, First Session]

[June 28, 1961]

MR. MILLS, from the committee of conference, submitted the following conference report to accompany H.R. 6027.

The committee of conference on the disagreeing votes of the two Houses on the amendments of the Senate to the bill (H.R. 6027) to improve benefits under the old-age, survivors, and disability insurance program by increasing the minimum benefits and aged widow's benefits and by making additional persons eligible for benefits under the program, and for other purposes, having met, after full and free conference, have agreed to recommend and do recommend to their respective Houses as follows:

That the Senate recede from its amendment numbered 11.

That the House recede from its disagreement to the amendments of the Senate numbered 1, 2, 3, 4, 5, 6, 7, 8, 9, 10, 13, 14, 15, 16, 17, 18, 19, 20, 21, 22, 23, and 26, and agree to the same.

* * * * * * *

W. D. MILLS,
CECIL R. KING,
THOS. J. O'BRIEN,
N. M. MASON,
JOHN W. BYRNES,
Managers on the Part of the House.

HARRY F. BYRD,
ROBT. S. KERR,
RUSSELL B. LONG,
JOHN J. WILLIAMS,
FRANK CARLSON,
Managers on the Part of the Senate.

STATEMENT OF THE MANAGERS ON THE PART OF THE HOUSE

The managers on the part of the House at the conference on the disagreeing votes of the two Houses on the amendments of the Senate to the bill (H.R. 6027) to improve benefits under the old-age, survivors, and disability insurance program by increasing the minimum benefits and aged widow's benefits and by making additional persons eligible for benefits under the program and for other purposes, submit the following statement in explanation of the effect of the action agreed upon by the conferees and recommended in the accompanying conference report:

* * * * * * *

Amendments Nos. 13, 14, 16, and 18: Section 201(a) of the House bill amends section 1401 of the Internal Revenue Code of 1954 to increase the rates of tax under the Self-Employment Contributions Act of 1954. Each rate provided by existing law for the self-employment tax is increased by three-sixteenths of 1 percent. Senate amendments Nos. 13, 14, 16, and 18 round these rates to the nearest one-tenth of 1 percent. The House recedes.

Amendments Nos. 15 and 17: Under existing law, an increase in the rate of the tax under the Self-Employment Contributions Act of 1954 is scheduled for taxable years beginning after December 31, 1968. Senate amendments Nos. 15 and 17 provide that this increase in the rate of tax, as modified by the House bill and by Senate amendment No. 18, is to apply to taxable years beginning after December 31, 1967. Under the conference agreement, the rate of such tax for taxable years beginning after December 31, 1967, will be 6.9 percent. The House recedes.

Amendments Nos. 19, 20, 21, and 22: Under existing law, an increase in the rate of tax for employers and employees under the Federal Insurance Contributions Act is scheduled to take effect for calendar year 1969 and subsequent

[7] Public Law 87-64, page 315, this Bulletin.

calendar years. Senate amendments Nos. 19, 20, 21, and 22 provide that this increase in the rate of tax, as modified by the House bill, is to apply to the calendar year 1968 and subsequent calendar years. Thus, under the conference agreement the rate of the employer tax, and the rate of the employee tax, for the calendar year 1968 and subsequent calendar years will be 4⅝ percent. The House recedes.

Amendment No. 23: Senate amendment No. 23 adds a new section 202 to the bill. Subsection (a) amends section 1402(e) of the Internal Revenue Code of 1954 by adding at the end thereof a new paragraph No. (6). Under the new paragraph in any case where a minister or Christian Science practitioner dies after September 12, 1960, and before April 16, 1962, his survivor or the fiduciary of his estate may file a certificate, on or before April 15, 1962, electing to have the services of the minister or Christian Science practitioner covered under title II of the Social Security Act. Such a certificate would be effective for the period prescribed in existing law as if filed by the minister or Christian Science practitioner on the date of his death.

Subsection (b) of the new section 202 provides the effective date for the amendment.

The House recedes.

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W. D. MILLS,
CECIL R. KING,
THOS. J. O'BRIEN,
N. M. MASON,
JOHN W. BYRNES,
Managers on the Part of the House.

[H.R. 7446] [8]
TAX RATE EXTENSION ACT OF 1961

[House of Representatives Report No. 450, Eighty-seventh Congress, First Session]

[June 5, 1961]

MR. MILLS, from the Committee on Ways and Means, submitted the following report to accompany H.R. 7446.

The Committee on Ways and Means, to whom was referred the bill (H.R. 7446) to provide a 1-year extension of the existing corporate normal-tax rate and of certain excise-tax rates, having considered the same, report favorably thereon without amendment and recommend that the bill do pass.

I. SUMMARY OF BILL

H.R. 7446 continues for 1 year certain existing tax rates. The existing tax rates which this bill continues until July 1, 1962, are the present 52-percent corporate income tax rate, which would otherwise revert to 47 percent (the 5 percentage point reduction would occur in the 30 percent normal tax) and the present rates of excise tax on distilled spirits, beer, wine, cigarettes, passenger cars, automobile parts and accessories, general telephone service, and transportation of persons. All of these reductions which under present law occur on June 30 of this year, except those relating to the latter two taxes, represent increases made at the time of the Korean war. The general telephone tax and the tax on the transportation of persons were added to the list of taxes subject to automatic reductions by the Tax Rate Extension Act of 1959 [P.L. 86-75, C.B. 1959-2, 679].

If these tax rates were not continued, it is estimated that there would be a revenue loss of almost $3.7 billion in a full year of operation and a loss of revenue in the fiscal year 1962 of over $2.5 billion (taking into account the effect of the bill on tax refunds).

The extension of these existing tax rates for 1 more year was recommended by the President in his tax message of April 20.

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[8] Public Law 87-72, page 317, this Bulletin.

II. EXPLANATION OF RATES EXTENDED

This bill provides for a 1-year extension of the present corporate income tax rates and the existing rates of certain excise taxes. The rates of these taxes otherwise are scheduled for reduction on July 1, 1961. The present 52-percent corporate income tax rate, without the 1-year extension provided by this bill, would revert to 47 percent as of July 1, 1961, through a reduction of the normal tax rate from 30 percent to 25 percent.

The excise tax rates, which without this bill would also be decreased as of July 1, 1961, are those on—

(1) distilled spirits, which would be reduced from $10.50 to $9 per proof gallon;

(2) beer, which would be reduced from $9 to $8 per barrel;

(3) wines, which are subject to various tax rates which would be reduced by approximately 11 percent;

(4) cigarettes, which would be reduced from 8 cents to 7 cents a pack;

(5) passenger cars, which would be reduced from 10 percent to 7 percent of the manufacturer's price;

(6) auto parts and accessories, which would be reduced from 8 percent to 5 percent of the manufacturer's price;

(7) general telephone service, which would be reduced from 10 percent of the amount paid to zero; and

(8) transportation of persons, which would be reduced from 10 percent to 5 percent of the amount paid.

The reductions in the corporate income tax and in the taxes referred to in the first six categories listed above are rate increases which were initially provided in 1951 at the time of the Korean war. The elimination of the tax on general telephone service (or local telephone service as it formerly was called) and the reduction in the tax on the transportation of persons was first scheduled (for the year 1960) in the Tax Rate Extension Act of 1959.

The bill, in addition to postponing the excise tax rates referred to, also makes a number of technical changes, including the postponement for 1 more year of the floor stock refunds or credits presently effective with respect to stocks of various taxpaid products on hand on July 1, 1961. These floor stock refunds are available in the case of distilled spirits, wines and beer, cigarettes, and passenger cars.

III. REVENUE EFFECT OF TAX RATE EXTENSIONS

Table 1 shows the revenue effect of the tax rates extended by this bill. This is shown both for a full year of operation and for the fiscal year 1962. The full year effect of the bill will be to maintain receipts of almost $3.7 billion which would otherwise be lost. In the fiscal year 1962, the receipts maintained by the rate extensions will amount to $2.5 billion (taking into account the effect floor stock refunds otherwise would have). The difference between the full year effect and the effect in the fiscal year 1962 is primarily attributable to the postponement of the corporate rate reduction which is not fully reflected in receipts in the fiscal year 1962. There is also some lag in collections in the manufacturers excise taxes on passenger cars and auto parts and accessories, as well as in the case of the general telephone and transportation of persons taxes. In the case of excise taxes, however, the lag in collections is largely offset by the fact that the bill postpones for 1 more year any refunds which otherwise would have to be made with respect to certain taxpaid commodities in dealers' hands on June 30, 1961.

As shown in table 1, slightly over $2 billion of the $3.7 billion revenue loss prevented by this bill is attributable to the corporate income tax. Of the remainder, $258 million is attributable to the taxes on alcoholic beverages, $244 million to the taxes on cigarettes, $477 million to the automotive taxes, $500 million to the general telephone tax, and $150 million to the tax on the transportation of persons.

TABLE 1.—*Corporation and excise taxes scheduled to be reduced July 1, 1961*

	Unit of tax	Present law rate	Rate to became effective July 1, 1961	Revenue loss (millions)	
				Full year	Fiscal 1962
Corporations	Normal tax net income.	30 percent	25 percent	$2,030	$925
Excises:					
Liquor taxes:					
Distilled spirits	Per proof gallon	$10.50	$9	158	155
Beer	Per barrel	$9	$8	89	87
Wine:					
Still wine:					
Containing less than 14 percent alcohol.	Per wine gallon	17 cents	15 cents	11	11
Containing 14 to 21 percent alcohol.	do	67 cents	60 cents		
Containing 21 to 24 percent alcohol.	do	$2.25	$2		
Containing more than 25 percent alcohol.	do	$10.50	$9		
Sparkling wines, liqueurs, etc.:					
Champagne or sparkling wine.	do	$3.40	$3		
Liqueurs, cordials, etc.	do	$1.92	$1 60		
Artificially carbonated wine.	do	$2.40	$2		
Tobacco taxes: Cigarettes	Per thousand	$4	$3.50	244	244
Manufacturers excise taxes.					
Passenger cars	Manufacturers' sale price.	10 percent	7 percent	402	352
Auto parts and accessories	do	8 percent	5 percent	75	65
Miscellaneous taxes:					
General telephone	Amount charged	10 percent	0	500	375
Transportation of persons	Amount paid	10 percent	5 percent	150	110
Total excises				1,629	1,399
Grand total, corporate and excise taxes.				3,659	2,324
Decrease in excess tax refunds					178
Total net revenue effect				3,659	2,502

Source: Staff of the Joint Committee on Internal Revenue Taxation.

IV. EFFECT OF BILL ON THE BUDGET

Representatives of the administration appearing before your committee in executive session have recently estimated that there will be a deficit for the fiscal year 1962 of $3.7 billion if the revenue and expenditure requests of the President are all enacted. This is based upon the following estimates of budgetary revenues and expenditures:

	Billion
Expenditures	$85.1
Revenues	81.4
Deficit	3.7

Table 2 shows the more detailed expenditure estimates on which the above expenditure total of $85.1 billion is based. This table shows the estimates appearing in the budget presented on January 16 by the last administration, together with the two revisions made by the present administration in these estimates. The $85 billion shown in table 2 as the current expenditure estimates excludes any amount for the expansion of the civil defense program as recommended by the President. Therefore, the administration representatives increased this $85 billion by $100 million to reflect the expenditure requirement of this program, as well as other contingencies. The expenditure figures presented above assume the enactment of the President's recommendations with respect to postal rates. If this is not done, it is estimated that the deficit will be $741 million larger than that shown. These figures also assume the enactment of all of the President's revenue requests, including those relating to jet fuel and

TABLE 2.—*Budget expenditure summary, May 25, 1961*

[Fiscal year 1962. In millions]

Department or agency	Jan. 16, 1961, estimate	Mar. 28, 1961, estimate	May 25, 1961, increases	Total
Legislative branch and the judiciary	$203	$207		$207
Executive Office of the President	92	92		92
Funds appropriated to the President:				
Mutual security—economic and contingencies	1,875	1,875	$75	1,950
Other	75	175		175
Independent offices:				
Atomic Energy Commission	2,680	2,670		2,670
Federal Aviation Agency	730	743		743
National Aeronautics and Space Administration	965	1,050	330	1,380
Small Business Administration	98	98	88	186
U.S. Information Agency	138	146	2	148
Veterans' Administration	5,369	5,404		5,404
Other	436	456		456
General Services Administration	496	498		498
Housing and Home Finance Agency	728	942		942
Department of Agriculture	5,782	6,440		6,440
Department of Commerce	566	614	19	633
Department of Defense (military):				
Military functions	42,910	43,800	100	43,900
Military assistance	1,750	1,650	50	1,700
Department of Defense (civil)	984	1,021		1,021
Department of Health, Education, and Welfare	4,005	4,798		4,798
Department of the Interior	873	906		906
Department of Justice	294	296		296
Department of Labor	223	654	60	714
Post Office Department	63	63		63
Department of State	345	351		351
Treasury Department:				
Interest	8,593	8,693		8,693
Other	1,095	1,120		1,120
District of Columbia	66	66		66
Allowance for contingencies	100	100		100
Subtotal	81,532	84,926	724	85,650
Deduct interfund transactions	667	667		667
Total	80,865	84,259	724	84,983

NOTES

1. Mar. 28 figures include reestimates of expenditures under the Jan. 16 program as well as new proposals of this administration.
2. Excludes amount for expansion of civil defense program.
3. Excludes certain small modifications proposed by the President between Mar. 28 and May 25 which will affect 1962 expenditures by a smaller amount than the allowance for contingencies.
4. Detail may not add to totals because of rounding.

Source: Bureau of the Budget.

the highway program. These figures further assume the continuation of the tax rates provided by this bill. If these rates were not continued, the deficit shown for the fiscal year 1962 would have to be increased by about $2½ billion. Thus without the continuation of these rates, even if all other revenue requests of the administration are enacted, there would be a deficit for the fiscal year 1962 in excess of $6 billion.

V. REASONS FOR THE BILL

Your committee believes that the status of the budget as outlined above represents an impelling reason for the continuation of the present corporate and excise tax rates. In this respect, the President, in his tax message of April 20, said:

> Such extension has been adopted by the Congress on a number of previous occasions, and our present revenue requirements make such extension absolutely necessary again this year. * * * We cannot afford the loss of these revenues at this time.

The Secretary of the Treasury, in his appearance before your committee on May 3, said:

> It is essential that these rates be extended promptly to maintain intact the revenue-producing power of our tax system, to prevent an increase in the budget deficit, and to avoid prejudging next year's overall tax reform.

Your committee believes that even if a tax reduction were to be made at this time, it is not necessarily clear that the reductions which would occur in the absence of the extension of the specified corporate and excise tax rates would be the most desirable.

In addition to recommending the continuation of the tax on the transportation of persons for another year, the administration recommended that a tax be imposed on aviation fuel. This tax was for the purpose of helping to defray the costs of operating and improving the Federal airways system and was somewhat similar to a recommendation of the previous administration.

Your committee's bill would continue for another year the tax on the transportation of persons. No action is taken in the bill on the proposal to tax aviation fuel. The public hearing conducted by the Committee on Ways and Means on these proposals developed information that indicated further study should be made of the impact of the transportation tax on the transportation industry and of the impact of the proposed aviation fuel tax on the airline segment of that industry. Therefore, the committee has directed such a study by the interested executive departments and agencies relative to the consequence of these taxing proposals on the transportation industry in general and the airlines industry in particular insofar as the aviation fuels tax is concerned. It is expected that in preparing this report representatives of the industry will be consulted and given ample opportunity to express their views and recommendations. In view of the recognized importance of this problem and the administration's concern that the civil aviation industry be required to pay a fair share of the costs of operating and improving the Federal airways system, it is expected that every effort will be made to expedite this study and that a report will be made to your committee at the earliest possible date. The Secretary of the Treasury has assured your committee that such a report will be made and that, in fact, the necessary study has already begun.

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VII. VIEWS OF THE MINORITY MEMBERS ON H.R. 7446

The signatories to these views have joined to express a position with respect to one aspect of the tax rates extension provided under H.R. 7446. This aspect is concerned with the 10-percent Federal excise tax applicable to the transportation of persons which would be continued through June 30, 1962, under the committee bill.

We are convinced that the retention of the tax on transportation of persons is not in the national interest. It is a tax that was imposed during World War II for the purpose of deterring travel and providing revenue. From the standpoint of commerce and defense considerations there is no longer a place for a deterrent to travel as a matter of national policy. From the fiscal standpoint the tax is a poor revenue raiser in that it discriminates among modes of travel and against domestic travel as compared with foreign travel. It has a consequence that tends to necessitate Government subsidization of segments of the transportation industry to offset the tax impact on the carriers.

We are supported in our advocacy of the prompt repeal of this tax by the unanimous positions of the Interstate Commerce Commission and the Civil Aeronautics Board—the agencies of the Federal Government most fully acquainted with the needs of the rail, bus, and air travel industry.

On May 8, 1961, the Chairman of the Interstate Commerce Commission, Hon. Everett Hutchinson, appeared before the Committee on Ways and Means to urge the repeal of the 10 percent tax on passenger travel. He quoted the Commission as characterizing the tax as being "highly inimical to the best interest of this country." He said in behalf of the Commission:

> We believe that the loss of revenue resulting from the repeal of this tax would be offset to a considerable extent by additional income tax receipts resulting from increased public use of common carriers and the public interest in strengthening and preserving a transportation system capable of meeting adequately our country's need for service both in peacetime and during emergencies in conformity with the national transportation policy, as declared by the Congress. * * * The Commission strongly urges

that your committee give favorable consideration to the repeal in its entirety of the 10 percent excise tax on the transportation of passengers.

On May 12, 1961, the Chairman of the Civil Aeronautics Board, Hon. Alan S. Boyd, appeared before the Committee on Ways and Means and urged repeal of the Federal 10 percent tax on transportation of persons. In advocating the repeal of this tax and commenting on the administration proposal relative to jet fuel he stated in behalf of the Board:

> In view of the substantial financial problems facing the airline industry today, it is clear that the industry is not capable of absorbing a tax increase at this time. * * * It is the Board's view that the continuation of the 10 percent excise tax on passenger transportation will aggravate the critical financial situation facing the airline industry today.

Chairman Boyd informed the committee that the Nation's 12 trunkline air carriers in calendar year 1960 showed a combined net income on domestic operations of $1,191,000 after special items and income taxes. He stated that the proposed new tax on aviation fuel would, if it had been in effect, have changed the small profit realized by the domestic air trunkline industry into a substantial loss of over $40 million. According to Chairman Boyd, under existing and proposed law the trunkline air carriers are confronted with a $250 million revenue shortage which would be the equivalent to an additional 15 percent increase in passenger fares.

During the committee consideration of our efforts to obtain repeal of the 10 percent transportation tax, those members who opposed the repeal argued that the tax should not be repealed because of the need for imposing a user charge with respect to Government costs incurred in connection with civil airway operations. They advocated that the repeal of the tax be deferred until the user tax problem is solved. We agree with the user charge concept but we point out that the problem is not likely to lend itself to prompt solution in the light of the earnings figures cited in the previous paragraph with respect to the air trunkline carriers. The plight of our transportation industry demands action now and the repeal of the transportation tax is widely and generally recognized as being action in the right direction. Its repeal would contribute significantly to the strengthening of our Nation's transportation system in the interest of economic progress and national security.

In urging the repeal of this tax, it is appropriate that we should comment on the fiscal implications that attend this recommendation. In the face of a budget deficit we would tend ordinarily to oppose a tax rate reduction of this type. However, we offer the following reasons why the transportation tax should be repealed now even in the face of a budgetary deficit. The Congress has in the past acted under similar circumstances to provide a necessary excise tax adjustment in the case of an industry that is experiencing economic hardship in part attributable to the existence of the excise tax. Also, it has been estimated that a substantial portion of the excise tax revenue loss from repeal of the transportation tax will be offset by revenue gain from the elimination of a deductible expense and that the revenue offset would be further enhanced by the likelihood of a more profitable transportation industry. In addition, we are influenced in our position of advocating repeal of this tax by the fact that the present administration seems determined to spend far in excess of any willingness to tax or to be taxed. The previous administration sent to the Congress on January 16, 1961, a proposal for budgetary expenditures for fiscal year 1962 amounting to $80.9 billion. The present administration in approximately 4 months' time has raised this total to $85.1 billion, or an increase of $4.2 billion. The apparent compulsion of the administration to spend ever-mounting sums for programs of relatively less priority than the urgent requirements for a sound transportation system causes us to support the repeal of the 10 percent transportation tax even under conditions of a budgetary deficit.

In essence, we believe it more important to tax less for a strong domestic transportation system than to tax more for a trip to the moon and a Federal spending level that threatens to achieve orbital proportions.

We regret that the majority members of the Committee on Ways and Means did not find it possible to join with us in recommending the prompt repeal of the Federal 10 percent tax on transportation of persons.

NOAH M. MASON.
JOHN W. BYRNES.
HOWARD H. BAKER.
THOMAS B. CURTIS.
VICTOR A. KNOX.
JAMES B. UTT.
JACKSON E. BETTS.
BRUCE ALGER.
STEVEN B. DEROUNIAN.
HERMAN T. SCHNEEBELI.

[H.R. 929] [9]
PREPAID DUES INCOME OF CERTAIN MEMBERSHIP ORGANIZATIONS

[House of Representatives Report No. 381, Eighty-seventh Congress, First Session]

[July 14, 1961]

MR. MILLS, from the Committee on Ways and Means, submitted the following report to accompany H.R. 929.

The Committee on Ways and Means, to whom was referred the bill (H.R. 929) to amend the Internal Revenue Code of 1954 to permit the prepaid dues income of certain membership organizations to be included in gross income for the taxable years to which the dues relate, having considered the same, report favorably thereon with amendments and recommend that the bill as amended do pass.

The amendments are as follows:

Page 4, line 4, strike out "1959" and insert "1960".

Page 6, line 19, strike out "member." and the quotation marks, and insert "member."

I. SUMMARY OF BILL

The bill provides that prepaid membership dues income of membership organizations may, at the election of the taxpayer, for tax purposes be spread over the period during which there is a liability on the part of the organizations to provide the service, rather than reported in the earlier year in which the income is received. The liability involved must extend beyond the current year but may not extend for more than 36 months. The membership organizations to which the provision applies are limited to those, such as automobile clubs, which have no capital stock and make no distributions of net earnings to members. A special rule is also provided which spreads over a 5-year period the revenue loss which would otherwise occur in each of the first 3 years of transition to the new method for reporting this prepaid income. The provision is effective for taxable years beginning with the calendar year 1961.

The bill has been reported unanimously by your committee. Except for the effective date, this bill is the same as H.R. 11266, passed unanimously by the House in 1960.

II. REASONS FOR THE BILL

This bill is concerned with the relationship of income tax accounting to generally accepted accounting principles in the case of prepaid income arising from membership dues.

In adopting the Internal Revenue Code of 1954 Congress provided in what was then section 452 that taxpayers might elect to report prepaid income for tax purposes as income over the current year and 5 succeeding years, to the extent proper under the accounting methods used by the taxpayer (the period over which the income could be spread was less than 6 years where the liability

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[9] Public Law 87-109, page 318, this Bulletin.

to perform services, etc., was for a lesser period). In 1955, however, Congress became aware of the fact that a large revenue loss was involved in another accounting provision, namely, section 462 which related to reserves for estimated future expenses and which involved the doubling up of deductions in its first years of application. As a result Congress at that time repealed not only the provision relating to reserves for estimated expenses, but also section 452 relating to prepaid income since this provision was interrelated with section 462 and since in some cases it was possible to accomplish much the same purpose under either section. Nevertheless, Congress recognized in the committee reports describing this action the desirability of following generally accepted accounting principles for reporting income for tax purposes. It also indicated that study would be given to ways in which this could be accomplished without the substantial revenue loss which would have arisen under sections 452 and 462. Subsequently, in the Technical Amendments Act of 1958, Congress adopted a section (sec. 455) providing for the spreading forward of prepaid income for tax purposes in the case of newspaper and periodical subscriptions. The income in this case may, at the election of the taxpayer, be spread over the period in which there is a liability to furnish the newspaper or periodcial.

The problem with which this bill is concerned is substantially similar to the problem dealt with in the case of the prepaid subscription income provision enacted in 1958. In *Automobile Club of Michigan* v. *Commissioner* (*353 U.S. 180*) [Ct.D. 1807, C.B. 1957–1, 513] in 1957, the Supreme Court held that membership dues received one year in advance by that automobile club must be reported for income tax purposes for the year of receipt rather than over the 12-month period to which the dues related. The 1939 Code (and also the 1954 Code) provides that income is to be computed in accordance with the method of accounting regularly employed by the taxpayer in keeping his books, unless this method does not clearly reflect income. The Supreme Court denied this automobile club the right to spread the income over the period to which the dues related primarily on the grounds that the services which the club must render for the member might not be spread in the same manner as a pro rata allocation of the club dues.

The pro rata allocation of annual membership dues over the 12 months to which the dues relate may not precisely match the periods in which services are performed for individual members. Nevertheless, your committee believes that spreading dues income of these clubs in this manner will more clearly approximate the period in which the services are rendered than reporting the income for the year of the receipt of the membership dues.

To more accurately reflect generally accepted accounting principles in this case, therefore, your committee has concluded that in the case of membership dues it is desirable to provide in the code (sec. 456) that this income, subject to certain restrictions, may at the election of the taxpayer be reported on a pro rata basis over the period to which the income relates, that is, over the period in which the services to which the dues relate are required to be performed.

Your committee recognizes that to permit the delay in reporting the income in this manner would have an initial impact upon revenues, although because of the limited nature of this provision this impact of necessity must be small. To further mitigate this revenue loss your committee's bill provides a device which in effect spreads over a 5-year period the initial tax benefit from deferring the reporting of each of the first three years' prepaid income.

III. GENERAL EXPLANATION OF THE BILL

Your committee's bill provides that the prepaid dues income to which this bill relates is to be included in income for tax purposes ratably over the period during which the liability to render the services exists. Prepaid dues income means amounts received by a membership organization which are attributable to liabilities to render services. However, the liability involved must extend beyond the end of the current taxable year, but not beyond a period of more than 36 months.

Membership organizations are the only taxpayers eligible for this treatment. They are organizations, such as automobile clubs, without capital stock no part of the net earnings of which may be distributed to any member.

The tax deferral for this prepaid income is available only if elected by the taxpayer. However, no election may be made for a trade or business where the taxpayer is using the cash basis method of accounting. Also, if this treatment

is elected generally it must apply to all of the taxpayer's prepaid dues income from any single trade or business. An exception to this latter rule is provided for prepaid dues income where the liability to perform the services, although extending beyond the end of the current taxable year, nevertheless is for less than 12 months. Such dues income (to the extent permitted by regulations) does not have to be included under any deferral election. Also, prepaid dues income received in years before this provision became effective, even though attributable to the current or future years, is not (except as affected by the transitional rule) included under the deferral provision.

The election to apply this provision may be made at any time with the consent of Treasury Department or it may be made for the first year beginning after December 31, 1960, in which the taxpayer receives prepaid dues income in a particular trade or business. Once an election becomes effective for a taxable year it applies not only for that year but for all subsequent years as well unless the taxpayer obtains the consent of the Treasury Department to the revocation of the election.

Where the liability to perform services for which the dues were prepaid for any reason ceases, any income remaining unreported at the time that event occurs is to be included in income for tax purposes in the year in which the liability ceases. This would apply, for example, in the case of a cancellation of a membership. Also, where the membership organization itself ceases to exist, the bill provides that any income not previously included in income for tax purposes is to be so included for the year in which the cessation of existence occurs.

As indicated previously, the bill provides a transitional rule to minimize the initial revenue impact of the new provision. This revenue impact, if there were no special transitional rule, would arise because most of the income which under present law would have been reported in the transitional period, under the new provision is to be reported in subsequent years as the liability to which it relates arises. Thus, without a transitional rule there would be an immediate revenue loss in the first 3 years in which the new provision is in operation.

The transitional rules provided by the bill have the effect of spreading over a 5-year period the loss which would otherwise occur in each of the first 3 years. This is accomplished by providing that a taxpayer who has elected this provision is to include in its income for tax purposes a special additional amount equal to the prepaid dues received in the 3 years immediately prior to electing this provision, to the extent that these dues would have been included in the income of any of the first 3 transitional years had the election been made 3 years earlier. Where a taxpayer has income which is prepaid for 3 years, this means that "additional amounts" are included in the taxpayer's income for the first 3 years the new provision applies to him. If the prepayment of income is for 2 years or 1 year, additional amounts are included for only the first 2 years, or first year. Under the bill, these additional amounts included in income in this manner are then deducted ratably over the current year and 4 succeeding taxable years.

This transitional rule is illustrated in table 1 by the example of a club receiving $30 each year, representing a 3-year prepayment of a single membership. Assume also that the members involved joined in the middle of the year so that 6 months of these dues payments are attributable to the current year. Assume further that the club involved elected the new provision for the calendar year 1961.

Thus, as is indicated in part II of the table, the $30 of receipts in the year 1961 are, under the bill, to the extent not attributable to the current year ($5 is attributable to the current year in this case or one-half of 1 year's dues) spread over the succeeding years during which the liability exists. Thus, $10 of this income is attributed to 1962, $10 to 1963, and the remaining $5 to the first 6 months of 1964. Part II of the table shows a similar spread of income for the years 1962 through 1968.

Part I of the table indicates the additional amounts which are required to be included in income as a result of the application of the transitional rule. Thus, for the first year of the election, 1961, $5 of receipts from 1958 would be included plus $10 of receipts for both of the years 1959 and 1960. In 1962 only receipts from the years 1959 and 1960 are included since 1962 is more than 3 years beyond 1958 and liabilities under the bill may not extend beyond that length of time. Similarly, in 1963 only receipts of 1960 are taken into account and in 1964 no additional amounts are included in income. As is indicated the

inclusion of these additional amounts, together with the inclusions regularly required in the year of liability for those electing the prepaid income provision, results in a uniform $30 of income throughout the entire period, the same amount which would have been reported as the income without the adoption of the new provision.

Part III of the table indicates over what period the additional amounts included in income (the amounts shown in pt. I of the table) are deducted. As is indicated the additional amounts included in income in each of the 3 transitional years are deducted on a pro rata basis over the particular transitional year in question and the succeeding 4 years. Thus the $25 of income (attributable to 1958, 1959, and 1960 receipts) which, as shown in part I of the table, is included in income in 1961, is deducted ratably at $5 a year in the years 1961 through 1965. Similarly, the $15 of income (attributable to 1959 and 1960 receipts), included in income in 1962, is deducted at the rate of $3 a year in the years 1962 through 1966. Finally the $5 of income (attributable only to 1960 receipts), included in income in 1963, is deducted at the rate of $1 a year in the years 1963 through 1967. Thus, the total deductions in 1961 are $5, or one-fifth of the additional amount included in income in that year. Similarly, in 1962 the total deductions taken into account represent another similar $5 deduction plus $3 representing one-fifth of the additional income of $15 in 1962, etc.

TABLE 1.—*Illustration of application of transmittal rule under bill*

[Based upon receipt each year of $30, representing a 3-year prepayment of dues]

Year of receipt or to which deduction is attributable	Total receipts or deductions	Year of reporting income or taking deduction							
		1961 [1]	1962	1963	1964	1965	1966	1967	1968
	Part I—Additional amounts to be taken into account from receipts in years prior to election								
1958	$30	$5							
1959	30	10	$5						
1960	30	10	10	$5					
Total amount included in income a second time		25	15	5					
	Part II—Operation of new provision in years after election								
1961	$30	$5	$10	$10	$5				
1962	30		5	10	10	$5			
1963	30			5	10	10	$5		
1964	30				5	10	10	$5	
1965	30					5	10	10	$5
1966	30						5	10	10
1967	30							5	10
1968	30								5
Total gross income		30	30	30	30	30	30	30	30
	Part III—Special deductions provided by transitional rule								
1961	[2] $25	$5	$5	$5	$5	$5			
1962	[3] 15		3	3	3	3	$3		
1963	[4] 5			1	1	1	1	$1	
Total special deduction		5	8	9	9	9	4	1	
Income after special deduction		25	22	21	21	21	26	29	$30

[1] Year of election.
[2] The $25 is attributable to including in income for a second time (in 1961) $5 of 1958 receipts, $10 of 1959 receipts, and $10 of 1960 receipts.
[3] The $15 is attributable to including in income for a second time (in 1962) $5 of 1959 receipts and $10 of 1960 receipts.
[4] The $5 is attributable to including in income a second time (in 1963) $5 of 1960 receipts.

The net effect of this transitional rule in this example is to provide that instead of the income in 1961 being reduced to $5, the reduction in 1961 is only from $30 to $25, or is $5. The remaining $20 reduction is spread evenly over the next 4 years. Similarly the reductions which otherwise would have occurred in 1962 and 1963 are spread evenly over those years and the succeeding 4 years. The same aggregate revenue reduction occurs as would be the case if there were no transitional rule. However, it is spread over a 7-year period instead of a 3-year period.

This bill applies to taxable years beginning after December 31, 1960.

IV. TECHNICAL EXPLANATION OF THE BILL

Your committee's bill adds a new section 456 to the Internal Revenue Code of 1954 relating to the treatment of prepaid dues income. Under subsection (a) of new section 456 qualifying taxpayers shall, at their election, include prepaid dues income to which that section applies in gross income for the taxable years during which the liability exists to render services or make available membership privileges, provided, however, that the period of time over which the liability exists extends beyond the taxable year of receipt but does not exceed 36 months.

Subsection (b) of new section 456 provides that where a taxpayer goes out of existence or where, for any other reason, the liability with respect to any prepaid dues income ends, the payments not previously reported as income become includible in gross income during the year in which such event occurs. Since a taxpayer may elect to report the income under the method provided by this section as to each separate trade or business, merely liquidating the trade or business as to which the election was made does not cause this provision to apply, unless in so doing the taxpayer's liability to render services is terminated. The liability described in this subsection may end, for example, by reason of the cancellation of a membership.

Subsection (c) of new section 456 contains the rules under which a taxpayer may elect to apply the provisions of that section. The election may be made only with respect to a trade or business the income from which is not reported on the cash receipts and disbursements method. If the taxpayer is engaged in two or more trades or businesses, it may elect to defer all items of prepaid dues income received in respect of any one or more trades or businesses. The election once made is generally applicable to all items of prepaid dues income attributable to such trade or business. An exception is provided, however, in the case of prepaid dues income in respect of which the liability is to end beyond the end of the taxable year but within 12 months after the date of receipt, in which case the entire amount received from the trade or business may be included in gross income when received to the extent permitted by regulations prescribed by the Secretary or his delegate. The election is effective for the taxable year with respect to which it is first made and for all subsequent taxable years. Computation of taxable income under an election shall be treated as a method of accounting. Except to the extent provided under the transitional rules in subsection (d), the election to defer prepaid dues income will not apply to amounts received before the first taxable year for which the election is made.

The taxpayer may make the election to defer prepaid dues income without consent of the Secretary or his delegate for the first taxable year beginning after December 31, 1960, in which it receives such prepaid income in connection with the particular trade or business. The election must be made not later than the time prescribed by law for the filing of the return for such taxable year (includings extensions). If the taxpayer wishes to make an election at a later time, the consent of the Secretary or his delegate must be obtained.

Paragraph (1) of subsection (d) of new section 456 provides transitional rules which require a taxpayer making an election under this section to include in gross income for each taxable year to which such election applies, not only that portion of prepaid dues income which is includible in gross income for each such taxable year under subsection (a), (b), and (c), but also an additional amount equal to the amount of prepaid dues income received in the 3 taxable years preceding the first taxable year to which such election applies which would have been included in gross income in the taxable year had the election been effective 3 years earlier. Under paragraph (2) of subsection (d), a taxpayer who has made the election with respect to prepaid dues income, and who includes in gross income for any taxable year an additional amount described in paragraph (1) shall be permitted to deduct, for such taxable year and for each

of the 4 succeeding taxable years, an amount equal to one-fifth of such additional amount. Such deduction shall only be allowed if such amount was actually included in the taxpayer's gross income during any of the 3 taxable years preceding the first taxable year to which such election applies. However, section 481 of the 1954 Code shall have no application to the additional amounts described in this subsection. The provisions of this subsection are illustrated by the example shown in the general explanation of this bill.

Paragraph (1) of subsection (e) of new section 456 defines prepaid dues income as any amount (includible in gross income) which is received by a membership organization in connection with, and which is directly attributable to, a liability to render services or make available membership privileges over a period of time which extends beyond the close of the taxable year in which such amount is received. Such services or privileges may include, for example, such services as road service, touring information and map service. A membership organization (defined in paragraph (3) of subsection (e)) is a corporation, association, federation, or other type of organization which is organized without capital stock of any kind and no part of the net earnings of which is distributable either directly or indirectly to any member.

The term "liability" is defined in paragraph (2) of subsection (e) as a liability to render services or make available membership privileges over a period of time which does not exceed 36 months. Such liability shall be deemed to exist ratably over the period of time that such services are required to be rendered, or over the period that such membership privileges are required to be made available. Accordingly, prepaid dues income shall be included in income ratably over the period that the liability exists. Any amount received in connection with a liability to furnish services or membership privileges over a period in excess of 36 months or which does not extend beyond the taxable year of receipt shall be included in income without regard to the enactment of this provision.

Paragraph (4) of subsection (e) provides that prepaid dues income shall be treated as received during the year it is includible in gross income without regard to section 456.

Subsection (b) of the bill contains a technical conforming amendment. The amendments made by this bill shall apply with respect to taxable years beginning after December 31, 1960.

[S. 1154] [10]

MUTUAL EDUCATIONAL AND CULTURAL EXCHANGE ACT OF 1961

[Senate Report No. 372, Eighty-seventh Congress, First Session, Calendar No. 352]

[June 14, 1961]

MR. FULBRIGHT, from the Committee on Foreign Relations, submitted the following report to accompany S. 1154.

The Committee on Foreign Relations, having had under consideration the bill (S. 1154) to provide for the improvement and strengthening of the international relations of the United States by promoting better mutual understanding among the peoples of the world through educational and cultural exchanges, reports it favorably with amendments and recommends that it be passed by the Senate.

1. MAIN PURPOSE OF THE BILL

The main purpose of the bill is to improve the quality and effectiveness of the international educational and cultural exchange programs administered and sponsored by the U.S. Government, especially by consolidating in one act various existing pieces of legislation authorizing such programs. At the same time, while there are few entirely new provisions in the bill, it does expand, strengthen, and better define certain activities authorized in earlier legislation. The overall aim is to promote educational and cultural affairs to a more im-

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[10] Incorporated in H.R. 8666 and enacted as the Mutual Educational and Cultural Exchange Act of 1961. This publication of the Senate Report is restricted to excerpts involving internal revenue matters; P.L. 87–256, page 322, this Bulletin.

portant position in the foreign relations of the United States. By emphasizing the mutual benefits of exchange programs, the bill makes it clear to other nations that this country recognizes that it has much to learn from, as well as offer to, others.

2. Salient Features of the Bill

The bill concentrates on educational and cultural programs of the type now mainly carried out by the Department of State and the U.S. Information Agency. The more technically, or less academically, oriented exchange activities of the International Cooperation Administration and of other agencies—to the extent that the latter participate in such programs—are generally left undisturbed.

Through the means of S. 1154, the following acts would be consolidated and wholly repealed: section 32(b)(2) of the Surplus Property Act of 1944, the "Fulbright amendment," Public Law 584, 79th Congress (hereinafter referred to as Public Law 584); the International Cultural Exchange and Trade Fair Participation Act of 1956, Public Law 860, 84th Congress (hereinafter referred to as Public Law 860); and the joint resolution on the use of Finnish debt payments, Public Law 265, 81st Congress (hereinafter referred to as Public Law 265). There would also be repealed two sections dealing with educational exchange in the United States Information and Educational Exchange Act of 1948, the Smith-Mundt Act, Public Law 402, 80th Congress (hereinafter referred to as Public Law 402); portions of a few other sections of that legislation would be reenacted, but the bulk of the act would not be affected. The relevant provisions of the India Emergency Food Aid Act of 1951, Public Law 48, 82d Congress, automatically will expire and need not be reenacted. In a number of instances, S. 1154 draws upon and reinforces, but does not amend pertinent sections of the Mutual Security Act of 1954, as amended, and the Agricultural Trade Development and Assistance Act of 1954, Public Law 480, 83d Congress (hereinafter referred to as Public Law 480).

By consolidating the various provisions of existing law, it is intended that the bill will alleviate, if not entirely overcome, the built-in limitations and the division of authority into compartments which have resulted from a failure in the past to develop a coherent overall plan and rationale for international educational and cultural programs. As an example of such restrictions, exchanges under Public Law 584 have been limited to countries where the United States has generated local currency repayments to the U.S. Treasury through other programs. Thus, despite the long-evident need for closer academic and cultural ties between this country and Latin America, there still are no Public Law 584 programs in a majority of South and Central American nations. The bill would provide a remedy for this situation.

Fiscal limitations constitute the most important, but certainly not the only, barriers to the creation of the flexibility needed to administer the programs more efficiently, especially in terms of better and longer term planning and programming. For instance, it is extremely difficult to screen applications for grants, to go through the selection process, to conclude necessary arrangements with academic institutions, and to make travel reservations without a considerable period of lead time; under present circumstances, the amount of such time is severely curtailed by the uncertainties of dollar appropriations for each fiscal year. In this connection, it is not sufficiently understood that dollars are generally needed in order to acquire and use foreign currencies, as well as to cover administrative support costs. Under S. 1154, appropriations are authorized on an "available until expended" basis, and there is reaffirmation that all sources of foreign currencies may be utilized, subject to appropriations. In addition, there are provisions which could stimulate less restricted use of such funds; for example by employing U.S.-owned currencies of one foreign country in a "third country."

The bill reestablishes the existing advisory and selection groups concerned with the implementation of the exchange programs. While there are provisions for improved coordination between the groups, and small increases in their membership in a few cases, their functions are continued largely unchanged. Various other minor amendments are made to promote better and easier operation of those bodies.

Sections amending the Immigration and Nationality Act and the Internal Revenue Code are designed to counter small but significant difficulties plaguing participants in the exchange programs, as well as others who are not supported by public funds. With respect to the Immigration Act, the amendments are

quite minor in both nature and effect: another nonimmigrant alien class is established for visa purposes to make specific an already existing practice; a student's or exchange visitor's spouse and minor children may be granted the same type of visa given the principal; within stringent definitions and limits, these visitors may accept employment while in this country; and a provision now found in Public Law 402 is shifted to the act. With regard to the Internal Revenue Code, the amendments provide that the income of a student or other exchange visitor shall be taxed and withheld on a basis similar to that applied to a U.S. citizen; the necessity for social security and unemployment withholding payments would be largely eliminated.

3. Background and Committee Action

It has been evident for some time that the international educational and cultural programs carried out by the U.S. Government have been laboring under increasing restraints and difficulties. The basic problem is that these programs have grown in an ad hoc, piecemeal fashion over a period of roughly two decades. They now operate under at least half a dozen pieces of legislation, largely created through separate initiatives and passed without much consideration of each other. Although widely recognized as an essential ingredient in the administration of our foreign relations, these programs have not had any clearly stated relationship to U.S. foreign policy.

Restrictions on the programs are found in three broad areas: the inadequacies of legislative authority to meet changing world conditions, the short term and uncertain character of the financing for the programs, and the confusing administrative arrangements which have been established to implement a variety of exchanges. Furthermore, there has been far too little recognition of the problems which are being encountered by American universities and other institutions of learning. They are having great trouble in dealing effectively with the large number of foreign students now in this country, most of whom (roughly 90 percent) are not covered by programs of the Federal Government. They are being called upon with increasing frequency to use their resources both at home and abroad to assist in the fulfillment of U.S. Government objectives without much thought being given to the replenishment, much less expansion, of those resources.

A measure of the problem and the concern shown by those who have the operating responsibility is afforded by the number of studies and conferences on the overall subject sponsored by the executive branch during the past 2 years or so. Substantial efforts have also been made by the executive branch to improve coordination within and outside the Government, but these have been partially frustrated by the dispersion of authority and resources resulting from an inadequate legislative base.

In midsummer of 1960, it was clear that the existing, almost offhand approach to international educational and cultural programs would not adequately serve our national interests over the decade ahead, and that congressional initiative was badly needed for the task of improvement. Such an initiative was taken in recognition of the fact that both the then presidential candidates had displayed great interest in the subject, insuring a high priority for action in this field regardless of the electoral outcome. Because of the uncertainty about that outcome and the time needed for any new administration to gets its house in order, it was felt that a standing committee of the Congress would be in a better position to direct the extensive work needed to create a fresh legislative approach.

A beginning was made last October by convening under committee auspices, and under the chairmanship of Senator Fulbright, an informal conference of top-level educators and Government officials most conversant with the operations of the exchange programs. Among the participants were the present Secretary of State, the Director of the U.S. Information Agency at that time, and the former head of the State Department Bureau of International Cultural Relations. There was complete agreement on the urgent need for action, and remarkable unanimity of feeling about the required major changes in legislation governing the exchange programs. While there was a clear consensus about the proper course to be followed, there naturally have been differing views about that question. A case could be made for an effort to recast and strengthen the entire range of international educational and cultural programs, but such an attempt would involve lengthy and arduous study and a sweeping

reorganization which would militate against needed early action. On the other hand, it could be argued that the relevant acts might just be amended in places to correct the more obvious deficiencies. This approach would only perpetuate the difficulty experienced in making a patchwork collection of legislation serve the new requirements of this period of world history. It therefore was decided that, in developing draft legislation, a middle course should be pursued which would offer the greatest promise of useful and prompt action in this current session of Congress.

The resulting bill (S. 1154), incorporating this moderate approach, was introduced by Senator Fulbright on March 2. Testimony from more than a dozen nongovernmental witnesses, representing among them the views of most major American institutions of higher learning, was received in public session on March 29, and was uniformly favorable in character. A public hearing to receive the views of the executive branch was delayed until April 27 so that the committee could be given a fully coordinated and approved single administration position on the bill. On that date, Philip H. Coombs, Assistant Secretary of State for Educational and Cultural Affairs, presented the composite views and proposed amendments of the executive branch, and strongly supported S. 1154. While there was a large number of such proposed amendments, many of the suggested changes were technical rather than substantive in character.

The committee considered the bill, and all amendments which had been presented, in several executive sessions during the latter half of May and early June, and voted on June 12 to report it favorably to the Senate as amended.

Since sections 109 and 110 of S. 1154 amend respectively the Immigration and Nationality Act and the Internal Revenue Code, the committee took steps to coordinate its actions with the Judiciary and Finance Committees of the Senate. The results of that coordination are set forth in the following letters from Senator Harry F. Byrd, chairman of the Committee on Finance, and Senator James O. Eastland, chairman of the Committee on the Judiciary:

Hon. J. W. FULBRIGHT,
Chairman, Foreign Relations Committee,
U.S. Senate, Washington, D.C.

DEAR MR. CHAIRMAN: The Committee on Finance, in executive session on May 18, 1961, considered and approved provisions included in S. 1154, the Mutual Educational and Cultural Exchange Act of 1961 which would amend the Internal Revenue Code of 1954. S. 1154 is currently pending before your committee.

The tax provisions of this bill deal with the status, for Federal income tax purposes, of certain nonresident alien individuals who are temporarily in this country under an educational or cultural exchange program. Under present law, these individuals are subject to a U.S. tax of 30 percent of their gross income without benefit of personal exemptions or other deductions. Moreover, gross income of these nonresident alien individuals may include amounts received by them as scholarships or fellowship grants from foreign governments or certain international organizations. The tax is collected through a system of withholding at a rate of 30 percent.

The income tax amendments approved by the Committee on Finance for inclusion in S. 1154 provide more favorable tax rules for these nonresident alien students.

The scholarship and fellowship grant provision of the Internal Revenue Code would be amended to permit amounts received as a scholarship or fellowship grant from a foreign government or from certain international organizations to be excluded from gross income in the same manner and to the same extent as such amounts received under a similar award from the U.S. Government.

The special rules for taxing nonresident aliens would be amended so that aliens temporarily in this country under an educational or cultural exchange program would not be subject to the 30-percent gross income tax but would be taxed (if at all) at the same rates at which U.S. citizens are taxed. In addition, they would be entitled to one personal exemption (for income tax and withholding purposes) and to deductions attributable to amounts included in gross income. If such an alien receives amounts from a foreign employer while he is in this country, such amounts would not be included in his gross income for purposes of the U.S. tax.

Neither the social security taxes nor the Federal unemployment tax would apply in the case of such nonresident aliens.

In addition, the amendments approved by the Committee on Finance exempt from the 30-percent withholding tax nonresident alien individuals temporarily present in the United States under an educational or cultural exchange program. However, it is believed amounts received by such aliens which are included in gross income should continue to be subject to withholding, but only at a rate commensurate with the tax such alien ultimately may be required to pay. Consequently, the wage withholding provisions of the Internal Revenue Code would be amended to require withholding with respect to amounts received (whether under a scholarship or fellowship grant, or otherwise) by such aliens at the rate applicable to U.S. citizens generally (approximately 18 percent).

The Committee on Finance authorized such technical amendments as may be necessary to conform the tax provisions of S. 1154 to the foregoing.

With kindest regards, I am,

Faithfully yours,

HARRY F. BYRD, *Chairman.*

JUNE 1, 1961.

Hon. J. W. FULBRIGHT,
U.S. Senate, Washington, D.C.

DEAR SENATOR FULBRIGHT: Reference is made to S. 1154, a bill to provide for the improvement and strengthening of the international relations of the United States by promoting better mutual understanding among the peoples of the world through educational and cultural exchanges.

It is my understanding that the amendments recommended by the executive departments to S. 1154 in connection with section 109 of the bill have been adopted by the committee. Under these circumstances it will not be necessary for the Committee on the Judiciary to request a referral of the bill.

With kindest regards, I am,

Sincerely yours,

JAMES O. EASTLAND, *Chairman.*

The Committee on Foreign Relations is impressed with the great and growing importance of educational and cultural exchanges in a world situation which is promoting constantly increased contact between nations. Increased contact does not automatically result in increased mutual understanding. however, and it can in fact sometimes have the reverse effect. It thus is all the more necessary for this Nation to make every effort to encourage its citizens and peoples from other lands to see the world as it actually is, and not as it is presented by aggressively ideological propaganda which encourages and feeds upon prejudice, ignorance, and deliberate distortion. Educational and cultural exchange programs are a key element in this effort and, consequently, in the conduct of our foreign relations.

Especially at a time when it is most evident that any broad use of military power represents a breakdown of foreign policy, it is, or should be, equally recognized that the greatest foreign policy asset of an open and democratic society is its force of attraction. We are judged by others, and we form judgments in our turn, on the basis of what things matter most in our societies. While ours is far from perfect, the United States has no reason to fear that it will suffer in any accurate comparison. Yet there is a disturbing susceptibility to hostile propaganda about us among people of other non-Communist countries, particularly those in the so-called underdeveloped areas. At the same time, there is ample evidence that many of our own citizens—including those in the best position to influence others—are making judgments about other nations on the basis of insufficient, if not erroneous, information. Educational and cultural programs offer vital means through which we and other peoples may overcome these difficulties. But these programs are not, and should not be considered, an instrument for coverting people to a particular point of view: As with education itself, such programs are designed to encourage clear thinking and the pursuit of the truth about world conditions.

However, a caveat must be entered here. These exchanges will not succeed without careful attention being devoted to all their aspects. Considerable damage may be done by badly planned, poorly administered, and financially

starved programs. The record of the programs carried out by the U.S. Government to date in most respects has been very good—but not good enough. In this connection, two facets of our official programs should be stressed: First, they account for only about 10 percent of the annual exchanges in which this country is involved; yet, second, in themselves and by example, they generate much of the great private efforts and contributions in the United States. Under these circumstances, the official programs should provide the proper lead by maintaining the highest standards of overall quality.

Testimony before the committee indicated that Sino-Soviet bloc activity in the sphere of international educational and cultural programs is continuously increasing, but remains substantially smaller than that of the United States. On the other hand, there is evidence that the bloc spares no expense and effort when it seeks to impress any particular country or group of countries, as it has been doing in areas such as Africa. The committee does not equate the bloc programs with those of this country, nor does it consider that specific countries should be singled out for red-carpet treatment. But it recognizes the implications of such developments for the conduct of our officially directed exchange programs.

The committee believes that S. 1154 will make it possible for the United States to improve both the quality and the quantity of its international educational and cultural programs. If a choice had to be made, quantity would have to be sacrificed to an urgent need for higher quality. Yet it is clear that the national interest dictates not a choice, but progress on both counts. Such an advance obviously requires substantially increased appropriations for the consolidated existing programs, as well as funds to cover improvements and new items authorized in this bill. The committee trusts that the executive branch will act decisively in presenting a soundly conceived and documented longer range educational and cultural program, and that there will be a favorable response in Congress.

4. Section-by-Section Analysis

The descriptive words preceding the enacting clause constitute an almost verbatim amalgamation of the language of Public Law 402 and Public Law 860. For reasons of brevity and priority emphasis, reference to trade fair activities authorized in the latter act is not made in this title. However, as evidence in section 102, there is no intention to slight or narrow in any way the present congressional mandate for participation in international fairs and similar functions.

A. STATEMENT OF PURPOSE (SEC. 101)

This section as drafted is largely a combination of the statements of purpose contained in Public Law 860 and Public Law 402. One very significant difference is that the theme of mutual efforts and benefits is expanded throughout the entire section in recognition of the fact that the United States, and specifically its educational and cultural resources, have much to gain from increased contact and cooperation with other countries. The executive branch amendments to this section adopted by the committee recognize that a number of already authorized activities—which are brought together and continued in this bill—are not adequately defined solely in the exchange context and require more positive identification.

The general consolidation of scattered existing authority into this section should encourage maximum flexibility in the use of dollars and foreign currencies. At present, some activities (e.g., those described in sec. 102(a)(2) (ii) and (iii) can be supported only with appropriated dollars; others (e.g., see sec. 102(b)(5)), only with foreign currencies. While the latter should always be used in lieu of dollars whenever possible, a decision to support a particular activity anywhere abroad should be made on the basis of its merit rather than on the grounds of whether or not a particular local currency is available. The general language of this section, in conjunction with section 105, would provide the necessary authority.

B. EXCHANGE ACTIVITIES (SEC. 102(a))

Using language from Public Law 584, Public Law 402, Public Law 265, and Public Law 860 this section authorizes continuation of the educational and cultural exchanges now carried out under those statutes. Such exchanges need not be conducted on a strictly reciprocal basis, but they are to be undertaken

only when it is considered that they will "strengthen international cooperative relations." There may well be times when the exchanges themselves will constitute the major effort by the United States in establishing and improving relations.

Section 102(a)(1) covers the full range of existing educational exchanges and eliminates certain restrictions which have hampered the Public Law 584 programs in particular. For example, the words, "in schools and institutions of higher learning," applied in Public Law 584 to the activities of Americans abroad, are omitted because many students and teachers will be doing their work in institutions that technically are not so described. More important, there is no continuation of the current limitation applicable to Public Law 584 grants for foreign students coming to the United States—namely, that they may cover only transportation expenses. It no longer will be necessary to issue joint awards citing one statute (Public Law 584) as authority for foreign currency travel funds and another (Public Law 402) for dollar expenses in the United States. This will permit flexibility that should result in simplified procedures and much less paperwork. Furthermore, the language of this section would permit broader and more efficient use of U.S.-owned local currencies in support of the attendance by foreign nationals at American schools and institutions of learning abroad. The single executive branch amendment to this section is the minor one of retaining the more general term, "trainees," precisely as contained in Public Law 402.

Section 102(a)(2) contains authority for the present leader and specialist exchange programs carried out under Public Law 402, and for cultural and trade fair participation in programs now conducted under Public Law 860. Subparagraph (ii) represents an exact transcription from the latter statute. Subparagraph (iii) contains a few one-word changes: "international" is substituted for "abroad" in order to permit financing of official U.S. representation in cultural events in this country as well as overseas; meetings and assemblies are added to the description of such cultural events. Subparagraph (iv) represents some new authority to permit assistance for nongovernmental foreign participation in nonprofit activities in the United States when there are no alternative means of financing a project, such as that of bringing works of art here for exhibition by museums. This authority could include assistance, such as international travel funds, for amateur groups (e.g., college glee clubs) to participate in noncommercial productions here; even though nominal admission fees might be charged, the sponsor and the activity both would be nonprofit in character.

Since the section (201) in Public Law 402 which contains authority for the exchanges of leaders and specialists is the largest element in that act to be repealed, mention should be made of the redistribution in S. 1154 of most of the other provisions in the section: orientation courses are authorized in section 104(e)(2); the desirability of reciprocity is expressed in section 103(a); and the bulk of the immigration and visa provisions are found in section 109, as amendments to the Immigration and Nationality Act. A few special provisions relevant to the Immigration Act, but placed in Public Law 402, are not reproduced; there are no such provisions in the other statutes (such as Public Law 860 and Public Law 584) authorizing exchange programs, and their absence has not been found detrimental to our national interests.

Section 102(a)(3) continues authority for U.S. participation in international fairs and expositions unchanged, with two exceptions: the limitation of activities to those held abroad is deleted, and the more inclusive word, "economic," is substituted in place of "industrial."

C. RELATED ACTIVITIES (SEC. 102(b))

Section 102(b)(1) authorizes interchanges, preparation, and distribution, in furtherance of the programs, of books of various kinds, their reproduction and translation, and other educational and research materials. Authorization of such activities and materials may be found in Public Law 265, Public Law 480, Public Law 402, and (in the case of handicrafts), Public Law 860.

Section 102(b)(2) reproduces the basic authorizing language of chapter VII of the Mutual Security Act of 1960, which provided for the center in Hawaii; the other provisions of that chapter to a large degree are covered elsewhere in this bill. Chapter VIII of the Mutual Security Act of 1960 contemplated the creation of a similar institution in Puerto Rico to serve this hemisphere. The

establishment and operation of centers in a few well-chosen locations could contribute much of the effectiveness of the overall program, especially in demonstrating abroad the concern of the United States for cultural and scholarly activities. Depending on their location, such centers could provide a very valuable means of utilizing foreign currencies generated under the Mutual Security Act and other legislation. Particular consideration, in this connection, might be given to creating cultural institutes in affiliation and physical proximity with existing U.S.-sponsored colleges and universities abroad (e.g., the American academic institutions in the Near East). Many Western European countries over the years have officially engaged in such activities and have gained prestige and influence overseas, as well as enrichment of their own cultures; the United States has never fully adopted a comparable approach.

Section 102(b)(3) continues the language and authority for assisting American-sponsored schools abroad contained in section 203 of Public Law 402 and section 104(o) of Public Law 480. It expands this authority to include assistance in the establishment of such schools and institutions in areas where they do not now exist. This new feature should be considered in the context of increasing sentiment and evidence that the United States, especially in view of its crowded and heavily burdened academic institutions, might well be devoting more attention to helping foreign students—particularly those in underdeveloped areas—on their own home grounds. It should be noted that the executive branch over a period has developed carefully drafted and sound criteria for assisting American-sponsored schools abroad; it is anticipated that such criteria will continue to be employed where relevant.

Section 102(b)(4) fosters and supports American studies abroad in various ways. Such support is now authorized directly in section 104(p) of Public Law 480, and indirectly in the exchanges under Public Law 584 and Public Law 402. The special institutes and seminars referred to in this section would be attended by foreign nationals either making a first contact with American educational techniques and subject matter or taking refresher courses to renew contact made earlier through a visit to the United States; there is new authority to help finance their attendance at such studies. The list of subjects for study is only meant to be illustrative—as evidenced by the amendment referring to other subjects—but the committee believed such a list provided helpful, if incomplete, guidelines.

Section 102(b)(5) is based on section 104(k) of Public Law 480 and has been amended to provide a sharper focus on educational and cultural affairs. Research and development in methods of teaching and learning through the exchange programs are particularly necessary in order to gain maximum benefits from contacts with areas and peoples which heretofore have scarcely participated in such programs.

Section 102(b)(6) is a new provision giving emphasis to exchanges of language teachers and students. Although such persons may be included to some degree in the regular exchange program, special recognition should be accorded the importance of language and area studies as a key to improved communication and understanding. In developing language skills there is no real substitute for visiting and studying in the country where the language is used. Recognizing that our own educational institutions are not satisfied with their resources for teaching foreign languages and cultures, the committee accepted an executive branch amendment authorizing the financing of reciprocal visits by foreign teachers to this country.

Sections 102(b) (7) and (8) were proposed by the executive branch, and accepted by the committee, in order to provide the same authority for participation by Americans and foreign nationals in educational, scientific, and technical meetings as is provided with respect to cultural meetings under sections 102 (a)(2) (iii) and (iv) of this bill.

D. BINATIONAL AND MULTINATIONAL AGREEMENTS (SEC. 103)

Section 103(a) authorizes the agreements with other nations and with the international organizations that may be needed in connection with the programs authorized by S. 1154. It continues the authority in Public Law 584 to enter into agreements for the use of foreign currencies for educational exchange, and extends that authority to the making of agreements with the United Nations (as proposed in several pending legislative items before the Congress) and other international organizations. The section also specifies the aim of reci-

procity, especially with regard to cooperation in financing programs under the bill, so that each cooperating country may spend its funds primarily within its own territory. While current agreements under Public Law 584 relate only to the use of foreign currencies held by the United States, this section permits the use of funds of the other countries and encourages the creation of implementing arrangements. This is now permissible to a limited extent under section 902 of Public Law 402, but with the initiative left to the other countries; under S. 1154 the President would be authorized to seek such an agreement.

Section 103(b) continues the authority to provide for the creation or continuation of the binational foundations and commissions which have done such fine work in implementing Public Law 584 programs abroad. These foundations are among the best testimonials to the mutual interest and benefits resulting from educational exchanges. Insofar as the President considers it desirable, the section could extend the responsibility of these organizations to the various programs under S. 1154. To the extent this is done, it would promote uniformity in the operation of the programs abroad, greater acceptability in the host country because of the binational factor, and maximum use of foreign currencies in oversea administration. The committee adopted the executive branch proposal that authority be provided for the creation of multinational foundations and commissions.

Section 103(c) authorizes participation by the United States in multilateral arrangements for educational and cultural programs through the United Nations and other international organizations. The committee altered the language of this section to comprehend programs rather than just exchanges, and to make it clear that the United States should accept only a fair share of the support, including financing, for such multilateral programs.

E. ADMINISTRATIVE PROVISIONS (SEC. 104)

The bill vests all authority in the President, following the precedent of Public Law 860, which is being repealed and reenacted by S. 1154. Section 104(a) authorizes him to exercise any power or authority through such agencies or officers as he shall direct. Doubtless this is what he would do in the absence of a specific provision, as was the case with Public Law 860.

While the section gives the President considerable latitude in administering programs under the bill, this is limited to the power and authority vested in him by this legislation. It would not authorize the transfer of authority vested by any other statute or by a reorganization plan in a specified officer of the executive branch. In this connection, it might be noted that this bill deals with only a portion of those functions authorized by Public Law 402 which were not transferred by Reorganization Plan No. 8 of 1953 to the U.S. Information Agency; namely, the educational exchange functions authorized by section 201 and aid to American-sponsored schools authorized by section 203.

Such provision for delegation continues the concept of both Public Law 860 and Public Law 402. While the latter act places all authority in the Secretary of State, rather than the President, it authorizes the Secretary to—

> delegate to such officers of the Government as the Secretary determines to be appropriate, any of the powers conferred upon him by this Act * * *.

Nevertheless, the committee has added a proviso to the amended section 104(a) to the effect that the appropriate committees of Congress should be given 60 days in which to review any proposal by the President for the transfer of power or authority under S. 1154. The committee considered this an entirely adequate safeguard for congressional interests, and believed that a more stringent provision would defeat the aim of flexibility as expressed throughout the bill. This proviso is designed to apply to a major transfer of existing functions, and not to necessary arrangements for implementing new programs contained in this bill.

The bill as referred to the committee contained a specific power to delegate to a new agency or an established department, emphasizing the understanding that either method would be acceptable. The committee acquiesced in the executive branch view that such discretionary power was unnecessary and should be deleted along with another section with related provisions.

Section 104(b) as amended provides specific authority to pay a limited number of officers at supergrade rates and permit five of these officers compensa-

tion at rates up to a maximum of $19,500 per annum. This authority is needed to attract and retain the highest caliber top staff and to raise the stature of the overall program. Similar authority is found, on a very much larger scale, in section 527(b) of the Mutual Security Act of 1954, as amended.

Sections 104 (c) and (d) as amended authorize the use of authority contained in the Foreign Service Act of 1946, as amended, for the employment and assignment of persons outside the United States. The employment and assignment of Americans to the binational and multinational foundations and commissions abroad is specifically provided for in section 104(c). As these are key organizations in the oversea administration of the program, a career service should be provided in order to obtain the high-caliber staff needed for effective operations. Section 104(d) authorizes employment and assignment, or assignment of persons already employed, as necessary for operations under the act abroad. Government employees would retain reemployment rights.

Section 104(e)(1) consolidates authority now present in Public Law 584, Public Law 402 and Public Law 265 providing for program grants to or for individuals, directly or through public and private institutions. The "incidental expenses" authorized mean dormitory fees and similar costs of the programs, and would, together with other parts of this section, include funds needed to enable the participants to realize a fully successful experience, including proper housing and admission to programs which are an integral part of our culture. The section also is intended to broaden the existing authority to provide for certain expenses of accompanying dependents, whose travel and transportation may now be provided to a limited degree under existing legislation. It should be recognized that many grantees cannot leave their families behind, and that dependents often contribute as much as the principal grantee to the purposes of the program. The provisions for health and accident insurance, and for transporting the remains of deceased grantees reproduce existing authority contained in the Mutual Security Act of 1954, as amended (sec. 537(b)), and Public Law 885, 84th Congress (sec. 3(e)), providing basic authority for the Department of State. Provision for emergency medical expenses is urgently, if very seldom, needed to prevent the sort of minor crisis which from time to time has been experienced in the past.

The amended provision for "such other expenses as are necessary for the successful accomplishment of the purposes of this act" is an extremely important item. It is vital to the success of the program and, indeed, to the prestige of the United States that foreign grantees receive the attention and treatment which would make their stay in this country a highly beneficial experience. In this connection, it should be stressed that S. 1154 provides for continuing the established role of foundations and educational and other institutions which assist the Government with the administration of the exchange programs. These institutions have rendered notable contract services despite the difficulties they confront, especially limited authority to make expenditures, in attempting to insure that foreign grantees receive the maximum benefit from their studies and contacts here. Section 104(e)(1) would authorize modest additional sums to be employed for services which often determine whether or not the purposes of the program are fulfilled. At the same time, considering that enactment of S. 1154 may result in the executive branch making greater demands of such institutions, their ability to sustain additional responsibilities would seem to be a valid subject for study.

Section 104(e)(2) continues the authority found in section 201(a) of Public Law 402 to provide "orientation courses and other appropriate services." Orientation is understood to take various forms, including the so-called home-stay practice of placing a foreign student in a private home to receive firsthand tutelage in the customs and language of this country. Provided that it furthers the purposes of the act, this authority is extended to exchanges other than those financed under this legislation. This latter provision will serve the cause of promoting mutual understanding at a minimum of expense, since the persons receiving the orientation will already be participating in an educational program at no cost to the Government. It is contemplated that the need for and use of this expanded authority would be greatest with regard to persons attending large academic institutions in metropolitan areas with an extensive foreign-student population. Such institutions, with few exceptions, are having great difficulty in providing adequate counseling, orientation, and other extracurricular services for their foreign students, most of whom are not under Government

sponsorship. Many of these students are receiving an unfavorable impression of the United States on other than academic grounds.

This section also gives specific authority for followup activities which are now being conducted on an inadequate basis as an incidental part of the exchange programs. While the effects of the programs cannot be measured with a slide rule, a good deal is known about their results through the later activities of the participants. This provision will permit the gaining of more knowledge and even greater confidence about the effectiveness of the programs.

Section 104(e)(3) is an almost verbatim reproduction of section 3(4) of Public Law 860. This section was omitted in the process of drafting the original version of S. 1154; its inclusion was recommended in the U.S. Information Agency comment on the bill.

Section 104(f) is intended to correct the dual system of security investigations now applicable to Government personnel performing functions under Public Law 402, or functions related to that act. The standard investigation for Government employees (under Executive Order No. 10450, as amended) will apply to all persons working under the provisions of S. 1154; the same type of change was enacted last year for ICA employees under the Mutual Security Act of 1960. It thus will be possible to transfer personnel from one function to another within a department without incurring the delay and expense of an additional investigation, which is not substantially different in content from the standard one. Executive Order No. 10450 already applies to operations of a considerably more sensitive nature than those authorized in this bill.

F. FINANCIAL PROVISIONS (SEC. 105)

Section 105(a) authorizes appropriations for all activities provided for in the bill and, with the executive branch amendment accepted by the committee, these are to remain available until expended. The general type of authorization is found in Public Law 402; no-year authority now exists in Public Law 860. This means that dollars can be appropriated for activities which currently can only be financed with local currencies. As noted elsewhere in this report, the United States has no access to such currencies in some countries and its supplies are exhausted in others. In many cases, local currencies have become convertible over the years and are of equal value with dollars. Availability of funds until expended is most necessary for agreements with countries to carry out programs involving expenditures over a period of years. It will permit advance planning, greater administrative flexibility, and more efficient operation. The section also includes authorization to enter into contracts in advance of appropriations when so provided in any appropriation act. Precedent for this authority to contemplate advance obligations is found in section 515 of the Mutual Security Act of 1954, as amended.

Section 105(b) provides for the acquisition of foreign currencies for the program which may be necessary for contributions to foundations and for grants and other expenses outside the country. For example, sufficient funds could be made available to a binational foundation or commission to cover operations for a period of years. The phrase "from any source" is intended to make it clear that the currencies for such purposes may be purchased on the market, from special funds, or from the U.S. Treasury.

Section 105(c), as amended, authorizes the President to transfer, under a 10-percent limitation, funds appropriated for like purposes under this and other acts; shifts could be made in both directions. This would provide for greater consistency and unity in similar programs conducted under different statutes. For example, the student program in the United Arab Republic now is split between ICA and the State Department because of the sources of funds involved, but for all practical purposes it is a single program and should be so conducted. The section is in harmony with a more general request for such transfer authority for heads of agencies made by the President in his budget message.

Section 105(d), as amended by executive branch proposals acquiesced in by the committee, would permit the President to reserve any currencies of foreign nations, over such periods as he determines, to provide for educational exchanges, and for cultural exchanges in certain categories. The generally existing authority (as contained, for example, in the Mutual Security Act of 1954, as amended) to make determinations about currencies needed goes to the Secretary of State; it is understood that the operating agency for the above exchange programs would be expected to determine the amounts of currencies

to be reserved, so that the Secretary's role would be continued. This section also authorizes the President, within limits to be established by Congress, to use such currencies of foreign nations for any programs authorized by S. 1154. Once the limits are established, the funds could be utilized, perhaps through foundations abroad, in a way that would minimize loss from depreciation or devaluation, and the principal and interest accruing to such organizations could be used over a period of time somewhat like educational endowments.

Paragraphs (i), (ii), (iii), and (iv), as amended, describe the sources from which foreign currencies are likely to be derived for reservation and use under this section 105(d). All the established sources, including both principal and interest, are intended to be covered. In this connection, the bill in its draft form prior to committee action contained an element of confusion because of the inclusion in this section of Finnish debt repayments in dollars provided in Public Law 265. This has been remedied by placing that dollar program in a new section 105(e). However, it should also be made clear that the term, "currencies of foreign nations," as used throughout section 105(d), as amended by the committee, includes "dollars" when that is the medium of exchange or the legal tender of a foreign nation.

Section 105(e), as amended, reenacts the special program in relation to Finland now authorized by Public Law 265. Existing agreements insure the continuation of that specific exchange program for a period of over two decades ahead.

Section 105(f), as redesignated, encourages foreign governments, international organizations, and private sources to participate and contribute to the purposes of S. 1154, and authorize the President to accept and use such contributions. The latter funds might be employed, for example, in support of a scholarship program of a multinational organization. Moreover, an artistic or athletic group, paying most of its own expenses, might be aided in some particular way, such as assisting the group to travel in a country it could not otherwise visit. Roughly similar authority to accept private contributions is found in Public Law 860 and Public Law 402.

G. SELECTION AND ADVISORY GROUPS (SEC. 106)

This section continues, with a number of relatively small changes to promote greater coordination and effectiveness of program policy, the selection and advisory bodies created in Public Law 584, Public Law 402 and Public Law 860.

Section 106(a) continues the Board of Foreign Scholarships (hereinafter referred to as the "Board") and increases its membership from 10 to 12. The Board is given responsibility for selection of all participants—including, implicitly, the educational institutions they attend—in the educational exchanges authorized in section 102(a)(1). It also is given a supervisory role in connection with those exchanges and some closely related provisions in section 102(b). The veterans' preference provision in the selection of American citizens under Public Law 584 is made more general and applied, along with the provision for due geographical representation, to all such selections for programs under S. 1154.

Section 106(b) replaces the Advisory Commission on Educational Exchange with the U.S. Advisory Commission on International Educational and Cultural Affairs (hereinafter named the "Commission"). The Commission will have advisory functions and responsibility for assessment in connection with all activities under S. 1154, including those for which the Board and the Advisory Committee on the Arts have a different category of responsibility. The membership of the Commission, nine in number, will be appointed by the President—by and with the advice and consent of the Senate—who will designate a chairman from among that membership. Political and other equally remote qualifications are not imposed as restrictions on the prospective membership, which may be wholly or partially reconstituted in terms of the existing Advisory Commission. The committee did not accept an executive branch proposal that the new Commission report to the Secretary of State as well as the President, since the latter automatically will inform and consult the Secretary in any case, and since it is intended that this direct link with the President will elevate the prestige of the Commission.

Section 106(c), as amended, continues the Advisory Committee on the Arts (hereinafter named the "Advisory Committee"), established by Public Law 860, virtually unchanged. The only differences are that the membership will increase from 9 to 10, that the Secretary of State will designate a chairman

from among those 10, that at least 1 member will also be a member of the Commission, and that the term of office will be 3 rather than 2 years.

Section 106(d) represents an approved executive branch amendment authorizing the Secretary of State to create other committees, if necessary, to assist the Commission. Precedent exists in Public Law 402.

Section 106(e), as redesignated, authorizes the President to create interagency and other committees when needed, and to convene conferences of interested persons and organizations when the creation of a committee is not necessary. This will elicit maximum cooperation and support from private groups and organizations, and assure that private and Government programs supplement and assist each other. Precedent is found in Public Law 860.

Section 106(f), as redesignated, by reference to 31 U.S.C. 691, prohibits the payment of additional compensation to Government employees who serve on interagency committees, but authorizes other expenses of such committees; a similar provision exists in Public Law 860. It also provides for transportation and per diem for Board, Commission, and Advisory Committee members at the rates prescribed generally by the Administrative Expense Act of 1946, as amended. The Board and the Advisory Committee are already entitled to such rates, but the Commission has been restricted to $10 per diem under Public Law 402. Finally, this section provides for compensation to members of the three groups (as well as other committees that might be established), at the usual consultant rate, for the days they are actually engaged in the authorized work.

Section 106(g), as redesignated, continues existing authority (in Public Law 860 and Public Law 402) for the provision of secretarial and staff assistance for these groups. There are separate staffs at present, but this will permit combining them if it seems desirable.

H. REPORTS BY SELECTION AND ADVISORY GROUPS (SEC. 107)

Section 107 requires the Board, the Commission, and the Advisory Committee to submit annual reports to Congress, and also to make reports to the public from time to time to assure a full understanding of the purposes of the exchange programs and their operations. Annual reporting is the method adopted in Public Law 584.

I. MISCELLANEOUS ADMINISTRATIVE PROVISIONS (SEC. 108)

Section 108(a) reenacts in exact form a provision in Public Law 860 giving specific authority to the President to disregard certain existing regulations and laws regarding contracting and expenditures. This authority is also contained in section 533 of the Mutual Security Act of 1954, as amended, and elsewhere.

Section 108(b), utilizing much of the language of Public Law 584, directs the President to submit annual reports to the Congress, detailing activities and expenditures made in furtherance of the purposes of S. 1154.

Section 108(c) continues without change the existing authority contained in section 7 of Public Law 860, and limits such authority to activities described in S. 1154 (in sec. 102(a)(2)) which heretofore have been conducted under Public Law 860.

Section 108(d) authorizes the continued use by the President of such of the administrative provisions of Public Law 402 as he deems necessary in implementing S. 1154. Such a provision is also found in Public Law 265 and Public Law 860. Its inclusion is needed both for these activities and for those previously conducted under Public Law 402.

J. IMMIGRATION ACT AMENDMENTS (SEC. 109)

This section of S. 1154, prior to its consideration by the committee, was designed: (1) to transfer to the Immigration and Nationality Act in the interest of orderliness and clarity of administration certain provisions now contained in Public Law 402; (2) to make it easier for students and certain of their dependents to stay together in this country for the same length of time, rather than be separated by different determinations as to length of sojourn; (3) to permit more choice between visa categories so that foreign scholars and medical personnel not covered by a U.S. Government program would not necessarily have to enter this country as exchange visitors and be subject to the provisions of Public Law 555, 84th Congress (i.e., sec. 201(b)

of Public Law 402); and (4) to allow a little more latitude for acceptance of employment by visiting students and scholars and their immediate families.

The committee has accepted all of the amendments to section 109 proposed by the executive branch. The objectives contained in the paragraph immediately above, with the exception of clause (3), are maintained, but in most cases are given considerably tighter definition. Since the committee regarded this section as auxiliary to the main purposes of S. 1154, and since it does not consider this bill an effective vehicle for proposing any extensive changes in the Immigration Act, it has not sought to deal with objectives beyond the present scope of this section. Some of the problems in this field seem to be more administrative than legislative in character. In any case, the committee understands that a full-scale study of the effects of the international exchange programs in relation to the Immigration Act is going forward under the auspices of the Judiciary Committee of the House of Representatives.

Section 109(a) authorizes the granting of nonimmigrant status under section 101(a)(15)(F) of the Immigration and Nationality Act (relating to the admission of students into the United States) to the alien spouse and minor children accompanying a student or following to join him. At present, the spouse and minor children are admitted on a temporary visitor visa, as distinct from a student visa, and often may not be admitted for a period of the same duration as that which has been allowed the student. This proposed amendment should have the effect of keeping family members together while the student is in this country.

Section 109(b), as amended, adds a new subsection (J) to section 101(a)(15) of the act, thereby establishing another category for the definition of nonimmigrant aliens. This creates a category for visa purposes which would include teachers, trainees, leaders, and specialists, and others of similar description (along with spouse and minor children) heretofore termed and admitted as "exchange visitors" under the general reference in Public Law 402 to section 101(a)(15) of the act. The principal effect of the provision is to regularize and to transfer into the act what is essentially an immigration matter. As noted below, approximately the current provisions of Public Law 555 would also apply to this new category.

Section 109(c) would amend section 241(a)(9) of the Immigration and Nationality Act by permitting a nonimmigrant (including spouse and minor children) in categories (F) and (J) to accept employment other than that specified in the terms of his admission to this country. But such employment must be needed for the support of the alien or his accompanying spouse or minor children, or for the expenses of returning to their home country. Moreover, advance permission is required from the Attorney General, who must decide that certain criteria have been met—notably a determination that the granting of permission will not deprive of employment any American citizen. It is now possible for a student himself, with the prior approval of the Immigration and Naturalization Service in all cases, to accept employment: (1) on the campus as part of his educational experience; (2) off campus, if his economic conditions have changed since admission, and if his academic work permits; (3) as practical training in connection with his field of study; and (4) during vacation periods if his educational institution agrees. Exchange visitors under Public Law 402 may now be employed for the purposes for which they are admitted; this would continue unchanged. However, the spouse and minor children admitted as temporary visitors at the present time may not be employed. This section thus would permit employment of the latter if the various conditions and restrictions are complied with. Also, as noted above, it would permit the nonimmigrant alien himself to accept employment other than that for which he is specifically admitted, provided that those same conditions are met.

Section 109(d), by amending section 245 of the Immigration and Nationality Act, transfers to the act the present provisions in section 201(b) of Public Law 402, usually referred to as Public Law 555. These require persons admitted as exchange visitors under Public Law 402, or coming under that act after having been admitted in some other way, to reside abroad for a period of 2 years after the close of their originally permitted stay here before becoming eligible to apply for an immigrant visa, for suspension of deportation and admission for permanent residence, or for adjustment to another nonimmigrant status, with minor exceptions. To the extent that the spouse and minor children of the person admitted under the new category (J) are issued a visa in that category, they, too, would be subject to the 2-year residence abroad provision. This section continues the special provision authorizing the Attorney General to waive the

2-year proviso in the case of any alien whose admission to the United States is found to be in the public interest. The waiver is subject to a request by an interested agency of the Federal Government and recommendation by the Secretary of State to the Attorney General.

The purpose of section 109(d), of course, is to continue to make certain that visitors who have received assistance under the Government exchange program will return home and utilize to the benefit of their countries—and, implicitly, of the United States—the knowledge of skill that they acquired here. In this connection, foreign governments (especially those of underdeveloped countries) are unlikely to cooperate enthusiastically in the exchange program if some of their most useful citizens choose to remain permanently in this country, and are encouraged to do so.

The classification of a nonimmigrant alien as an exchange visitor for visa purposes created by Public Law 402—proposed for regularization in a new category (J)—was designed to apply to persons entering this country in connection with the official exchange programs of the U.S. Government. In practice, however, use of the informally designated "exchange visitor visa" has been extended to cover large numbers of nonimmigrant aliens teaching or otherwise employed here who are not sponsored by the U.S. Government or supported in any way with public funds. These persons thus are automatically brought under the 2-year residence abroad requirement; the result often has been to deprive our universities of needed foreign faculty members and to encourage a flood of waiver applications. The problem lies in the fact that the Immigration and Nationality Act of 1952 omitted a provision in the Immigration Act of 1924 which permitted entry to professors and their families solely for the purpose of carrying on academic pursuits. One present relevant category (sec. 101(a)(15)(H)) of the Immigration Act is written so narrowly and interpreted so stringently that it provides no valid substitute for the earlier provision. Use of a first preference immigrant quota for these purposes relieves the situation with respect to academicians from Western Europe, for example, but provides no alternative in terms of small-quota countries, mainly the underdeveloped ones about which our academic institutions require a good deal more information. This problem is not resolved in S. 1154. At the same time, it should be added that the 2-year residence abroad provision apparently does not present serious difficulties in a majority of cases, so long as the recipient of a visa is initially made fully aware of the condition placed upon his reentry into the United States at a future date.

K. INTERNAL REVENUE CODE AMENDMENTS (SEC. 110)

Section 110 as it stood prior to committee action proposed amendments to the Internal Revenue Code of 1954 as amended, to relieve foreign students, teachers, and scholars of two burdensome tax requirements which reduce the value of their stipends (currently defined technically as "income") while they are in this country. One is the present flat 30-percent tax rate on amounts received by nonresident aliens who are not engaged in business (including employment) in the United States, and who are from countries which do not have double taxation treaties with the United States. The other requirement is the 3-percent tax withheld for social security purposes from which those foreign visitors could not expect to benefit.

In proposing remedies for these two problems, however, the original section 110 inadvertently failed to deal with the even greater difficulty represented by the flat 30-percent withholding rate on the taxable income of such foreign students and scholars. The amendments proposed by the executive branch cover not only these three issues, but also make changes in the definition of the taxable income of those persons and relieve employers of the necessity for making Federal unemployment payments on their behalf. In addition, various other minor technical amendments are included in the executive branch proposals, which were developed by the Treasury Department in cooperation with the Department of State and other interested agencies. As noted above, the Senate Committee on Finance has approved the amendments to the Internal Revenue Code with small additional perfecting language changes. The Committee on Foreign Relations has accepted all these proposals. It must be made clear that the tax reliefs provided in section 110 for the most part apply to foreign students and exchange visitors as defined in the proposed categories (F) and (J) of section 101(a)(15) of the Immigration and Nationality Act. The committee understands that the loss of revenue resulting from section 110 as a whole is likely to be negligible.

Section 110(a) amends section 117(b)(2)(A) of the code, which relates to the conditions for exclusion of scholarship and fellowship grants from gross income in the case of individuals (nonresident and resident aliens, as well as American citizens) who are not candidates for degrees. If the individual is enrolled at an educational institution but is not a candidate for a degree, amounts received as fellowships and scholarships are exempt up to $300 a month, not to exceed 36 months, provided that the grant comes from the U.S. Government, a local government unit, or a tax-exempt organization. Section 110(a) modifies this provision to include foreign governments, international organizations, and binational foundations or commissions—

created or continued pursuant to the Mutual Educational and Cultural Exchange Act of 1961.

Section 110(b)—similar in effect to section 110(a) in the unamended version of S. 1154—amends section 871 of the code, relating to the tax rate on nonresident alien individuals. In place of the current flat 30-percent rate, the amendment brings all alien students and exchange visitors (i.e., those in the United States as nonimmigrants under sec. 101(a)(15) (F) or (J) of the Immigration Act) under the lower regular graduated tax rates applicable to nonresident aliens in the United States who are engaged in trade or business.

Section 110(c) amends section 872(b) of the code, relating to exclusion from gross income of nonresident alien individuals. Such individuals now are taxable only on income "from sources within the United States." However, the Internal Revenue Service ruled that payments by a foreign employer to a person in the United States under the exchange program are income from sources within the United States, even if made in foreign currency to his dependents abroad. This ruling has little effect upon our revenues and causes considerable irritation and criticism. Section 110(c) would exempt such payments from U.S. tax while the alien under (F) or (J) is temporarily in this country.

Section 110(d) amends sections 1441 (a), (b), and (c) of the code, relating to tax withholding on nonresident aliens. As noted above, such individuals are subject to withholding of tax at the special rate of 30 percent. The 30 percent applies to the gross amount received. This often results in overwithholding and works a hardship on the individual, especially since the dollar funds are badly needed for expenses while he is here. The payment of a refund after he returns home does not provide the money at the time when the need is greatest, and results in sending dollars out of the United States rather than keeping them here. Section 110(d) permits all students and exchange visitors to be exempted from the 30-percent withholding rate on compensation for personal services and, in conjunction with section 110(g), subjects them to the 18-percent rate applied to resident aliens and American citizens. Section 110(d) also reduces the withholding from 30 to 18 percent in the case of amounts which are received as scholarships or fellowships by foreign students and exchange visitors who are not candidates for degrees and which exceed the amounts that are excluded from gross income under section 117.

Section 110(e) amends section 3121(b) of the Internal Revenue Code—relating to the definition of employment for purposes of the Federal Insurance Contributions Act (FICA)—and section 210(a) of the Social Security Act. Nonresident aliens are now subject to the 3-percent FICA, or social security tax. Since they are temporarily in the United States, they scarcely have any expectation of realizing benefits from such a taxpayment. Section 110(e) exempts foreign students and exchange visitors from payment of FICA tax on amounts earned in performing services to carry out the purposes for which they were admitted, such as studying, teaching, or conducting research. If they are employed for other purposes, consequent payments would not be exempt. (This latter provision represents a modification of the similar sec. 110(b) in the unamended version of S. 1154.) Finally, the Social Security Act is amended specifically to deny social security benefits to those individuals, except insofar as they have contributed consequent to employment for purposes other than those governing their admission to the United States.

Section 110(f) amends section 3306(c) of the code, relating to the definition of employment for purposes of the Federal Unemployment Tax Act. This amendent would relieve employers of the obligation to pay Federal unemployment taxes on the same services that are exempted from FICA tax by the preceding section 110(e). As in the case of social security, foreign students, and exchange visitors could rarely, if ever, be in a position to benefit from unemployment compensation coverage.

Section 110(g) amends sections 3401(a)(6) and 3402(f) of the code, having to do with definition of wages for withholding, and exemptions for the latter purpose. As noted above, this subsection, in conjunction with section 110(d), removes compensation paid to foreign students and exchange visitors from the 30-percent withholding rate and subjects it to the general 18-percent rate. Section 110(g) also makes it explicit that the nonresident aliens concerned will be entitled to only one withholding exemption.

Section 110(h) specifies with as much clarity and detail as possible the effective dates of the foregoing amendments to the Internal Revenue Code and the Social Security Act. In each case, the effective date is December 31, 1961.

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H.R. 8666 [11]

MUTUAL EDUCATIONAL AND CULTURAL EXCHANGE ACT OF 1961

[Conference Report No. 1197, Eighty-seventh Congress, First Session]

[September 15, 1961]

MR. HAYS, from the committee of conference, submitted the following Conference Report to accompany H.R. 8666.

* * * * * * *

STATEMENT OF THE MANAGERS ON THE PART OF THE HOUSE

The managers on the part of the House at the conference on the disagreeing votes of the two Houses on the amendment of the Senate to the bill (H.R. 8666) to provide for the improvement and strengthening of the international relations of the United States by promoting better mutual understanding among the peoples of the world through educational and cultural exchanges submit the following statement in explanation of the effect of the action agreed upon by the conferees and recommended in the accompanying conference report:

The Senate struck out all of the House bill after the enacting clause and inserted a substitute amendment. The committee of conference has agreed to a substitute for both the House bill and the Senate amendment. Except for clarifying, clerical, and necessary conforming changes, the differences are noted below:

STATEMENT OF PURPOSE (SEC. 101)

The House bill and the Senate amendment contained substantially similar statements of policy concerning the objectives and purposes of the act. However, the Senate amendment eliminated the phrase "to promote a better understanding of the United States in other countries".

The managers on the part of the House accepted the Senate language in recognition of the fact that the phrase "to increase mutual understanding between the people of the United States and the people of other countries" which was retained in the statement of policy fully covered the idea expressed in the deleted phrase.

The managers on the part of the House desire that in the administration of the various programs authorized by this bill no discrimination as to race, creed, or color be practiced in the selection of individuals to perform functions under this bill or to benefit from the provisions of the programs authorized in the bill. Similarly they desire that countries that practice such discrimination shall not be the beneficiaries of any of the programs authorized in this bill.

RESEARCH PROGRAMS (SEC. 102(b)(5))

Section 102(b)(5) of the House bill authorized the President to provide, among others, for "encouraging and promoting medical, scientific, cultural, and educational research and development". The Senate amendment made provision for "promoting and supporting" identical activities. The language in the

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[11] This publication of the Conference Report is restricted to excerpts involving internal revenue matters; Public Law 87-256, page 322, this Bulletin.

House bill was intended to make clear that this paragraph did not provide authority to finance laboratories and other costly physical installations. The Senate conferees accepted this interpretation but pointed out that there would be instances where research in and the development of specialized equipment, of modest cost, particularly in the teaching of foreign languages, could be supported under the terms of the Senate language. The House conferees therefore accepted the Senate language on the understanding that such programs envisioned by the Senate amendment merited support.

REPRESENTATION AT INTERNATIONAL MEETINGS (SEC. 102(b) (7) AND (8))

Section 102(b) (7) and (8) of the Senate amendment authorized the President to provide for U.S. representation at international nongovernment educational, scientific, and technical meetings; and participation by groups and individuals from other countries in educational, scientific and technical meetings held under American auspices in or outside the United States. The House bill contained no similar provisions. The managers on the part of the House accepted the Senate language which will make possible greater participation by eminent scientists and scholars in learned societies. This authority is similar to that provided with respect to participation in cultural meetings under section 102(a)(2) (iii) and (iv) of the bill.

SUPPORT OF INTERNATIONAL ORGANIZATION PROGRAMS (SEC. 103(C))

The Senate amendment to the House bill eliminated the ceiling of 25 percent on the U.S. share in support of educational and cultural programs of international organizations.

The managers on the part of the House accepted the Senate position that U.S. participation in these multilaterally supported programs should be to the maximum extent feasible and should include a provision for U.S. contribution of a reasonable share of the costs. The committee of conference recognized that the spelling out of a definite percentage limitation too often becomes the floor for U.S. participation. It was felt further that the nature of these programs provides the necessary incentive for active interest, including a willingness to pay a fair share on the part of participating members of these organizations.

The managers on the part of the House accepted the Senate amendment with the understanding that every effort will be made on the part of the program administrators to keep U.S. support at a level as much below 25 percent as possible, consistent with the needs of the program.

SUPERGRADES (SEC. 104(b))

Section 104(b) of the House bill authorized the President to employ such personnel as he deems necessary to carry out the provisions and purposes of the bill and to fix their compensation in accordance with the Classification Act of 1949, as amended. The Senate amendment contained a similar provision and authorized 15 positions that may be compensated without regard to the provisions of that act, 5 of which may receive not in excess of $1,000 per annum more than a GS–18. Such positions would be in addition to the number authorized by section 505 of the Classification Act. The committee of conference recognized that the administration of this program requires individuals of unusual skills. The managers on the part of the House accepted the Senate language with an amendment limiting to 10 the number of positions that may be compensated without regard to the Classification Act of 1949.

DEPENDENTS' TRAVEL EXPENSES (SEC. 104(e)(1))

Section 104(e)(1) of the House bill broadened the language of existing law to include dependent members of the immediate family of exchangees as those who may have their expenses financed under the House bill. The House report set forth limitations on the use of this authority. First, it was not intended to defray expenses of dependents of touring groups. It was to be limited to assistance to grantees who are pursuing a course of study abroad or providing instruction abroad or to distinguished scholars and others where the presence of the family will contribute to the success of the program. Second, "dependent members of their immediate families" means the spouse and dependent children who normally reside in the grantee's household. The Senate amendment contained

no comparable authority. In accepting the House language the Senate conferees expressed occurrence in the restrictions written in the House report.

SEMINARS AND COUNSELING SERVICES (SEC. 104(e)(2))

Section 104(e)(2) of the House bill authorized support for "intercultural seminars and counseling". The Senate amendment did not specify these activities. Other language in the House bill is sufficiently broad to cover "intercultural seminars". Section 104(e)(3) of the House bill, which the Senate conferees accepted, deals at greater length with counseling services. Hence the managers on the part of the House receded from the language in section 104(e)(2).

PUBLICITY AND PROMOTION (SEC. 104(e)(4))

The Senate amendment to the House bill provided that "representation" be included as part of the promotion and publicity authorized for activities of the type covered by the bill.

The managers on the part of the House accepted the Senate language in view of the fact that occasional costs of a representational nature may have to be incurred in any publicizing or promotional activities.

LOYALTY AND SECURITY INVESTIGATIONS (SEC. 104(f))

Section 104(f) of the House bill specified an investigation of all persons employed or assigned to duties under the act with respect to their loyalty and suitability in accordance with standards and procedures established by the President. The Senate amendment contained a similar provision. The Senate conferees accepted the House language with the understanding that Executive Order 10450, as amended, would be applicable in the investigative process.

TRANSFER OF FUNDS (SEC. 105(c))

Section 105(c) of the Senate amendment authorized the President to transfer, under a 10-percent limitation, funds appropriated for like purposes under this and other acts; shifts could be made in both directions. This would provide for greater consistency and unity in similar programs conducted under different statutes. For example, the student programs in some countries are now split between the International Cooperation Administration and the State Department because of the sources of funds involved, but for all practical purposes they are a single program and should be so conducted. The section is in harmony with a more general request for such transfer authority for heads of agencies made by the President in his budget message.

The House bill contained no comparable provision.

The managers on the part of the House, recognizing the value of this transfer authority in promoting overall efficiency and effectiveness, accepted the Senate amendment.

USE OF FOREIGN CURRENCIES (SEC. 105(d)(2))

The Senate amendment deleted the limitation prohibiting the waiver of the Mutual Defense Assistance Control Act of 1951 in the use of foreign currencies. The committee of conference understands that the limitation has only a very minimal effect in that it would relate only to the use of currencies for acquiring physical facilities. Generally activities carried out in the field of educational and cultural exchange are not considered assistance and therefore would not be subject to the Mutual Defense Assistance Control Act.

In consideration of the fact that the use of these currencies would require an appropriation, the managers on the part of the House accepted the Senate language.

BOARD OF FOREIGN SCHOLARSHIPS (SEC. 107(a)(1))

Section 106(a)(1) of the House bill provided for the appointment of 10 members to the Board of Foreign Scholarships. The Senate amendment provided for the appointment of 12 members to this Board.

In recognition of the added flexibility the Board would have in establishing subcommittees with the increase of two members, the managers on the part of the House accepted the Senate language.

POLITICAL AFFILIATION OF COMMISSION MEMBERS (106(b) (2))

Section 106(b)(2) of the House bill provided that, of the nine members of the U.S. Advisory Commission on International Educational and Cultural Affairs, not more than five shall be from one political party. The Senate amendment stated that the members of the Commission shall be appointed on a nonpartisan basis. In accepting the Senate language, the managers on the part of the House agreed that the Commission should not be a means of rewarding political supporters. The Commission is an important agency for carrying out the numerous educational and cultural programs authorized in the bill. It is a "working" commission that should include only individuals of the highest competence without regard to political affiliations.

COMPENSATION (SEC. 106(e))

Section 106(e) of the House bill provided that members of the Board of Foreign Scholarships, the U.S. Advisory Commission on International Educational and Cultural Affairs, and the Advisory Committee on the Arts shall receive only transportation and per diem for their work. The Senate amendment authorized compensation of $50 per diem for the members while performing their services if they were not otherwise in the employ of the U.S. Government. The managers on the part of the House recognized that most of the members of these several boards would be drawn from relatively low paid professions. Accordingly, they accepted the language of the Senate amendment.

AMENDMENTS TO THE IMMIGRATION AND NATIONALITY ACT (SEC. 109)

Section 109 of the House bill contained language amending the Immigration and Nationality Act, as amended. It incorporated into basic law a new nonimmigrant visa, category (J), to serve solely the purposes of the Mutual Educational and Cultural Exchange Act of 1961. It thus reserves the (F) visa for students other than exchange students. It also reenacted and amplified Public Law 555 of the 84th Congress but contained one modification, namely, the requirement of the finding by the Secretary of State that the 2 years' residence abroad of an exchange alien, if not occurring in the country from which he came to the United States, is in accord with the basic purpose of the exchange program. The Senate amendment contained language similar in intent but different in wording. The Senate conferees accepted the House language with amendments.

In order to permit individuals coming to the United States on public or private programs other than those authorized by this act but which further the purposes of this act, it was necessary to broaden the new category (J) visa to include such individuals. To make available the services of exchangees who possess talents desired by our universities, foundations and other institutions, the language of the House bill was modified to permit the waiver of the foreign residence requirement on the request of an interested U.S. Government agency. The language was also modified to permit an interested U.S. Government agency to request a waiver in other especial circumstances. Its terms were extended to include those who acquire exchange visitors' status under the Educational Exchange Act of 1948.

The House accepted the language of the Senate amendment which permits the alien spouse and minor children to have an (F) visa if the principal entered the United States on an (F) visa. The effect of this will be to permit an identical time period during which the family may stay in the United States.

In accepting the language for a new category (J) visa it is the intention of the conferees that the language will not preclude employment by the principal or his spouse who entered under a (J) visa when such employment is not inconsistent with the program.

AMENDMENTS TO INTERNAL REVENUE CODE (SEC. 110)

Section 110 of the Senate amendment made certain minor changes in the Internal Revenue Code of 1954, as amended, to relieve foreign students, teachers, and scholars of certain requirements which have the effect of reducing the value of their stipends while they are in this country. The House bill contained no comparable provision. The managers on the part of the House accepted the

language of the Senate amendment upon the understanding that the loss of revenue resulting from changes made by section 110 are likely to be negligible.

Section 110(a) amends section 117(b)(2)(A) of the code, which relates to the conditions for exclusion of scholarship and fellowship grants from gross income in the case of individuals (nonresident and resident aliens, as well as American citizens) who are not candidates for degrees. If the individual is enrolled at an educational institution but is not a candidate for a degree, amounts received as fellowships and scholarships are exempt up to $300 a month, not to exceed 36 months, provided that the grant comes from the U.S. Government, a local government unit, or a tax-exempt organization. Section 110(a) modifies this provision to include foreign governments, international organizations, and binational foundations or commissions "created or continued pursuant to the Mutual Educational and Cultural Exchange Act of 1961."

Section 110(b) amends section 871 of the code, relating to the tax rate on nonresident alien individuals. In place of the current flat 30-percent rate, the amendment brings all alien students and exchange visitors (i.e., those in the United States as nonimmigrants under sec. 101(a)(15) (F) or (J) of the Immigration Act) under the lower regular graduated tax rates applicable to nonresident aliens in the United States who are engaged in trade or business.

Section 110(c) amends section 872(b) of the code, relating to exclusions from gross income of nonresident alien individuals. Such individuals now are taxable only on income "from sources within the United States." However, the Internal Revenue Service ruled that payments by a foreign employer to a person in the United States under the exchange program are income from sources within the United States, even if made in foreign currency to his dependents abroad. This ruling has little effect upon our revenues and causes considerable irritation and criticism. Section 110(c) would exempt such payments from U.S. tax while the alien under (F) or (J) is temporarily in this country.

Section 110(d) amends sections 1441 (a), (b), and (c) of the code, relating to tax withholding on nonresident aliens. As noted above, such individuals are subject to withholding of tax at the special rate of 30 percent. The 30 percent applies to the gross amount received. This often results in overwithholding and works a hardship on the individual, especially since the dollar funds are badly needed for expenses while he is here. The payment of a refund after he returns home does not provide the money at the time when the need is greatest, and results in sending dollars out of the United States rather than keeping them here. Section 110(d) permits all students and exchange visitors to be exempted from the 30-percent withholding rate on compensation for personal services and, in conjunction with section 110(g), subjects them to the 18-percent rate applied to resident aliens and American citizens. Section 110(d) also reduces the withholding from 30 to 18 percent in the case of amounts which are received as scholarships or fellowships by foreign students and exchange visitors who are not candidates for degrees and which exceed the amounts that are excluded from gross income under section 117.

Section 110(e) amends section 3121(b) of the Internal Revenue Code—relating to the definition of employment for purposes of the Federal Insurance Contributions Act (FICA)—and section 210(a) of the Social Security Act. Nonresident aliens are now subject to the 3-percent FICA, or social security tax. Since they are temporarily in the United States, they scarcely have any expectation of realizing benefits from such a taxpayment. Section 110(e) exempts foreign students and exchange visitors from payment of FICA tax on amounts earned in performing services to carry out the purposes for which they were admitted, such as studying, teaching, or conducting research. If they are employed for other purposes, consequent payments would not be exempt. Finally, the Social Security Act is amended specifically to deny social security benefits to those individuals, except insofar as they have contributed consequent to employment for purposes other than those governing their admission to the United States.

Section 110(f) amends section 3306(c) of the code, relating to the definition of employment for purposes of the Federal Unemployment Tax Act. This amendment would relieve employers of the obligation to pay Federal unemployment taxes on the same services that are exempted from FICA tax by the preceding section 110(e). As in the case of social security, foreign students, and exchange visitors could rarely, if ever, be in a position to benefit from unemployment compensation coverage.

Section 110(g) amends sections 3401(a)(6) and 3402(f) of the code, having to do with definition of wages for withholding, and exemptions for the latter purpose. As noted above, this subsection, in conjunction with section 110(d), removes compensation paid to foreign students and exchange visitors from the 30-percent withholding rate and subjects it to the general 18-percent rate. Section 110(g) also makes it explicit that the nonresident aliens concerned will be entitled to only one withholding exemption.

Section 110(h) specifies with as much clarity and detail as possible the effective dates of the foregoing amendments to the Internal Revenue Code and the Social Security Act. In each case, the effective date is December 31, 1961.

WAYNE L. HAYS,
LEONARD FARBSTEIN,
JOHN S. MONAGAN,
E. ROSS ADAIR,
HORACE SEELY-BROWN, JR.,
Managers on the Part of the House.

[H.R. 6302] [12]
ESTABLISHING A TEACHING HOSPITAL FOR HOWARD UNIVERSITY

[Senate Report No. 876, Eighty-seventh Congress, First Session, Calendar No. 858]

[September 5, 1961]

Mr. MORSE, from the Committee on Labor and Public Welfare, submitted the following report to accompany H.R. 6302.

The Committee on Labor and Public Welfare, to whom was referred the bill H.R. 6302, having considered the same, report favorably thereon, without amendment, and recommend that the bill do pass.

This bill would provide modern teaching hospital facilities for Howard University, thereby assisting the university in training medical and allied personnel and in providing hospital services for the community. For this purpose the bill would (1) authorize transfer of the present Freedmen's Hospital to Howard University pursuant to an agreement between the university board of trustees and the Secretary of Health, Education, and Welfare; (2) authorize appropriation of such sums as may be necessary for the construction of a new hospital for the university and for partial support of its operation; and (3) provide for continued employment of the Freedmen's Hospital employees and maximum consideration of their interest after the transfer.

Hearings on a similar bill in the 85th Congress (S. 3626) were held by a special subcommittee of the Senate Committee on Labor and Public Welfare August 7, 1958, and the bill was reported favorably to the Senate by the full committee without amendment on August 12, 1958.

BACKGROUND

Freedmen's Hospital was started by the Freedmen's Bureau of the Federal Government in the 1860's as an emergency facility to provide care for destitute and sick Negroes who came to Washington in large numbers during and immediately after the Civil War. It has been continued ever since by annual appropriation acts without substantive legislation to establish its permanent role. The present plant consists of a main building built in 1908, with wings added in 1911 and 1931, and an annex built in 1940 for tuberculosis patients. The hospital is located on land belonging to Howard University and is used by Howard as its principal teaching hospital. Patients are admitted on the basis of medical need and the capacity of the hospital to treat them. They include full-pay, part-pay, and indigent patients. Some have their own private physicians. Howard University furnishes the attending staff of physicians for patients who do not have their own private physicians. The hospital, however, is federally owned and operated, under the direction of the Department of Health, Education, and Welfare. Unlike the attending and courtesy staff of physicians, the hospital

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[12] This publication of the Committee Report is restricted to excerpts involving internal revenue matters; Public Law 87-262, page 333, this Bulletin.

personnel, including nurses, interns, residents, attendants, and administrative personnel, are Federal employees, responsible to the hospital superintendent who is also a Federal civil service employee. Freedmen's Hospital is the only general community hospital operated by the Federal Government.

The need of new hospital facilities for Howard University's medical teaching program and for proper care of the patients at Freedmen's Hospital has long been recognized, and has been vividly reported by Members of both Houses of Congress who have made personal visits to the site. The executive branch and committees of the Congress, however, have believed that construction of a new plant should be considered in connection with a policy determination as to the future of the hospital. The present legislation will end the anomaly of Federal operation of Freedmen's as a community hospital, and will establish the Federal Government's role in relation to the new hospital on the same basis as its relation to Howard University as a whole.

Howard University is a private, self-governing institution, operating under a Federal charter granted in 1867 (14 Stat. 438). Pursuant to legislation enacted in 1928 (45 Stat. 1021), Howard University receives an annual appropriation from the Federal Government in partial support of its operation. The Federal Government in recent years also has carried on a large building program to provide the university with the physical facilities necessary for its work. Such Federal assistance has been provided in recognition of Howard University's importance in meeting the Nation's educational needs. This has been particularly true of medical education. Nearly one-half of the Negro students enrolled in the medical schools of the United States are trained at Howard.

Howard University also has become important internationally, with the highest percentage of foreign students of any American university, and many distinguished foreign visitors. In 1960, the university enrolled 1,861 foreign students from 48 countries in Asia, Africa, Europe, North, Central, and South America, and 17 island possessions of the British, French, and Dutch Indies.

The Secretary of Health, Education, and Welfare, in 1955, appointed a study commission of distinguished citizens, representative of medicine and medical education, hospital administration, and community interests, to study the need and the future role of Freedmen's Hospital. The study commission submitted its unanimous recommendations, including the following:

> Neither the education, research, or service programs of the university and its teaching hospital, nor the public and international relations objectives of the Nation, can be fully achieved by the obsolete, outmoded, and uneconomical general hospital plant and facilities of Freedmen's Hospital. Accordingly, the present plant should be replaced by a modern plant, with facilities comparable to the recently constructed hospitals of George Washington and Georgetown Universities.
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> In order that Howard University and its teaching hospital may achieve their education, research, and service objectives under full racial integration, and to assure requisite hospital discipline, effective coordination, and control of universitywide professional programs, good business management, and financial support, it is recommended that ownership, control, and supervision be vested in the Howard University Board of Trustees.

The full text of the study commission's report is printed in the transcript of the Senate hearings of August 7, 1958.

The medical education program at Howard University and its medical service to the community will be strengthened by the new facilities and unified administration provided by this bill. Medical teaching, medical research, and medical service are inseparable in a strong university program, and this legislation will make the new hospital an integral part of Howard University with the advantages of unified responsibility and control.

When this committee held hearings on similar legislation in 1958 the only opposition was based on the fact that employees transferring from the present Freedmen's Hospital to the new Howard University Hospital would no longer be Government employees. The legislation, however, provides special assurances to protect employees as far as is reasonably possible from any substantial disadvantage resulting from this change from Government to private employment; also to maintain an adequate staff and continuity of service for the new hospital.

Supplementing the legislation, the Civil Service Commission will extend its present separated career employees program to give career and career-conditional employees who transfer to Howard University 3 years from the transfer date (instead of the 90 days generally allowed) in which to claim reemployment priority in the Federal civil service if separated in good standing from the university. Upon filing such a claim an eligible employee would remain on the separated career employee roster and be entitled to priority in Federal employment for a further period of either 2 years (for career employees) or 1 year (for career-conditional employees). Since the entire program for separated career employees is prescribed by the Civil Service Commission's regulations rather than by statute, this liberalization does not call for any provision in the bill. The Commission's statement is set out in full in the published hearings of August 7, 1958, on the predecessor of the present bill, S. 3626 of the 85th Congress. This safeguard will permit employees to transfer and have actual experience as employees of Howard University for more than 3 years while still retaining their preference rights for reemployment in the Federal Government.

The committee is convinced that the interests of the hospital employees are safeguarded and the interests of the public promoted by the proposed legislation.

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SECTION-BY-SECTION DESCRIPTION OF THE BILL

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Section 2. Provisions for employees of hospital

Subsection (a) of this section requires that the agreement of transfer contain provisions guaranteeing that individuals who are career and career-conditional employees of Freedmen's Hospital on the day before the transfer of the hospital will be offered an opportunity to transfer to Howard University, except for any who have received at least 6 months' notice before the transfer of the hospital that their positions are to be abolished. In addition, the agreement must provide that Howard University (1) will not reduce the salary levels for employees who transfer to it, (2) will deposit the salary deductions and agency contributions required by the Civil Service Retirement Act and the Federal Employees' Group Life Insurance Act, (3) will provide other employee benefits as nearly equivalent as practicable to those generally enjoyed by civilian employees of the United States at the time of the transfer (among the benefits which would be provided under this language are the benefits under the Federal Employees Health Benefits Act of 1959), and (4) in determining seniority rights of its employees, will credit service with Freedmen's Hospital performed by such employees who transfer, on the same basis as it would credit such service if it were performed for the university. The agreement must also provide that the transfer will become effective not later than the beginning of the second month which begins after construction of the new hospital facilities authorized by section 3 of the bill is commenced.

Subsection (b) of section 2 directs the Department of Health, Education, and Welfare to make every reasonable effort to place in other comparable Federal positions those individuals who are career or career-conditional employees of Freedmen's Hospital on the date of enactment of the bill who do not transfer to Howard University.

Subsection (c) of section 2 provides that those employees of Freedmen's Hospital on the date of enactment of the bill who transfer to Howard University shall, so long as they are continuously in the employ of Howard University, be regarded as continuing in the employ of the United States for the purposes of the Civil Service Retirement Act and the Federal Employees' Group Life Insurance Act of 1954. This subsection further provides that for purposes of section 3121(b) of the Internal Revenue Code of 1954 and section 210 of the Social Security Act, service performed by such transferred employees during their employment at Howard University shall be regarded as though performed in the employ of the United States. Considering these individuals as Federal employees would result in their exclusion from coverage under the old-age, survivors, and disability insurance system, since Federal employees are excluded from such coverage if they are covered by another Federal retirement system—in this case, the civil service retirement system.

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[H.R. 7500] [13]
THE PEACE CORPS

[House of Representatives Report No. 1115, Eighty-seventh Congress, First Session]

[September 22, 1961]

MR. MORGAN, from the Committee on Foreign Affairs submitted the following report to accompany H.R. 7500

The Committee on Foreign Affairs, to whom was referred the bill (H.R. 7500) to provide for a Peace Corps to help the peoples of interested countries and areas in meeting their needs for skilled manpower, having considered the same, report favorably thereon with amendments and recommend that the bill as amended do pass.

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TITLE II—AMENDMENT OF INTERNAL REVENUE CODE AND SOCIAL SECURITY ACT

TAXATION OF ALLOWANCES

SEC. 201. (a) Section 912 of the Internal Revenue Code of 1954 (relating to exemption from gross income for certain allowances) is amended by adding at the end thereof the following new paragraph:

(3) PEACE CORPS ALLOWANCES.—In the case of an individual who is a volunteer or volunteer leader within the meaning of the Peace Corps Act and members of his family, amounts received as allowances under section 5 and 6 of the Peace Corps Act other than amounts received as—

(A) termination payments under section 5(c) or section 6(1) of such Act,

(B) leave allowances,

(C) if such individual is a volunteer leader training in the United States, allowances to members of his family, and

(D) such portion of living allowances as the President may determine under the Peace Corps Act as constituting basic compensation.

(b) Section 1303(b) of the Internal Revenue Code of 1954 (relating to definition of back pay) is amended by adding at the end thereof the following new paragraph:

(4) Termination payments under section 5(c) or section 6(1) of the Peace Corps Act which are received or accrued by an individual during the taxable year on account of any period of service, as a volunteer or volunteer leader under the Peace Corps Act, occurring prior to the taxable year.

(c) Section 3401(a) of the Internal Revenue Code of 1954 (relating to the definition of wages for purposes of the collection of income tax at source on wages) is amended by striking out the period at the end of paragraph (12) and inserting in lieu thereof "; or", and by adding at the end thereof the following new paragraph:

(13) pursuant to any provision of law other than section 5(c) or 6(1) of the Peace Corps Act, for service performed as a volunteer or volunteer leader within the meaning of such Act.

(d) The amendments made by subsections (a) and (b) of this section shall apply with respect to taxable years ending after March 1, 1961. The amendment made by subsection (c) shall apply with respect to remuneration paid after the date of the enactment of this Act.

SOCIAL SECURITY COVERAGE

SEC. 202. (a)(1) Section 3121(i) of the Internal Revenue Code of 1954 (relating to computation of wages for purposes of the Federal Insurance Contributions Act) is amended by adding at the end thereof the following new paragraph:

(3) PEACE CORPS VOLUNTEER SERVICE.—For purposes of this chapter, in the case of an individual performing service, as a volunteer or volunteer

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[13] This publication of the Committee Report is restricted to excerpts involving internal revenue matters; Public Law 87-293, page 336, this Bulletin.

leader within the meaning of the Peace Corps Act, to which the provisions of section 3121(p) are applicable, the term "wages" shall, subject to the provisions of subsection (a)(1) of this section, include as such individual's remuneration for such service only amounts paid pursuant to section 5(c) or 6(1) of the Peace Corps Act.

(2) Section 3121 of such Code is amended by adding at the end thereof the following new subsection:

(p) PEACE CORPS VOLUNTEER SERVICE.—For purposes of this chapter, the term "employment" shall, notwithstanding the provisions of subsection (b) of this section, include service performed by an individual as a volunteer or volunteer leader within the meaning of the Peace Corps Act.

(3) The first sentence of section 3122 of such Code (relating to Federal service) is amended by inserting after "section 3121(m)(1) are applicable," the following: "and including service, performed as a volunteer or volunteer leader within the meaning of the Peace Corps Act, to which the provisions of section 3121(p) are applicable,".

(4) Section 6051(a) of such Code (relating to receipts for employees) is amended by adding at the end thereof the following new sentence: "In the case of compensation paid for service as a volunteer or volunteer leader within the meaning of the Peace Corps Act, the statement shall show, in lieu of the amount required to be shown by paragraph (5), the total amount of wages as defined in section 3121(a), computed in accordance with such section and section 3121(i)(3)."

(b)(1) Section 210 of the Social Security Act (42 U.S.C. 410) is amended by adding at the end thereof the following new subsection:

Peace Corps Volunteer Service

(o) The term "employment" shall, notwithstanding the provisions of subsection (a), include service performed by an individual as a volunteer or volunteer leader within the meaning of the Peace Corps Act.

(2) Section 209 of such Act (42 U.S.C. 409) is amended by adding at the end thereof the following new paragraph:

For purposes of this title, in the case of an individual performing service, as a volunteer or volunteer leader within the meaning of the Peace Corps Act, to which the provisions of section 210(o) are applicable, (1) the term "wages" shall, subject to the provisions of subsection (a) of this section, include as such individual's remuneration for such service only amounts certified as payable pursuant to section 5(c) or 6(1) of the Peace Corps Act, and (2) any such amount shall be deemed to have been paid to such individual at the time the service, with respect to which it is paid, is performed.

(3) The first sentence of section 205(p)(1) of such Act (42 U.S.C. 405(p)(1)) is amended by inserting after "are applicable," the following: "and including service, performed as a volunteer or volunteer leader within the meaning of the Peace Corps Act, to which the provisions of section 210(o) are applicable,".

(c) The amendments made by subsections (a) and (b) of this section shall apply with respect to service performed after the date of the enactment of this Act. In the case of any individual who is enrolled as a volunteer or volunteer leader under section 16(a) of this Act, such amendments shall apply with respect to service performed on or after the effective date of such enrollment.

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TITLE II—AMENDMENT OF INTERNAL REVENUE CODE AND SOCIAL SECURITY ACT

The Committee on Foreign Affairs has received the following letter from the Committee on Ways and Means:

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COMMITTEE ON WAYS AND MEANS,
HOUSE OF REPRESENTATIVES,
Washington, D.C., August 31, 1961.

Hon. THOMAS E. MORGAN,
Chairman, Committee on Foreign Affairs,
U.S. House of Representatives.

MY DEAR MR. CHAIRMAN: In accordance with the agreement which has been worked out between the Committee on Ways and Means and the Committee on Foreign Affairs, I am enclosing the material relative to the tax and social security provisions of the Peace Corps bill.

As I indicated to you in my letter of yesterday, it is the suggestion of the Committee on Ways and Means that the provisions relating to taxes and social security be included as a separate title in the Peace Corps bill. For that reason, the enclosed material is for inclusion in the committee report which your committee will make on the bill to the House of Representatives.

As you know, since the subjects of taxes and social security are within the jurisdiction of the Committee on Ways and Means, it was agreeable with you that our committee would make the policy decisions on these provisions and draft language carrying out these decisions. The attached material constitutes the report of the Committee on Ways and Means on this separate title and contains an expression of dissent by the Republican members of the committee.

With kind personal regards, I am,

Sincerely yours,

WILBUR D. MILLS, *Chairman.*

The explanation furnished to the Committee on Foreign Affairs by the Committee on Ways and Means is set forth below.

A. GENERAL STATEMENT

Title II of the bill contains amendments to the Internal Revenue Code of 1954 and to the Social Security Act. The provisions of this title were considered and approved by the Committee on Ways and Means and referred to the Committee on Foreign Affairs. In general, the effect of these amendments is to treat Peace Crops volunteers and volunteer leaders in a manner similar to enlisted men in the Armed Forces for tax purposes and for social security purposes.

Tax provisions.—Section 912 of the Internal Revenue Code as amended by this bill excludes from gross income of Peace Corps volunteers and volunteer leaders certain amounts received by them as living or travel allowances.

The exclusion provided under the amendment does not apply to the so-called "termination payments" received by volunteers and volunteer leaders ($75 per month in the case of volunteers), to leave allowances (small cash amounts paid to volunteers, volunteer leaders and, in some cases, the spouses and children of volunteer leaders on leave), and living allowances paid to the spouses and minor children of volunteer leaders while such leaders are training in the United States. The exclusion also does not apply to such portion of living allowances as the President may determine constitutes basic compensation. Generally, this last category is designed to tax amounts received for such incidental articles as cigarettes, toothpaste, etc., which military personnel must buy out of taxable base pay. A living allowance provided for a spouse and minor children of a volunteer leader while he is not in training in the United States will be excluded from gross income except to the extent that the President determines that such allowance is part of the volunteer leader's basic compensation.

The bill also amends section 1303(b) of the Internal Revenue Code of 1954 to permit a volunteer or volunteer leader to treat his termination payment allocable to service in more than 1 taxable year as "back pay" if such payment is more than 15 percent of his gross income for the year. Under this provision, the tax he would have to pay in the year in which the termination payment is received may not be greater than the tax he would have paid if the amount of the termination payment had been received ratably over his period of service. This prevents the Peace Corps volunteer, or volunteer leader, from losing part of the benefit of his personal exemptions during his years of service in the Peace Corps. Moreover, this provision accords the same treatment to termination payments as the law presently provides for other types of back pay and "bunched income." This treatment is justified by the fact that it is the Government decision not to pay these amounts until termination of the volunteer's service, rather than the volunteer's choice not to receive it currently.

The bill provides for withholding income tax from termination payments at the time such payments are made to Peace Corps volunteers or volunteer leaders. No other payments made to a volunteer or volunteer leader for services in the Peace Corps will be subject to withholding, although such payments may be includible in gross income.

The income tax amendments will apply with respect to taxable years ending after March 1, 1961. The withholding tax amendment will apply to amounts paid after the date of enactment.

Social security coverage.—The bill provides for coverage of services performed by Peace Corps volunteers and volunteer leaders under the old-age, survivors, and disability insurance program. During any period of service as a Peace Corps volunteer or volunteer leader, an individual will be deemed to be performing service in covered employment and will also be deemed to have received wages in each month of his service at the rate on which his termination payments will be based.

It is considered desirable that Peace Corps volunteers and volunteer leaders be afforded the protection provided by the old-age, survivors, and disability insurance program. Social security coverage of Peace Corps service will enable those who come from covered work to maintain continuity of protection and will enable young people who have had no previous social security coverage to begin building up protection under old-age, survivors, and disability insurance which they can continue when they leave the Peace Corps and enter other employment. The survivor protection obtained through social security coverage of such individuals will be especially important during the years immediately following the termination of an individual's Peace Corps service.

B. DETAILED EXPLANATION

Section 201. Taxation of allowances

(a) *Exemptions from gross income.*—Section 201(a) of the bill amends section 912 of the Internal Revenue Code of 1954, relating to exemptions from gross income for certain allowances, by adding a new paragraph (3) thereto.

Section 912(3) provides that there shall not be included in gross income and shall be exempt from income taxation certain amounts received as allowances by a Peace Corps volunteer, under section 5 of the act, and by a Peace Corps volunteer leader and members of the leader's family, under section 6 of the act.

Section 5(b) of the bill provides for the payment of living, travel, and leave allowances. The new paragraph (3) of section 912 of the 1954 code applies to these allowances. Section 5(b) of the bill also provides for providing (in kind) housing, transportation, supplies, equipment, subsistence (food and incidentals), and clothing. To the extent items so provided in kind are in lieu of the providing of allowances expressly described in section 912(3), they are to be treated as allowances so described.

Section 6 of the bill provides for similar allowances for, and the furnishing of similar items in kind to, the volunteer leaders of the Peace Corps. In addition, under paragraph (2) of section 6, the spouse and minor children of a volunteer leader may, under exceptional circumstances, receive such living, travel, and leave allowances, and such housing, transportation, subsistence, and essential special items of clothing, as the President may determine. The treatment under section 912(3) of these items provided in kind is to be the same as the treatment described above in connection with the items provided in kind under section 5 of the bill.

Paragraph (3) of section 912 of the code specifically excludes from the exemption provided by such paragraph (*a*) termination payments made under sections 5(c) and 6(1) of the bill, (*b*) all leave allowances, whether payable to a volunteer, a volunteer leader, or members of the family of a volunteer leader, (*c*) allowances to members of the family of a volunteer leader who is undergoing training in the United States, and (*d*) such portion of living allowances as the President may determine constitutes basic compensation.

(b) *Termination payments.*—Subsection (b) of section 201 of the bill amends section 1303(b) of the Internal Revenue Code of 1954 (relating to the definition of back pay) by adding a new paragraph (4) at the end thereof. Under the new paragraph (4) the definition of the term "back pay" is expanded to include termination payments under section 5(c) or section 6(1) of the bill received or accrued during the taxable year by an individual for services performed prior to the taxable year as a volunteer or volunteer leader in the Peace Corps.

Subsection (a) of section 1303 of the Internal Revenue Code of 1954 (relating to the limitation on tax) provides that if the amount of back pay (as defined in section 1303(b) of the Internal Revenue Code of 1954) exceeds 15 percent of the gross income of the individual for the taxable year, the part of the tax for such year which is attributable to the inclusion of the back pay in gross income shall not exceed the sum of the increases in the taxes which would result from the inclusion of the respective portions of the back pay in gross income for the taxable years to which such portions are respectively attributable, as determined under regulations prescribed by the Secretary of the Treasury or his delegate.

(c) *Income tax withholding.*—Subsection (c) of section 201 of the bill amends section 3401(a) of the Internal Revenue Code of 1954 (relating to the definition of "wages" subject to the collection of income tax at source on wages) by adding a new paragraph (13) at the end thereof, applicable to remuneration for service performed as a volunteer or volunteer leader in the Peace Corps. Under the new paragraph (13), the term "wages" will not include remuneration paid for such service unless the remuneration is paid pursuant to section 5(c) or 6(1) of the bill, relating to termination payments . This amendment will apply to remuneration paid after the date of enactment of this bill.

Section 202. Social security coverage

(a) *Amendments of Internal Revenue Code of 1954.*—Subsection (a) of section 202 of the bill amends several sections of the Internal Revenue Code of 1954 relating to the taxes imposed by the Federal Insurance Contributions Act (chapter 21 of such Code) with respect to remuneration for service performed as a volunteer or volunteer leader in the Peace Corps. The amendments apply with respect to service performed after the date of enactment of this bill except that, in the case of any individual who is enrolled as a volunteer or volunteer leader pursuant to section 16(a) of the bill, the amendments apply with respect to service performed on or after the effective date of such enrollment.

(a)(1) *Computation of wages for Peace Corps volunteer service.*—Subsection (a)(1) of section 202 of the bill amends section 3121(i) of the Internal Revenue Code of 1954 by adding a new paragraph (3) at the end thereof. The new paragraph (3) provides that, in the case of remuneration for service as a volunteer or volunteer leader, only amounts paid pursuant to section 5(c) or 6(1) of the bill (relating to termination payments), up to a maximum of $4,800 paid in any calendar year, will count as "wages" for purposes of the Federal Insurance Contributions Act. The taxes imposed by such act will apply as and when the amounts are paid pursuant to section 5(c) or 6(1) of the bill, regardless of the time of performance of the services for which such amounts are paid.

(a)(2) *Peace Corps volunteer service.*—Subsection (a)(2) of section 202 of the bill amends section 3121 of the Internal Revenue Code of 1954 by adding a new subsection (p) at the end thereof. Under the new subsection (p), service performed by an individual as a volunteer or volunteer leader within the meaning of the bill will constitute "employment" for purposes of the Federal Insurance Contributions Act.

(a)(3) *Determinations with respect to Federal service.*—Subsection (a)(3) of section 202 of the bill amends section 3122 of the Internal Revenue Code of 1954 so as to make it clear that the basic determinations with respect to employment and wages in the case of service performed by volunteers and volunteer leaders in the Peace Corps will be made by the head of the Federal agency having control of such service, or by such agents as such head may designate.

(a)(4) *Receipts for volunteers and volunteer leaders.*—Subsection (a)(4) of section 202 of the bill amends section 6051(b) of the Internal Revenue Code of 1954, to provide a special rule with respect to the information to be contained on employees' tax receipts in the case of remuneration paid to volunteers and volunteer leaders in the Peace Corps. Under the amendment, the amount to be shown as wages for purposes of the Federal Insurance Contributions Act, in the case of such volunteers and volunteer leaders, will be the amount paid pursuant to section 5(c) or 6(1) of the bill, up to a maximum of $4,800 paid in any calendar year.

(b) *Amendments to title II of the Social Security Act.*—Subsection (b) of section 202 of the bill, which amends several sections of title II of the Social Security Act, relates to credits under the old-age, survivors, and disability insurance program with respect to remuneration for service performed as a volunteer or volunteer leader in the Peace Corps. The amendments apply with respect to service performed after the date of enactment of this bill except that, in the case of any individual who is enrolled as a volunteer or volunteer leader pursuant to section 16(a) of the bill, the amendments apply with respect to service performed on or after the effective date of such enrollment.

(b)(1) *Peace Corps volunteer service.*—Subsection (b)(1) of section 202 of the bill amends section 210 of the Social Security Act by adding a new subsection (o) at the end thereof. Under the new subsection (o), service performed by an individual as a volunteer or volunteer leader within the meaning of the bill will constitute "employment" for purposes of title II of the Social Security Act.

(b)(2) *Computation of wages for Peace Corps volunteer service.*—Subsection (b)(2) of section 202 of the bill amends section 209 of the Social Security Act by adding a new paragraph at the end thereof. The new paragraph provides that, in the case of remuneration for service as a volunteer or volunteer leader, only amounts certified as payable pursuant to section 5(c) or 6(1) of the bill (relating to termination payments) will count as "wages" for purposes of the old-age, survivors, and disability insurance program. (This is subject to the limitation in section 209(a) of the Social Security Act that not more than $4,800 of the remuneration may be counted as wages for this purpose in any year.) The amounts so certified as payable would, for purposes of title II of the Social Security Act, be deemed to have been paid when the service, with respect to which the amounts are paid, is performed no matter when the payment is actually made.

(b)(3) *Determinations with respect to Federal service.*—Subsection (b)(3) of section 202 of the bill amends section 205(p)(1) of the Social Security Act so as to make it clear that the basic determinations with respect to employment and wages in the case of service performed by volunteers and volunteer leaders in the Peace Corps will be made by the head of the Federal agency having control of such service, or by such agents as such heads may designate.

C. EXPRESSION OF DISSENT BY THE REPUBLICAN MEMBERS OF THE COMMITTEE ON WAYS AND MEANS RELATIVE TO TITLE II OF H.R. 7500

Title II of H.R. 7500 relates to participants in the so-called Peace Corps and specifically pertains to social security coverage for those participants and the tax treatment accorded certain remuneration and allowances they are scheduled to receive.

Without commenting in these views on the Peace Corps concept itself, we express opposition to the proposal in title II to proliferate our Federal tax laws with special provisions relating solely and exclusively to Peace Corps problems. Under the amendments to the Internal Revenue Code provided in title II exclusion from tax liability would be provided for allowances received for living expenses. In addition, with respect to remuneration that is subject to tax, a "spread-back" provision would be applicable so that such compensation could be allocated over the period in which it is earned.

Either or both of these provisions may have merit but we believe it is wrong to attempt to gear our general tax structure, affecting as it does all our taxpayers, to the Peace Corps. A more desirable course in our view would be for the compensation schedules of the Peace Corps to be so adjusted that existing code provisions could be relied on to produce the intended result whatever it may be.

We presently have tax laws and regulations which relate to persons who work abroad for private concerns and for the Federal Government either as civilians or military personnel. During the executive consideration of title II there was no demonstration of any need to conform our tax laws to the pay schedules to be set up in the Peace Corps. As we have said, there is every reason that the pay schedules in the Peace Corps be made to conform to our present tax laws. The proposed changes raise question as to who is doing the wagging—the dog or the tail.

We believe that the Ways and Means Committee is setting an unwise precedent in altering the tax laws to fit the pay schedules of any group unless there is a basic difference in structure between that group and groups already covered by tax laws and tax regulations. There seems to be no reason for different treatment for the Peace Corps from that accorded many other enterprises, governmental as well as private, to which the Peace Corps pay and allowance schedules could be conformed. The provisions of title II will needlessly add new provisions to our tax laws and will also add to the complexity in the application of our tax laws to the members of the Peace Corps.

An administration spokesman, in explaining the "spread-back" provision allowing Peace Corps members to spread-back over 24 months the lump-sum payments they received at the end of their 2-year service, stated that it was a policy decision of the administration that the members of the Corps should not receive this money monthly. The basis for such a policy decision was the fear that the members would use the money to improve their allowed standard of living overseas. This amazing and shocking theory prompts us to comment that if the members of the Peace Corps are so lacking in self-discipline that they cannot be relied on in this minor respect, they are certainly going to fail

in meeting the even more rigid discipline requirements necessary to do the job it is contemplated they will be called upon to do as members of the Peace Corps.

We cannot allow the unsound reasoning and unwise precedent implicit in approval of the special tax treatment for members of the proposed Peace Corps which is included in this bill to go uncontested.

NOAH M. MASON.
JOHN W. BYRNES.
HOWARD H. BAKER.
THOMAS B. CURTIS.
VICTOR A. KNOX.
JAMES B. UTT.
JACKSON E. BETTS.
BRUCE ALGER.
STEVEN B. DEROUNIAN.
HERMAN T. SCHNEEBELI.

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[H.R. 7057] [14]

TAX TREATMENT OF CERTAIN CLAYS AND SHALE FOR TAXABLE YEARS BEGINNING PRIOR TO 1961

[House of Representatives Report No. 939, Eighty-seventh Congress, First Session]

[August 15, 1961]

Mr. IKARD of Texas, from the Committee on Ways and Means, submitted the following report to accompany H.R. 7057.

The Committee on Ways and Means, to whom was referred the bill (H.R. 7057) relating to the application of the terms "gross income from mining" and "ordinary treatment processes normally applied by mine owners or operators in order to obtain the commercially marketable mineral product or products" to certain clays and shale for taxable years beginning before December 14, 1959, having considered the same, report favorably thereon with an amendment and recommend that the bill as amended do pass.

The amendment is as follows:

Page 2, line 7, strike out "paragraphs (3)(A), (3)(B), and (5)(B)" and insert "paragraphs (3), (5)(A), and (6)".

The committee amendment is a technical amendment so that the references to the enumerated paragraphs of section 613(b) of the Internal Revenue Code of 1954 are to the paragraphs in force for taxable years beginning before January 1, 1961.

I. SUMMARY OF THE BILL

This bill provides in the case of brick and tile clay and certain other clays that insofar as the holding in the *Cannelton Sewer Pipe* case departs from the principles previously enunciated in the *Cherokee Brick and Tile Company* and *Merry Brothers Brick and Tile Company* cases, it is not to be applied retroactively for years beginning before the Supreme Court granted certiorari in the *Cannelton* case on December 14, 1959. Thus in the case of brick and tile clay and any other clay or shale where the finished product is the first commercially marketable product, percentage depletion for these past years to the extent they are open will be based upon the value of the finished or end product. This bill was reported unanimously by your committee.

II. GENERAL STATEMENT

This bill is concerned with the proper base for the application of percentage depletion in the case of various clays and shale for the period *before* the Supreme Court granted certiorari in the *Cannelton Sewer Pipe* case, i.e., for taxable years beginning before December 14, 1959. It is important to note that the question presented here is not what the base for percentage depletion should be in the

[14] Public Law 87-312, page 339, this Bulletin.

future, since this was decided quite specifically by Congress in the so-called Gore amendment to the Public Debt and Tax Rate Extension Act of 1960. (That act specified for the future, not only in the case of clay, but in the case of other mineral products as well, the so-called cutoff points at which the various percentage depletion rates were to be applied, or which processes could be applied to the mineral products before determining their value for percentage depletion purposes.)

The problem presented here is to determine, in view of all the circumstances then existing, what the taxpayers involved could properly have expected their percentage depletion base to be in the case of clay in years prior to the decision by the Supreme Court in *U.S.* v. *Cannelton Sewer Pipe Company* (364 U.S. 76 (June 27, 1960)). To make such a determination a résumé of the historical background is required.

A. HISTORICAL BACKGROUND

Percentage depletion was provided for ball and sagger clay in 1942 and in 1947 for china clay. In 1951 brick and tile clay, shale and refractory and fire clay were added to the list of clays eligible for percentage depletion. In that act the rate of depletion for brick and tile clay and shale was set at 5 percent and the rate for ball, sagger, china and refractory and fire clay at 15 percent. In the 1960 amendments, instead of referring to refractory and fire clay as such the code was amended to provide percentage depletion at a 15 percent rate for "clay used or sold for use for purposes dependent on its refractory properties." Also, in the category of clay receiving percentage depletion at the 5 percent rate, instead of referring to brick and tile clay as such, the 1960 legislation provided for percentage depletion for "clay used, or sold for use, in the manufacture of building or paving brick, drainage and roofing tile, sewer pipe, flower pots, and kindred products."

The statute provides that the percentage depletion rates referred to above are to be applied to the "gross income from the property." Congress in the Revenue Act of 1943 defined the "gross income from the property" as the "gross income from mining." The term "mining" in turn was considered to include—

> not merely the extraction of the ores or minerals from the ground but also the ordinary treatment processes normally applied by the mine owners or operators in order to obtain the commercially marketable mineral product or products.

This definition was made applicable to taxable years beginning after December 31, 1931. Although this definition has recently been changed (by the Gore amendment in 1960) it was fully applicable for the period with which this bill is concerned; namely, taxable years beginning prior to December 14, 1959. The Senate Finance Committee report on the Revenue Act of 1943 stated that—

> The purpose of this provision is to make certain that the ordinary treatment processes which a mineowner would normally apply to obtain a marketable product shall be considered as a part of the mining operation * * *.

The issue presented to your committee was what represents the ordinary treatment processes normally applied by the mineowners or operators in order to obtain the commercially marketable mineral product or products. In 1954 a district court in ruling for the taxpayer in the *Cherokee Brick and Tile Company* case (122 F. Supp. 59) held that in the case of the brick and tile clay involved in that case there was no commercially marketable product prior to the finished product and, therefore, that percentage depletion in this case should be based on the finished product. This case was appealed to the Court of Appeals, Fifth Circuit. In affirming (in 1955) the decision of the lower court, that court held:

> The statutory language is clear and unambiguous, which is that gross income from mining must include the income from ordinary treatment processes which must be applied to the ore or mineral in order to obtain the commercially marketable mineral product, that is, the first product which is marketable in commerce. There is no provision in the statute for excluding any process before such a marketable product is reached. The only restriction is that the processes must be the ordinary treatment processes normally applied by mineowners or operators.
>
> The complaint alleges that, of the brick and tile clay mined in the United States, there is opportunity for the sale of only a negligible quantity before it is put into the form of burnt brick and tile. This allegation is admitted

in the answer of the appellant. For this and other reasons (but mainly for this one) stated in the opinion of the district court, above cited, the judgment appealed from should be affirmed.

Substantially similar positions to that described above were taken by three other Circuit Courts of Appeals (the Third, Fourth and Tenth), the U.S. Tax Court, and district courts in the Sixth and Ninth Circuits. In fact, with the exception of a district court case (*Dragon Cement Company* v. *United States*, 244 F. 2d 513) which was subsequently reversed by the court of appeals, there were no decisions on this issue in favor of the Government prior to the *Cannelton* case. The Government in 1957 asked the Court of Appeals, Fifth Circuit, to reconsider its decision in the *Cherokee* case as a part of its consideration of *United States* v. *Merry Brothers Brick and Tile Company* (242 F. 2d 708). In the *Merry Brothers* decision, the court of appeals again upheld its *Cherokee* decision in holding for the taxpayer as follows:

> [B]ecause in their decisions the district court and this court dealt adequately and correctly with the question presented in it and here, we will not undertake to restate or further elaborate upon the reasons they gave but will content ourselves with saying that, upon the plain and simple consideration set down and for the reasons pointed up in the *Cherokee* case, we decline to depart from the decision in it, and, on its authority, affirm the judgments appealed from.

Following the *Merry Brothers* decision, the Government petitioned the Supreme Court to review this case and the *Dragon Cement* case. However, on October 14, 1957, the Supreme Court denied certiorari in both of these cases. Four days later, on October 18, 1957, the Internal Revenue Service issued Technical Information Release No. 62, which is as follows:

> The Internal Revenue Service announced today that in view of the denial by the Supreme Court of the United States on October 14, 1957, of the Government's petitions for certiorari in *United States* v. *Merry Brothers Brick & Tile Co., et al.*, 242 Fed. (2d) 708 (1957), and in *Dragon Cement Co., Inc.* v. *United States*, 244 Fed. (2d) 513 (1957), it is taking steps to dispose of pending litigation and claims involving brick and tile clay and cement rock, as required under these decisions, and to conform Treasury regulations and outstanding rulings accordingly. This should permit the expeditious disposition of the great majority of such cases. Consideration is being given as to the applicability of these decisions in cases involving fire clay and limestone.

For 2 years after the issuance of TIR 62, the Internal Revenue Service followed the position expressed in that release and on that basis did in fact settle many depletion claims in prior years in the case of brick and tile clay. As a result, first it can be said that until the Supreme Court granted the Government's petition for certiorari in the *Cannelton* case on December 14, 1959, there is nothing to indicate in the case of clays such as brick and tile clay that percentage depletion would not be allowed on the finished product. Second, this position had been held in an unbroken chain of many court cases dealing with this subject. Third, the Internal Revenue Service had announced that it would follow this policy in an official release and in fact had followed this practice in settling cases.

Following the decision in the *Cannelton* case on June 27, 1960, the Internal Revenue Service announced that it would follow the principles of the *Cannelton* case in the disposition of cases involving the definition of the term "mining" and—

> in view of this decision certain revenue rulings, long in contest by many taxpayers and inconsistent with the position taken administratively and in litigation, will be revoked.

Subsequently, in specific reference to brick and tile clay, the Service ruled that "any process which is not necessary to bringing such mineral to shipping form will not be considered an ordinary treatment process." Thus hundreds of taxpayers throughout the Nation were, and are, confronted with a completely new policy in this area.

Your committee has concluded from a full examination of the record that taxpayers in the brick and tile industry were justified in this past period before the Supreme Court granted certiorari in the *Cannelton* case in basing percentage depletion on the value of the end product. As previously indicated, this in

no way is intended to reflect any view as to the rules established in 1960 and applicable for the future. Your committee is convinced, however, that taxpayers are justified in placing full faith and credit on the long line of court cases upholding percentage depletion on the finished product in the case of brick and tile on the official statement issued by the Internal Revenue Service that it intended to follow the principles laid down in these court cases, and the fact that the Internal Revenue Service had, in fact settled many cases on this basis.

Also the view of the Government was that percentage depletion could be taken on the selling price of the end product in the case of brick and tile clay, as is evidenced by recommendations in two successive budget messages for changes in the tax laws in this area and by statements sent to Congress and made before your committee in hearings on this subject. For example, former Secretary of the Treasury Robert B. Anderson, in a letter to the Speaker of the House in 1959 requesting legislation, stated:

> Early last year I testified before the Ways and Means Committee on the need to revise the law in order to preclude excessive depletion deductions for the brick and cement industry. My recommendation was made as a result of a series of court cases which permitted manufacturers of brick and cement to compute percentage depletion on the basis of the selling price of the finished manufactured product rather than on the value of the clay or cement rock before it is manufactured.

As a result of these considerations your committee has approved a bill which provides how the terms "gross income from mining" and "ordinary treatment processes normally applied by mineowners or operators in order to obtain the commercially marketable product or products" (as these terms were used in the tax laws for taxable years beginning before January 1, 1961) are to be interpreted in their application to the terms "clay" and "shale" as used in the percentage depletion provisions, but only for taxable years beginning before December 14, 1959. For this period the bill provides that these terms are to be treated as having a meaning consistent with the principles set forth in the *Cherokee Brick & Tile Company* and *Merry Brothers Brick & Tile Company* cases, referred to previously in this report, notwithstanding the decision of the Supreme Court in the *Cannelton* case.

To attempt to apply the Treasury Department's interpretation of the *Cannelton* case to past open years of taxpayers who are miners of clay and shale would be highly inequitable because of the very large number of cases which the Treasury Department has in the past already settled upon the principles of the *Cherokee* and *Merry Brothers* cases. A survey made by the industry from a large sample of the taxpayers in the brick, tile and fire clay industry for example, suggests that for years prior to 1957, approximately 80 percent of the cases are closed. Thus, the Service cannot assess deficiencies in those cases, and to do so in other cases or to refuse claims for refunds based upon the same principles would result in a highly discriminatory situation.

Moreover, retroactive application of the Treasury interpretation of the *Cannelton* case would work hardships on many clay miners. Many of them made decisions—as to the price for the product, whether to use funds for plant expansion, to use them for dividend distributions, etc.—on the assumption that the court and Internal Revenue Service interpretation of what the base was for their percentage depletion allowance could be relied upon. To retroactively impose a tax in these cases would be especially serious in the brick and tile industry because it is traditionally an industry of many small independent businesses which do not have large financial resources to fall back on if there is to be a redetermination of their tax liability.

Revenue effect

The Treasury Department has informed your committee that the revenue involved in refunds pending for the years 1951 through 1957 in the case of brick and tile clay and fire clay used in making brick and tile products represent approximately $17 million. Not all of this amount will necessarily be lost under the bill. In addition, for the period from 1957 to 1960, the Treasury estimated that under its interpretation of the law there would be deficiencies amounting to $22 to $24 million with respect to the same types of clay. This latter amount has not been taken into account in revenue estimates under present law and, therefore, would not represent a reduction in presently estimated revenues.

[H.R. 7057] [15]

TAX TREATMENT OF CERTAIN CLAYS AND SHALE FOR TAXABLE YEARS BEGINNING PRIOR TO 1961

[Senate Report No. 903, Eighty-seventh Congress, First Session]

[September 7, 1961]

MR. BYRD of Virginia, from the Committee on Finance, submitted the following report together with minority views to accompany H.R. 7057.

The Committee on Finance, to whom was referred the bill (H.R. 7057) relating to the application of the terms "gross income from mining" and "ordinary treatment processes normally applied by mine owners or operators in order to obtain the commercially marketable mineral product or products" to certain clays and shale for taxable years beginning before December 14, 1959, having considered the same, report favorably thereon with amendments and recommended that the bill as amended do pass.

The amendments strike out all after the enacting clause and substitute the material appearing in italic in the bill as reported by your committee. A summary of the committee amendments appears in the second paragraph below.

I. SUMMARY OF THE BILL

The version of the bill passed by the House provided in the case of brick and tile clay, shale, refractory and fire clay, and ball, sagger, and china clay that insofar as the holding in the *Cannelton Sewer Pipe* case departs from the principles previously enunciated in the *Cherokee Brick and Tile Company* and *Merry Brothers Brick and Tile Company* cases, it is not to be applied retroactively for years beginning before the Supreme Court granted certiorari in the *Cannelton* case on December 14, 1959. Thus, in the case of brick and tile clay and the other clays or shale where the finished product is the first commercially marketable product, percentage depletion for these past years to the extent they are open would, under the House bill, be based upon the value of the finished or end product.

Your committee has amended the House bill to provide that in the case of brick and tile clay, fire clay and shale used to make certain products, "gross income from the property" for purposes of computing the percentage depletion deduction is to be 50 percent of the gross income from the finished product but not in excess of $12.50 for each ton of this clay or shale used in the finished product. The types of products for which the shale or specified types of clay must be used are building and paving brick, drainage and roofing tile, sewer pipe, flowerpots, or kindred products. This provision is in the form of an election which taxpayers may make for all open years beginning before January 1, 1961.

II. GENERAL STATEMENT

This bill is concerned with the proper base for the application of percentage depletion in the case of various clays and shale for taxable years beginning before January 1, 1961. The question presented here is what the base for percentage depletion should be in the past and not in future, since the basis for taxable years beginning on or after January 1, 1961, was decided quite specifically by Congress in the so-called Gore amendment in the Public Debt and Tax Rate Extension Act of 1960. (That act specified for the future, not only in the case of clay, but in the case of other mineral products as well, the so-called cutoff points at which the various percentage depletion rates are to be applied, or which processes could be applied to the mineral products before determining their value for percentage depletion purposes.)

A. HISTORICAL BACKGROUND

Percentage depletion was provided for ball and sagger clay in 1942 and in 1947 for china clay. In 1951 brick and tile clay, shale and refractory, and fire clay were added to the list of clays eligible for percentage depletion. In that act the rate of depletion for brick and tile clay and shale was set at 5 percent and the rate for ball, sagger, china and refractory and fire clay at 15 percent. In the 1960 amendments, instead of referring to refractory and fire clay as such the code was amended to provide percentage depletion at a 15-percent rate for "clay used

[15] Public Law 87–312, page 339, this Bulletin.

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or sold for use for purposes dependent on its refractory properties." Also, in the category of clay receiving percentage depletion at the 5-percent rate, instead of referring to brick and tile clay as such, the 1960 legislation provided for percentage depletion for "clay used, or sold for use, in the manufacture of building or paving brick, drainage and roofing tile, sewer pipe, flowerpots, and kindred products."

The statute provides that the percentage depletion rates referred to above are to be applied to the "gross income from the property." Congress in the Revenue Act of 1943 defined the "gross income from the property" as the "gross income from mining." The term "mining" in turn was considered to include—

> not merely the extraction of the ores or minerals from the ground but also the ordinary treatment processes normally applied by the mineowners or operators in order to obtain the commercially marketable mineral product or products.

This definition was made applicable to taxable years beginning after December 31, 1931. Although this definition has recently been changed (by the Gore amendment in 1960) it was fully applicable for the period with which this bill is concerned; namely, taxable years beginning before January 1, 1961. Your committee in its report on the Revenue Act of 1943 stated that—

> The purpose of this provision is to make certain that the ordinary treatment processes which a mineowner would normally apply to obtain a marketable product shall be considered as a part of the mining operation * * *.

The issue presented is what represents the ordinary treatment processes normally applied by the mine owners or operators in order to obtain the commercially marketable mineral product or products. In 1954 a district court, in ruling for the taxpayer in the *Cherokee Brick and Tile Company* case (122 F. Supp. 59), held that in the case of the brick and tile clay involved in that case there was no commercially marketable product prior to the finished product and, therefore, that percentage depletion in this case should be based on the finished product. This case was appealed to the Court of Appeals, Fifth Circuit. In affirming (in 1955) the decision of the lower court, that court held:

> The statutory language is clear and unambiguous, which is that gross income from mining must include the income from ordinary treatment processes which must be applied to the ore or mineral in order to obtain the commercially marketable mineral product; that is, the first product which is marketable in commerce. There is no provision in the statute for excluding any process before such a marketable product is reached. The only restriction is that the processes must be the ordinary treatment processes normally applied by mine owners or operators.
>
> The complaint alleges that, of the brick and tile clay mined in the United States, there is opportunity for the sale of only a negligible quantity before it is put into the form of burned brick and tile. This allegation is admitted in the answer of the appellant. For this and other reasons (but mainly for this one) stated in the opinion of the district court, above cited, the judgment appealed from should be affirmed.

Substantially similar positions to that described above were taken by three other circuit courts of appeals (the 3d, 4th, and 10th), the U.S. Tax Court, and district courts in the 6th and 9th circuits. In fact, with the exception of a district court case (*Dragon Cement Company* v. *United States*, 244 F, 2d 513) which was subsequently reversed by the court of appeals, there were no decisions on this issue in favor of the Government prior to the *Cannelton* case. The Government in 1957 asked the Court of Appeals, Fifth Circuit, to reconsider its decision in the *Cherokee* case as a part of its consideration of *United States* v. *Merry Brothers Brick and Tile Company* (242 F. 2d 708). In the *Merry Brothers* decision, the court of appeals again upheld its *Cherokee* decision in holding for the taxpayer as follows:

> [B]ecause in their decisions the district court and this court dealt adequately and correctly with the question presented in it and here, we will not undertake to restate or further elaborate upon the reasons they gave but will content ourselves with saying that, upon the plain and simple consideration set down and for the reasons pointed up in the *Cherokee* case, we decline to depart from the decision in it, and, on its authority, affirm the judgments appealed from.

Following the *Merry Brothers* decision, the Government petitioned the Supreme Court to review this case and the *Dragon Cement* case. However, on October

14, 1957, the Supreme Court denied certiorari in both of these cases. Four days later, on October 18, 1957, the Internal Revenue Service issued Technical Information Release No. 62, which is as follows:

> The Internal Revenue Service announced today that in view of the denial by the Supreme Court of the United States on October 14, 1957, of the Government's petitions for certiorari in *United States* v. *Merry Brothers Brick & Tile Co., et al.*, 242 F. (2d) 708 (1957), and in *Dragon Cement Co., Inc.* v. *United States*, 244 F. (2d) 513 (1957), it is taking steps to dispose of pending litigation and claims involving brick and tile clay and cement rock, as required under these decisions, and to conform Treasury regulations and outstanding rulings accordingly. This should permit the expeditious disposition of the great majority of such cases. Consideration is being given as to the applicability of these decisions in cases involving fire clay and limestone.

For 2 years after the issuance of TIR–62, the Internal Revenue Service followed the position expressed in that release and on that basis did in fact settle many depletion claims in prior years in the case of brick and tile clay. As a result, first it can be said that until the Supreme Court decided the *Cannelton* case there is nothing to indicate in the case of clays such as brick and tile clay that percentage depletion would not be allowed on the finished product. Second, this position had been held in an unbroken chain of many court cases dealing with this subject. Third, the Internal Revenue Service had announced that it would follow this policy in an official release and in fact had followed this practice in settling cases.

Following the decision in the *Cannelton* case on June 27, 1960, the Internal Revenue Service announced that it would follow the principles of the *Cannelton* case in the disposition of cases involving the definition of the term "mining" and—

> in view of this decision certain revenue rulings, long in contest by many taxpayers and inconsistent with the position taken administratively and in litigation, will be revoked.

Subsequently, in specific reference to brick and tile clay, the Service ruled that "any process which is not necessary to bringing such mineral to shipping form will not be considered an ordinary treatment process." It has been indicated that such a position would be followed in all open cases despite the fact that section 7805(b) of the code provides that the Secretary or his delegate may prescribe the extent, if any, to which rulings or regulations may be applied without retroactive effect. Thus hundreds of taxpayers throughout the Nation were, and are, confronted with a completely new policy in this area.

B. REASONS FOR THE BILL

The House Committee on Ways and Means concluded from an examination of the record cited above that taxpayers in the brick and tile industry were justified, at least for this past period, before the Supreme Court granted certiorari in the *Cannelton* case, in basing percentage depletion on the value of the end product. The House was convinced that taxpayers are justified in placing full faith and credit on the long line of court cases upholding percentage depletion on the finished product in the case of brick and tile clay, on the official statement issued by the Internal Revenue Service that it intended to follow the principles laid down in those court cases, and on the fact that the Internal Revenue Service had settled many cases on this basis. The House report also noted that the Government itself apparently assumed that percentage depletion could be taken on the selling price of the end product in the case of brick and tile clay as was evidenced by recommendations in two budget messages for changes in the tax laws and by statements to Congress on this subject. The House report cites as an example of this the statement made by the former Secretary of the Treasury, Robert B. Anderson, in a letter to the Speaker of the House in 1959 requesting legislation in which it is stated:

> Early last year I testified before the Ways and Means Committee on the need to revise the law in order to preclude excessive depletion deductions for the brick and cement industry. My recommendation was made as a result of a series of court cases which permitted manufacturers of brick and cement to compute percentage depletion on the basis of the selling price of the finished manufactured product rather than on the value of the clay or cement rock before it is manufactured.

As a result of the considerations outlined above, the House bill provided how the terms "gross income from mining" and "ordinary treatment processes normally applied by mine owners or operators in order to obtain the commercially marketable product or products" (as these terms were used in the tax laws for taxable years beginning before January 1, 1961), are to be interpreted in their application to the terms "clay and shale" as used in the percentage depletion provisions, but only for taxable years beginning before December 14, 1959. For this period the House bill would provide that these terms are to be treated as having a meaning consistent with the principles set forth in the *Cherokee Brick and Tile Company* and *Merry Brothers Brick and Tile Company* cases referred to previously in this report, notwithstanding the decision of the Supreme Court in the *Cannelton* case.

The House committee report also suggests that to apply the Treasury Department's interpretation of the *Cannelton* case to past, open years of taxpayers who are miners of clay and shale would be highly inequitable because of the very large number of cases which the Treasury Department had in the past already settled upon the principles of the *Cherokee* and *Merry Brothers* cases. It points out that a survey made by the industry from a large sample of the taxpayers in the brick, tile, and fire clay industry, for example, suggests that for years prior to 1957, approximately 80 percent of the cases are closed. Since the Service cannot assess deficiencies in those cases, the House committee report suggests that it would be highly discriminatory to assess deficiencies in other cases or to refuse claims for refunds based upon the same principles.

The House report further pointed out that the retroactive application of the Treasury interpretation of the *Cannelton* case would work hardships on many clay miners. Many of them made decisions—as to the price of the product, whether to use funds for plant expansion, to use them for dividend distributions, etc.—on the assumption that the court and Internal Revenue Service interpretation of what the base was for their percentage depletion allowance could be relied upon. To retroactively impose a tax in these cases would in the view of the House be especially serious in the brick and tile industry because it is traditionally an industry of many small, independent businesses which do not have large financial resources to fall back on if there is to be a redetermination of their tax liability.

Your committee recognizes the validity of much of the case made in the House report for the enactment of this legislation. However, the Treasury Department has taken strong exception to the House version of the bill and representatives of the industry, in view of this Treasury opposition, have agreed to a modification of the House-passed bill. In addition, the legislation which would be provided if the House-passed bill were enacted presents uncertainties in application. For example, it is not possible to determine with certainty exactly what the "principles" of the *Cherokee Brick and Tile Company* and *Merry Brothers Brick and Tile Company* cases actually are, particularly in their application to different types of clay.

The Treasury Department, in its report to your committee on a companion measure to H.R. 7057 (S. 2289), recognized that the technical information release issued by the Internal Revenue Service in 1957 "justifies some degree of legislative relief because of the reliance which may have been placed on this announcement." The report indicates that the Treasury Department would not object if the brick and tile industry were granted a cutoff point for purposes of determining percentage depletion after crushing and grinding and separation of waste material. In addition, the Treasury report indicates that there is some merit to the contention that merely allowing the process of crushing and grinding would not allow the same proportion of relief in the brick and tile industry as the compromise worked out last year in the case of the cement industry. In this connection the Treasury representative before your committee referred to an alternative proposal which would provide that the gross income per ton would be equal to 25 percent of the amount for which the finished product is sold so long as the gross income per ton of clay used in the finished product is not in excess of a maximum of $6 a ton. However, your committee has concluded that, giving due regard to the tax treatment it previously was thought was applicable in such cases, this proposal would provide too little relief for the miner-producers involved; and, in the case of the small companies, it would be likely to place many of them in severe financial straits. It is believed that the committee proposal described below, while still causing some hardship, nevertheless will meet the Government's interpretation of the *Cannelton* case halfway without seriously undermining the financial condition of the companies involved.

In view of the factors described above, your committee has concluded that a legislative settlement of the basis for percentage depletion is desirable in the case of certain clays. The legislative settlement, or compromise, provides that the "gross income from the property" in the case of brick and tile clay, fire clay, and shale used for certain specified purposes is to be 50 percent of the amount for which the finished products are sold but not more than $12.50 for each ton of such clay or shale used in the finished product. To be eligible for this provision the clay or shale must be used in manufacturing building or paving brick, drainage and roofing tile, sewer pipe, flowerpots, or kindred products.

This provision, in general, is a compromise which is much closer to the 25 percent of the value of the finished product, which the Treasury would not oppose, than the 100 percent specified by the House bill. Moreover, it is more restrictive than the House bill in that it is limited to brick and tile clay, fire clay, and shale, and available only for these products when they are used in manufacturing building or paving brick, drainage and roofing tile, sewer pipe, flowerpots, or kindred products. This category of products is the same as that specified in present law where percentage depletion at the rate of 5 percent is allowable. (This is not in any way intended, however, to reduce the allowable percentage rate of depletion in those cases in prior years where the 15-percent rate was applicable.)

The limitation of $12.50 for each ton of the specified type of clay or shale used in the finished product is designed to restrict the allowance of depletion to the amount which would be available if the clay or shale had been used to make standard common brick. (It has been found that such brick generally sells for approximately $25 per ton of clay used in the brick.) This limitation is to be applied separately with respect to each of the clay and shale products covered by this bill which are sold by a miner-producer during his taxable year. Under the bill there are five "products" for purposes of applying this limitation: namely, (1) all building and paving brick, (2) all drainage and roofing tile, (3) all sewer pipe, (4) all flowerpots, and (5) all kindred products.

Your committee's amendment also provides a means of computing the provision which limits the depletion deduction allowable to 50 percent of the taxable income from the property (computed without allowance for depletion).

Your committee has provided that the treatment specified in this bill is to be in the form of an election with respect to all open years (in the aggregate) in the period from January 1951 through any taxable years beginning before January 1, 1961. Thus, your committee's amendment also covers the year 1960 to which the House provision would not have been applicable. Thus, under your committee's action (if the election is made under this provision) only two sets of rules, namely, the rules provided by this bill for taxable years beginning before January 1, 1960, and the rules provided by the Gore amendment with respect to taxable years beginning on or after January 1, 1961, will be applicable in the case of these clays and shale. The House bill would have made the treatment provided in that version of the bill available only for years beginning before December 14, 1959, which meant that the taxable years beginning after that time and before January 1, 1961, the "principles" of the *Cannelton* case would have applied and that after 1960 the Gore amendment would be applicable. Your committee's amendment makes it unnecessary for taxpayers to apply the "principles" of the *Cannelton* case for what usually is merely a 1-year interval.

The election if made applies with respect to all assessments of deficiencies and refunds or credits of overpayments where the statute of limitations has not run on the date of enactment of this bill. Under the bill the taxpayer has until 60 days after date of the publishing of the final regulations to make this election. Any such election once made may not be revoked. The bill also provides that for any deficiency or overpayment arising from the excerise of the election specified in this bill, the statute of limitations is not to close until 1 year after the last day for making the election.

C. REVENUE EFFECT

It is estimated that this bill will decrease revenues by about $20 million if the Treasury interpretation of the *Cannelton* case is correct. This is the aggregate loss anticipated for the years 1951 through 1960. It includes both losses expected from deficiencies which might otherwise be assessed and collected and also losses occurring from making refunds required under the bill.

MINORITY VIEWS OF SENATORS PAUL H. DOUGLAS AND ALBERT GORE

The granting of percentage depletion to a variety of minerals has been one of the most controversial provisions of our tax code. But whatever may be said against the excesses of percentage depletion for raw materials, these excesses, pale in principle when compared with the attempt of this bill to provide percentage depletion on a retroactive basis on the greatly enhanced value of the final manufactured product of brick and tile clay, fire clay, and shale.

Even those who may support percentage depletion for certain minerals could hardly justify such an allowance for the final product.

In 1951, when percentage depletion was extended to brick and tile clay, shale, fire clay, and a number of other nonmetallic minerals, no one foresaw where we would find ourselves 10 years later. Prior to 1951 the various persons entitled to percentage depletion had computed their depletion allowances on the basis of the value of the raw materials or the mineral concentrates. No one appearing before the committees of Congress requesting percentage depletion benefits for his mineral had ever asked that depletion be based on the value of his manufactured product. There is no evidence that the brick and tile industry requested Congress to allow percentage depletion on finished bricks, sewer pipe, and other such products. The various industry representatives who appeared before the congressional committees generally stated that they were mining a certain mineral, such as clay, which became exhausted or depleted over a period of time, and that they felt they were entitled to a greater deduction for depletion of the mineral. No one suggested that he was mining a brick or a flowerpot and that he was entitled to a depletion deduction based on its value.

Yet, shortly after percentage depletion was extended to the brick and tile industry, the members of the industry began for the first time to express the view that Congress had granted them depletion of their finished products. Naturally, the Internal Revenue Service opposed this effort to extend depletion to manufacturing. The industry then embarked on a well-organized and carefully planned litigation campaign which was designed to secure, through the courts, depletion on the manufactured products.

Nine years later, this litigation effort ended in failure for the industry. The Supreme Court declared unanimously in the case of *U.S.* v. *Cannelton Sewer Pipe Company* the obvious answer that Congress had never intended that depletion be based on manufactured products, and that depletion was not intended as a subsidy to manufacturers. Since the brick and tile industry did not attain its objective through the courts, the forum which it originally selected, it then turned its gaze back toward Congress and said, "Give us for the past 10 years that which the courts have denied us—depletion on the manufactured product."

This request was ostensibly based on two factors. First, the industry pointed out that it had obtained a number of favorable lower court decisions before the Supreme Court decision was handed down, and second, at one stage of the litigation the Internal Revenue Service had issued a press release indicating that pending claims involving brick and tile clay would be settled as required by certain of these lower court decisions

What the brick and tile industry failed to point out is that producers of a number of other minerals followed the lead of the brick and tile producers so that the lower court decisions involved a substantial number of minerals in addition to brick and tile clay. Thus, if these lower court decisions are used as a basis for granting legislative relief to brick and tile clay, producers of a number of other minerals may press similar claims. It is a novel theory that a decision in favor of a taxpayer in a lower court followed by a reversal by the Supreme Court produces grounds for legislative relief. As far as the press release is concerned, it was merely one event in the course of extended litigation, and the brick and tile industry itself knew that the issuance of the press release did not finally resolve the question. Thus, the brick and tile industry was aware that it alone could not obtain depletion on the manufactured product, and that the litigation would continue until either all mineral producers or none obtained depletion on the finished product.

However, on the basis of the lower court decisions and the press release, the House of Representatives passed a bill granting finished product depletion to producers of all clay and shale for all open years back to 1951. The Senate

Finance Committee has amended this bill to grant producers of brick and tile clay, fire clay, and shale 50 percent of the value of the manufactured product limited to $12.50 per ton of clay or shale. Even this measure is far too generous in distributing money that belongs to all taxpayers to one industry which interpreted the law incorrectly, and which, we suspect, knew it was interpreting the law in a manner contrary to accepted depletion concepts.

The passage of this bill would truly reward the contentious. All the taxpayers in the various mineral industries who did not seek to take depletion on their manufactured products, who conscientiously adhered to the rulings and practices long followed by the Internal Revenue Service and taxpayers alike, would not obtain depletion on 50 percent of the value of the manufactured products. Only those who sought to extend depletion beyond its normal meaning, who were instrumental in creating a 10-year period of uncertainty and turmoil in the entire depletion area, would obtain this substantial benefit. The passage of such legislation is an invitation for taxpayers to "shoot for the moon" knowing that if they do not succeed, there is a good chance that Congress will grant them 50 percent of what they aspired to.

In addition to these fundamental objections to the bill reported by the committee, it is defective for another reason. Although the bill has as one of its primary reasons for existence the aforementioned press release, it applies to fire clay which was specifically excepted from the terms of the press release. Thus, those who favor this bill base their advocacy primarily on the fact that persons mining brick and tile clay may have relied on the press release, and are entitled because of this reliance to some tax forgiveness for past years. Miners of fire clay, however, cannot claim reliance on the press release. They may say that they relied on the lower court decisions and are entitled to relief on that ground; but this same claim can be asserted by miners of many different minerals. On this count, the bill is not only objectionable but is also dangerous since many other segments of the mining industry will attempt to use it as a precedent. The extension of this type of unjustified retroactive relief to the mining industry as a whole would involve a revenue loss to the Government of several hundred million dollars.

We are appending the letter of the Treasury opposing the enactment of H.R. 7057 as it passed the House.

The Senate should reject this bill.

PAUL H. DOUGLAS.
ALBERT GORE.

TREASURY DEPARTMENT,
Washington, August 29, 1961.

Hon. HARRY F. BYRD,
Chairman, Senate Committee on Finance,
Old Senate Office Building, Washington, D.C.

DEAR MR. CHAIRMAN: This is in response to your request dated July 29, 1961, for the views of the Treasury Department with respect to S. 2289, a bill relating to the application of the terms "gross income from mining" and "ordinary treatment processes normally applied by mine owners or operators in order to obtain the commercially marketable mineral product or products" to certain clays and shale for taxable years beginning before December 14, 1959. The purpose of S. 2289, which was introduced by Senator Ervin, is to permit taxpayers who mine certain clays and shale to compute the percentage depletion allowance on the basis of gross income from the sale of finished manufactured products for taxable years beginning before December 14, 1959. This bill is the same as H.R. 7057 which was passed by the House of Representatives on August 21, 1961.

The Treasury Department is opposed to the enactment of S. 2289 for reasons which will be discussed hereinafter.

BACKGROUND

Congress has provided the percentage depletion allowance to permit recovery of the investment in a wasting asset and to provide an incentive for the discovery and development of additional mineral deposits. The amount of the percentage depletion allowance is computed by applying the percentage rate for the particular mineral, as determined by Congress, against the gross income attributable to mining the mineral. The allowance may not, however, exceed

50 percent of the taxable income from the property. To determine the gross income from mining, it is necessary to define the point at which mining ends and manufacturing begins. This point is often referred to as the "cutoff point."

In the 1951 Revenue Act, percentage depletion was first extended to brick and tile clay, shale, refractory and fire clay, limestone, and a number of other nonmetallic minerals. Shortly thereafter, the question arose with respect to a number of these minerals as to where the "cutoff point" occurs.

In November of 1951, the Brick and Clay Record, a leading trade journal in the brick and tile industry, stated that "the depletion allowances apply to the market value of the *raw minerals* * * *." [Emphasis supplied.] This statement indicated that many in the industry were of the opinion that mining ended in the brick and tile industry when the clay was extracted from the ground. However, by January of 1952 the same trade journal stated the opinion that the cutoff point was not reached for brick and tile clay until the finished brick was obtained. Under this view, "mining" included crushing, grinding, elimination of any waste material, mixing in the pugmill, the shaping and cutting of bricks, drying, and burning. At this point some producers of brick and tile clay and cement rock (a low-grade limestone suitable for making cement) began to apply the percentage rate granted by Congress against the gross income from the sale of finished brick and finished bagged cement, respectively. This approach was based on an interpretation of statutory language which provided that the cutoff point occurs after the mine owner or operator has applied "the ordinary treatment processes normally applied by mine owners or operators in order to obtain the commercially marketable mineral product or products." These brick and tile clay and cement rock producers contended that, in their industries, the finished manufactured products were the commercially marketable mineral products, and that all the processes necessary to obtain these products were normally applied by miners of brick and tile clay and cement rock.

The Internal Revenue Service took the view that Congress had never intended "mining" to include manufacturing processes, and that it was known generally in the mining industries that depletion was not to be based on gross income from the sale of finished manufactured products. Because of this dispute, it was necessary for the Revenue Service to determine precisely where the cutoff points fell in the brick and tile and cement industries. In 1953 the Revenue Service published a revenue ruling providing that the cutoff point for minerals used in making cement occurs after the materials are crushed and ground but before they are burned in the kiln; and in 1954 the Service published a similar revenue ruling providing that the cutoff point for brick and tile clay and shale used in making brick and tile products occurs after crushing, grinding, and the elimination of any waste material associated with the clay or shale. It was the view of the Revenue Service that after crushing and grinding, the taxpayer had obtained the commercially marketable mineral product, and that subsequent processing converted the mineral product into a manufactured product.

In 1955 the Court of Appeals for the Fifth Circuit decided in the case of *U.S.* v. *Cherokee Brick & Tile Co.* (218 F. 2d 424) that percentage depletion should properly be based on the gross income from the sale of finished brick. In 1956 and 1957 other cases involving brick and tile clay and cement rock were decided against the Government. In these cases the Government had stipulated that there was an opportunity for the sale of only negligible amounts of the minerals involved before obtaining the finished products, but had contended that, in spite of this fact, the taxpayers were not entitled to obtain depletion for the manufacturing part of their business. In holding for the taxpayer in the *Cherokee* case, the Court stated that the "gross income from mining must include the ordinary treatment processes which must be applied to the ore or mineral in order to obtain the commercially marketable mineral product; that is, the first product which is marketable in commerce."

Two of the cases lost by the Government in 1957 were *U.S.* v. *Merry Brothers Brick and Tile Co.* (242 F. 2d 708) and *Dragon Cement Co., Inc.* v. *United States* (244 F. 2d 513). The Government requested the Supreme Court to review these decisions, but the Supreme Court denied the request. Shortly thereafter, the Internal Revenue Service issued Technical Information Release 62 stating that it would take steps to dispose of pending litigation and claims involving brick and tile clay and cement rock as required under the *Merry Brothers* and *Dragon Cement* decisions. This release read as follows:

"The Internal Revenue Service announced today that in view of the denial by the Supreme Court of the United States on October 14, 1957, of the Government's petitions for certiorari in *Uinted States* v. *Merry Brothers Brick & Tile Co., et al.* (242 Fed. (2d) 708 (1957)) and in *Dragon Cement Co., Inc.*, v. *United States* (244 Fed. (2d) 513 (1957)), it is taking steps to dispose of pending litigation and claims involving 'brick and tile clay' and 'cement rock,' as required under these decisions, and to conform Treasury regulations and outstanding rulings accordingly. This should permit the expeditious disposition of the great majority of such cases. Consideration is being given as to the applicability of these decisions in cases involving fire clay and limestone." This release was applicable to no minerals except brick and tile clay and cement rock, and even in the case of these two minerals it was considered by the Revenue Service to be applicable only to the extent it could be shown in the particular case that the finished product was "the first product which is marketable in commerce."

This was not the end of the litigation, however. It was now necessary under the court decision to determine with respect to each mineral what was the "first commercially marketable product," and whether this determination was to be made on an individual, a regional, or an industrywide basis. The Government took the position that the first marketable product must be determined on an industrywide basis. Otherwise, there would be no uniformity of treatment throughout the country. Taxpayers in one area might base the depletion allowance upon the gross income from finished products because there was no market in the area at an earlier stage, and taxpayers mining similar minerals in other areas where there were markets might be cut off after obtaining the crude mineral product. However, taxpayers mining numerous different minerals took the position that the first marketable product should be determined on an individual basis and that depletion should be based on the gross income from the first product that the particular taxpayer could sell at a profit. Under this approach, the depletion allowance could vary widely for the same mineral depending upon whether it was used by the particular taxpayer in making cheap or expensive finished products and upon whether the taxpayer had a low-cost mining operation so that he could profitably sell the crude mineral at prevailing prices or a high-cost mining operation which did not permit the sale of the crude product at a profit.

This question of the determination of the first commercially marketable product was before the courts in 1958 and 1959. Taxpayers prevailed in this litigation in cases involving limestone used in making lime, cement, pulverized material for agricultural purposes, and other products; refractory clay used in making expensive ceramic tile and sewer pipe; shale used in making lightweight aggregate; slate used in making roofing tiles; and several other minerals such as perlite, gilsonite, and dimension stone.

This problem was considered by the Government to be so serious from the standpoint of equity between taxpayers, the theory of the depletion allowance, and revenue considerations, that the Government in 1959 again requested the Supreme Court to review a lower court decision involving the cutoff point question. The case in which the Government requested Supreme Court review was *U.S.* v. *Cannelton Sewer Pipe Company* (C.A. 7th 1959) 268 F. 2d 334, a case involving a taxpayer which mined fire clay and shale and used them in the manufacture of sewer pipe and other finished products. The taxpayer contended that its depletion allowance should be based on the gross income from the sale of its finished products since it could not profitably sell its clay or shale at any earlier stage. The Government contended that fire clay and shale are marketable in crude form and are in fact marketed by many miners in crude form, and that it is immaterial whether or not the taxpayer could sell its crude clay and shale at a profit since a uniform cutoff point for all miners of these minerals is applicable under a correct interpretation of the statute.

On December 14, 1959, the Supreme Court granted certiorari; and in June of 1960 the Supreme Court handed down a unanimous opinion in favor of the Government (364 U.S. 76). The Court held that raw clay and shale were the marketable mineral products and that the fact that the taxpayer could not sell its raw clay and shale at a profit was immaterial. The Court distinguished the *Cannelton* case from the *Cherokee* and *Merry Brothers* cases. However, it stated that it did not express approval of these earlier decisions. In fact, although the Court did not overule these earlier decisions, the language

used by the Court indicates that depletion should not be taken with respect to value added by manufacturing processes in any case. Thus the Court stated that depletion "is not a subsidy to manufacturers or the high-cost mine operator," and that in the case of an integrated operation "the miner-manufacturer is but selling to himself the crude mineral that he mines, insofar as the depletion allowance is concerned."

A recent District Court case in Kansas, *Great Bend Brick and Tile Co.* v. *U.S.* (61–1 U.S.T.C. par. 9394), held that the principles of the *Cannelton* decision apply to brick and tile clay as well as to fire clay and shale.

At approximately the same time that the Supreme Court handed down the *Cannelton* decision, Congress amended the cutoff point provisions of the code for 1961 and future years. This amendment made it clear that taxpayers could not base depletion on the gross income from the finished manufactured products. It also provided cutoff points at crushing and grinding for clay used in making brick and tile products and for minerals used in making cement. These cutoff points are in accord with the above-mentioned revenue rulings published by the Internal Revenue Service in 1953 and 1954 with respect to these industries.

In 1960 the Internal Revenue Service announced that cases involving the years 1951–60 would be settled in accordance with the principles of the *Cannelton decision*. This meant that, for these years, the cutoff point for clay used in making brick and tile products would occur when the raw clay was obtained, and the cutoff point for limestone and cement rock would occur after crushing since these are the points at which the minerals would be sold by the nonintegrated miner.

Because the cutoff points for the cement and brick and tile industries would occur at an earlier stage of processing under the *Cannelton* decision than under the rulings published by the Internal Revenue Service in 1953 and 1954 and the statutory amendment adopted by Congress in 1960, and because of the technical information release issued by the Revenue Service in 1957 indicating that some cases involving brick and tile clay and cement rock would be settled on the basis of finished brick and cement, the Treasury Department indicated that it would not oppose legislation granting producers of brick and tile products and cement an election to utilize for past years the provision adopted by Congress for future years. Under such an election, the affected taxpayers would be assured that crushing and grinding would be treated as mining. The Congress adopted such an elective provision for the cement industry, and it has been used by the great bulk of the taxpayers in the industry. This election did not grant cement producers the right to base depletion on the gross income from finished cement for the past years. It merely assured these taxpayers that crushing and grinding, the processes necessary to ready the minerals for the kiln, would be treated as mining. The net effect of this elective provision was generally that taxpayers relinquished their claims for refund based on finished cement for the years 1951–56, and the Government relinquished its right to assess approximately 15 percent of the deficiencies that could be assessed for the years 1957–60 under the *Cannelton* decision.

The Treasury Department indicated to industry representatives and to the House Ways and Means Committee last year and again during this session of Congress that it would not object to comparable legislation for the brick and tile industry. The equities of this industry are similar to those of the cement industry since both were the subject of published rulings by the Revenue Service and since the technical information release issued in 1957 was partially applicable to both industries.

DISCUSSION OF THE BILL

S. 2289 would provide that, notwithstanding the decision of the Supreme Court in the *Cannelton* case, the percentage depletion allowance with respect to various clays and shale shall be determined under the principles of the *Cherokee* and *Merry Brothers* cases for all years beginning before December 14, 1959 (the date that the Supreme Court granted certiorari and the *Cannelton* case). The Treasury Department has two fundamental objections to the bill. The primary objection is that the granting of depletion for manufacturing operations with respect to any mineral for any period of time violates the basic concepts and theories underlying the congressional grant of depletion allowances. The secondary, but also important, objection to the bill relates to the uncertainty of its effect. Any bill which provides that cases are to be settled on the principles of court decisions which are subject to various interpretations can

only result in continued and extensive litigation which will be costly and burdensome both to the taxpayers and to the Government. Furthermore, the eventual results of this litigation are likely to be unsatisfactory to many of the parties involved.

The only justification for granting finished product treatment to producers of brick and tile clay stems from the technical information release issued by the Internal Revenue Service in 1957. It is admitted that this justifies some degree of legislative relief because of the reliance which may have been placed on this announcement. However, there are a number of factors on the other side of the ledger which must be weighed in the balance to determine the extent to which special relief is justified.

First, mineral producers, including brick and tile clay producers, were no doubt aware that it was a distortion of percentage depletion principles to base depletion on value added by manufacturing. Percentage depletion has been a part of our revenue system since 1926 in the case of oil and gas and since 1932 in the case of metals, sulfur, and coal. During this long period of time, it has been widely understood that the cutoff point occurs when the mineral has been obtained, not when it has been converted into a manufactured product. For example, a preliminary report on depletion in 1930 by the staff of the Joint Committee on Internal Revenue Taxation stated, with respect to iron ore, that "probably 95 percent of the entire production is owned or contract-controlled by the smelting companies." In spite of the fact that this industry was integrated (as much as the brick and tile industry is integrated), there was no thought in Congress of extending percentage depletion for iron ore through the smelting process and there was no thought on the part of the industry of claiming depletion on such a basis. Many other industries were integrated to a greater or lesser degree when percentage depletion was extended to them, but they did not seek to base depletion on income from finished products. Many representatives of various mining industries, including representatives of integrated miner-manufacturers, have appeared before congressional committees to request the extension of percentage depletion to their minerals, but not one of them has asked that depletion be allowed with respect to a finished manufactured product. As mentioned previously, the trade journal of the brick and tile industry itself first indicated that depletion was to be based on the value of the raw product. In addition, many brick and tile clay producers did not base their depletion allowances on the gross income from the finished products when they filed their 1951 tax returns; these producers subsequently adopted the finished product argument and then filed claims for refund. A representative of the American Mining Congress, in appearing before the House Ways and Means Committee in 1959, indicated that the interpretation of the cutoff point provisions by the courts "not only allows results which go beyond the original concept of the percentage depletion deduction, but also can produce unintentional discrimination between taxpayers employing the same treatment processes to produce the same end product [because of different marketing practices in different areas]." Thus, the allowance of finished product treatment is not only inconsistent with the basic theory of the depletion allowance but is also contrary to the understanding of the mining industry itself.

Second, the technical information release was issued in response to a series of court decisions. All told, the Government lost upward of 50 cases relating to the cutoff point question prior to the *Cannelton* decision. Less than half of these cases involved brick and tile clay. The balance involved talc, cement rock, refractory and fire clay, shale, gilsonite, limestone, perlite, slate, granite, and dolomite. Either the *Merry Brothers* or *Cherokee* decision, or both, have been cited by courts as authority for allowing depletion to be based on gross income from the sale of such diverse products as talc crayons in packages, hydrated hydraulic lime in bags, ceramic tile, and finished dimension stone. In addition, by 1959 there were approximately 380 cases, involving more than 25 different minerals, pending either administratively or in litigation in which taxpayers were seeking to use the finished product cutoff point. These cases involved some $300 million in revenue. These figures relate only to the cases which had come to the attention of the Internal Revenue Service by 1959 so that both the number of cases involved and the potential revenue loss were actually much greater.

Producers of all of these other minerals thought they were entitled to rely on the principles of the *Merry Brothers* case, and they did so rely in filing their

returns. Thus, they too could make a claim for legislative relief for past years similar to that being made by the brick and tile industry, stressing reliance on the court decisions rather than the information release. Mineral producers did not expect, and indeed brick and tile clay producers themselves did not expect, that producers of one mineral would obtain a cutoff point at the finished product and that producers of all other minerals would be held to earlier cutoff points. Thus, in the Brick and Clay Record of December 1957 after the technical information release had been issued, a summary of a statement made by Douglas Whitlock, chairman of the Structural Clay Products Institute, contained the following paragraph:

"As another key point, it is believed that depletion [on the finished product] must be granted to all mineral industries and that the clay industry must help to keep depletion allowances for all. He's sure that no situation can exist wherein only the brick and tile people are allowed depletion [on the finished product]. For this reason, the question of the fire clay allowance as a means of protecting the brick and tile clay allowance needs attention."

In view of the entire background and the complex of factors involved, it is difficult to justify the selection of one factor, an information release which happened because of the course of litigation to apply to two minerals, as a basis for granting finished product treatment to brick and tile clay for a 9-year period. Such treatment differentiates too sharply between brick and tile clay producers and the other mineral producers who also claimed reliance on the court decisions.

Third, the allowance of a finished product cutoff point for brick and tile clay would grant a depletion allowance with respect to this mineral which is out of proportion to the allowance granted to many other more valuable minerals. Brick and tile clay is a low-cost and plentiful mineral which Congress granted only a 5-percent depletion rate. Yet, if depletion is based on finished product values, the depletion allowed with respect to this mineral will exceed that allowed to minerals to which Congress has extended higher rates. For example, statistics of the Internal Revenue Service and the U.S. Bureau of Mines show that the depletion allowance for coal for the years 1951–58 averaged from 10 cents per ton in 1954 to 17 cents per ton in 1957. Coal enjoys a 10-percent depletion rate and was first granted percentage depletion in 1932. Percentage depletion on finished brick values for 1951–59 would, at a 5-percent rate, be as high as $1.25 per ton since some types of brick sold for as much as $25 per ton of clay during this period. If the principles of the *Merry Brothers* decision extend to finished sewer pipe, which sells for as much as $50 per ton of clay, the depletion allowance could equal $2.50 per ton; and if the principles of *Merry Brothers* are applicable to clay enjoying a 15-percent depletion rate, the allowance on sewer pipe could equal $7.50 per ton of clay. It has been pointed out that when depletion reaches this level, it would be more advantageous from a revenue standpoint for the Government to mine the clay and give it to the taxpayer.

Fourth, to the extent the bill applies to clay other than brick and tile clay (which is uncertain), it applies to clay to which the information release issued by the Revenue Service did not apply.

Fifth, the information release applied to cement rock as well as to brick and tile clay. Yet the special legislation enacted by Congress with respect to the cement industry did not grant finished product treatment to producers of cement rock. It is estimated that the legislative relief granted to the cement industry resulted in forgiving 15 percent of the deficiencies which could be assessed against this industry under the *Cannelton* decision. It is difficult to justify eliminating all potential deficiencies with respect to brick and tile clay and only 15 percent of the deficiencies of cement rock producers since producers of both minerals were in identical positions so far as reliance on the information release is concerned.

In view of these factors, it is our view that, although some legislative relief may be justified, no taxpayer should be permitted to base his depletion allowance on the gross income from the sale of the finished manufactured product.

In addition, by providing that the percentage depletion allowance is to be determined under the principles of the *Cherokee* and *Merry Brothers* cases, S. 2289 would result in widespread litigation. The entire course of litigation from 1957 to 1959 related to differences of opinion as to the proper interpretation of these cases. Thus, if the bill were passed, it would not be clear whether it granted a finished product cutoff point to all brick and tile clay or only to that brick and tile clay in areas where the industry was wholly integrated so that there was no market for the crude clay; it would not be clear whether a

finished product cutoff point was extended to fire clay and other clays since they are sold in larger amounts in crude form; and with respect to the clay to which the bill finally applied, it would not be clear whether the finished product cutoff point extended only to finished brick or also to other products manufactured by the taxpayer such as sewer pipe, flowerpots, ceramic tile, etc., some of which sell for many times the value of finished brick. All of these questions would have to be settled by further litigation, and what would purport to be a legislative settlement for past years would settle very few cases. Moreover, after the conclusion of this litigation, it is possible that the court decisions would reach results which are not uniform as to taxpayers mining similar minerals. Such results would be unsatisfactory to many taxpayers as well as to the Government.

The Treasury Department has indicated to industry representatives and to the House Committee on Ways and Means last year and again this year that it would not object to a bill providing legislative relief for the brick and tile industry comparable to that provided for the cement industry. Because of the rulings and the information release that applied to brick and tile clay and cement rock, these two industries have some basis for relief which is not available to other mineral industries. At the time the legislative relief for the cement industry was considered, the Treasury Department indicated that it would not object if the brick and tile industry was granted a cutoff point after crushing and grinding and separation of waste material. Subsequently it was pointed out by industry representatives that although this cutoff point would allow similar processes as were allowed to the cement industry, it would not relieve an equivalent amount of the deficiencies resulting from the *Cannelton* decision. We recognize that there is some merit to this contention if this proposal is viewed largely as a matter of measuring equities, as respects situations in these two industries in which returns were filed on the basis of the finished product, rather than of identifying mining processes. If your committee feels that legislation would be appropriate which will eliminate approximately the same proportion of deficiencies for the brick and tile industry as the Congress eliminated in the case of the cement industry, we will be happy to cooperate with your committee and your staff in devising a proposal to achieve this objective.

It has been suggested that the brick and tile industry would suffer a severe hardship if it was required to pay any portion of the deficiencies resulting from *Cannelton*. In this regard, it is to be noted that these companies must be profitable in order to obtain any significant percentage depletion allowance since the allowance is limited to 50 percent of the taxable income from the property. A company which had little income during the past years would have little depletion and thus would not be the subject of a large deficiency assessment. In addition, the financial statements of some of the companies involved indicate that they have set up reserves for the payment of any deficiencies which may arise from the depletion issue. Further, the future prospects of the industry appear to be bright. The Brick and Clay Record stated in its June 1961 issue that "there are indications that production of structural clay products will hit capacity levels before the end of 1961." The Internal Revenue Service has already stated that it will cooperate in every reasonable way with taxpayers who cannot make immediate full payment of deficiencies without undue financial hardship. Under this program, taxpayers for whom immediate payment would result in hardship would be permitted to pay the deficiencies in installments.

REVENUE LOSS

If S. 2289 would grant finished product treatment to brick and tile clay and shale used in brick and tile products, the revenue loss from its enactment is estimated at $24 million. If the bill extends to fire clay used in making brick and tile products, the revenue loss is estimated at $33 million. If it applies to clays used in other finished products outside the structural clay products industry, the revenue loss could rise to $80 million. If the bill becomes a precedent for other minerals the producers of which filed their returns, or filed claims for refund, on a finished product basis, the revenue loss could be in excess of $400 million.

The Bureau of the Budget has advised the Treasury Department that there is no objection from the standpoint of the administration's program to the presentation of this report.

Sincerely yours,

STANLEY S. SURREY,
Assistant Secretary.

[H.R. 2585] [16]
UNEMPLOYMENT TAX CREDIT

[House of Representatives Report No. 425, Eighty-seventh Congress, First Session]

[May 24, 1961]

Mr. MILLS, from the Committee on Ways and Means, submitted the following report to accompany H.R. 2585.

The Committee on Ways and Means, to whom was referred the bill (H.R. 2585) relating to the credits against the employment tax in the case of certain successor employers, having considered the same, report favorably thereon with an amendment and recommend that the bill as amended do pass.

The amendment is as follows:

Page 1, line 7, strike out "(d)" and insert "(e)".

I. SUMMARY OF BILL

This bill is designed to prevent the imposition of a double tax in the case of the Federal and State unemployment taxes which arises because of a technical deficiency in the Federal tax laws. At the present time, due to a variation in the definition of employer between the Federal and State laws, cases can arise where the usual credit for State unemployment taxes is not available where a trade or business changes hands within the first 20 weeks of a calendar year. This bill corrects the faulty operation of the Federal laws by making the usual credit available in such cases. This bill is effective for calendar year 1951 and subsequent years.

Last year Congress passed a similar bill (H.R. 6482) but it was vetoed by the President. The President indicated that he favored the purpose of the legislation but was vetoing it because it was retroactive. Your committee has very carefully considered the President's position in this respect but has nevertheless unanimously reported this bill with an effective date applicable to the calendar year 1951 and subsequent years. As indicated subsequently in this report, it has taken this position because of the belief that to do otherwise would seriously discriminate against a relatively small group of employers and result in unjust enrichment for the Federal Government.

II. GENERAL STATEMENT

Present law levies a Federal unemployment tax on employers of four or more, equal to 3.1 percent of the wages paid each employee up to a maximum of $3,000 per employee per calendar year. Credits of up to 2.7 percentage points out of this 3.1 percentage-point tax are allowed, however, for taxes paid to State unemployment funds. In addition, credits are allowed under an approved plan for unemployment taxes which would be paid to States if the employer did not have a good experience rating.

Since 1950, wages paid by a predecessor employer have been deemed to be paid by a successor with respect to the calendar year in which the successor succeeded to the business. Ordinarily this entitles the successor to a credit against its Federal unemployment tax for State unemployment taxes paid by its predecessor. However, the 1950 amendments have proved to be defective in certain respects and as a result the Federal Government does not always allow the credit to the successor where the predecessor has paid both the State and Federal unemployment tax. This problem can arise where a State and the Federal Government have different definitions of an employer.

The Internal Revenue Code defines an employer for purposes of the Federal unemployment tax as not including any person unless in 20 different calendar weeks the person employs at least four individuals. As a result, where one employer obtains the business of another before the end of the first 20 weeks of the year, in either a tax-free or taxable transaction, the Treasury Department has held that this means that the first business making the wage payments was not an "employer" for purposes of the Federal unemployment tax. However, 19 States do not have the 20-week requirement in their laws for purposes of defining an "employer." In addition, 27 other States have retained the 20-week test but alternatively determine liabilty for the unemployment tax on

[16] Public Law 87–321, page 341, this Bulletin.

the basis of employment experience in the preceding year. The States which do not have this 20-week test and those which have an alternative base under which liability for tax is determined on the basis of the status of the person as "employer" in the preceding year are shown in tables 1 and 2, respectively.

TABLE 1.—*States which do not have a 20-week requirement in defining employer for unemployment tax purposes*

Alaska	Maryland	Oregon
Arkansas	Massachusetts	Pennsylvania
California	Nevada	Rhode Island
Connecticut	New Mexico	Utah
District of Columbia	New York	Washington
Hawaii	Ohio	Wyoming
Idaho		

TABLE 2.—*States which have retained the 20-week test in defining employer for unemployment tax purposes, but which alternatively base liability for tax on the status as employer in the preceding year*

Alabama	Kentucky	North Dakota
Arizona	Louisiana	Oklahoma
Delaware	Mississippi	South Carolina
Florida	Missouri	South Dakota
Georgia	Montana	Tennessee
Illinois	Nebraska	Texas
Indiana	New Hampshire	Virginia
Iowa	New Jersey	West Virginia
Kansas	North Carolina	Wisconsin

In these 46 States where there is a different basis from that under the Federal law for determining who is the "employer," the Federal credit for the State unemployment tax does not work properly. Thus, where there is a successor business before the end of the 20th week during the calendar year, the Federal tax must be collected from the successor business which is the only "employer" for Federal tax purposes. However, in 46 States the State tax is to be collected from the first business, with little or no State tax due from the second business. As a result, almost a full State unemployment tax may be collected from the first business and a full Federal unemployment tax from the second business, but since these are considered to be different employers, little, if any, of the Federal credit for State taxes is allowable.

The problem described above can be illustrated by an example showing how the crediting of the Federal tax is intended to work in the usual case and how it may result in a double tax in the situations with which this bill is concerned. In the usual case, the Federal Government imposes a tax equal to 3.1 percent of the first $3,000 paid any employee by an employer but then allows a credit of 2.7 percent of these wages where a State unemployment tax is paid. Thus, assuming at least $3,000 in wages, there is a $93 Federal tax but against this there is allowed an $81 credit, with the result that there is a net Federal tax in this case of $12 per employee. The State tax in this case may amount to as much as $81. If the business is transferred within the first 20 weeks of the year, however, quite a different result obtains. A State tax of up to $81 is paid by the first business. In addition, a full $93 Federal tax is imposed with respect to the second business. However, no credit against this Federal tax is available because of the technical difference as to which business is considered the initial "employer." As a result, instead of a combined Federal-State tax of up to $93 per employee, there may be a combined tax of $174 per employee.

Last year Congress recognized the unfairness of imposing a double tax in the type of situation described above and passed a bill (H.R. 6482) providing that where an employer acquired the business of another person and continued to employ part or all of the employees of this other person, the employer would be allowed the credit for the State unemployment taxes paid by the other person to the extent attributable to employees who went over with the business. This amendment was to apply to calendar years beginning on or after January 1, 1951, the effective date of the Social Security Amendments Act of 1950, which contained the defective language. However, this bill was vetoed by the President. In his message of June 3 (H. Doc. 411) he indicated that he vetoed this bill because—

Strict avoidance of retroactive tax legislation, except in extraordinary and compelling circumstances not here in evidence, is essential to orderly tax administration, the Government's revenues, and the fair treatment of taxpayers.

Despite this veto, the President urged Congress at its earliest opportunity to enact new legislation without retroactive effect. In this connection he referred to the bill as having a desirable purpose which is thwarted under present law where a predecessor does not qualify as an "employer" for Federal tax purposes.

Your committee has given careful reconsideration of this bill and on the basis of this consideration is again reporting this bill with an effective date applicable to years beginning with the calendar year 1951. Your committee is taking this action because it believes that it is improper for the Federal Government to obtain a double tax in such situations. It concluded that not to grant relief from the double taxation in these situations for this back period would represent unjust enrichment for the Federal Government. Not only is a double tax involved, but the burden of it is particularly heavy since it discriminates against a limited number of employers by imposing a double tax in their case while no similar double tax is imposed with respect to employers generally. Moreover, when the amendment was made in 1950 allowing credits to successors for payments made by predecessors, it was thought by your committee that double taxation in these cases was prevented. This belief was also shared by taxpayers who would not have made the transfers of business assets at the time they did had they known that the tax laws would be interpreted as resulting in the defective operation of the credit.

The bill does not change the definition of employer for purposes of the Federal unemployment tax. Instead, it provides for a credit (up to the usual maximum) where certain successor and predecessor employers are involved. A new subsection (sec. 3302(e)) provides that where an employer acquired during the calendar year substantially all of the property used in the trade or business of another person (or used in a separate unit of a trade or business of such person) and immediately after the acquisition employs in his trade or business one or more individuals who just before the acquisition was employed by the predecessor, then the employer may credit against its Federal unemployment tax for the year involved an amount equal to the credits it could have otherwise obtained if the predecessor had been recognized as the employer for Federal tax purposes. This treatment is available only where the predecessor is not recognized as an employer for the individuals involved for the calendar year in which the acquisition takes place.

This amendment is made to the Internal Revenue Code of 1954 for the calendar year 1955 and subsequent calendar years. Provisions having similar effect are also deemed to be included in the Internal Revenue Code of 1939 for the calendar years 1951 through 1954.

[H.R. 2585] [17]
UNEMPLOYMENT TAX CREDIT

[Senate Report No. 692, Eighty-seventh Congress, First Session, Calendar No. 668]

[August 9, 1961]

Mr. BYRD of Virginia, from the Committee on Finance, submitted the following report to accompany H. R. 2585.

The Committee on Finance, to whom was referred the bill (H.R. 2585) relating to the credits against the employment tax in the case of certain successor employers, having considered the same, report favorably thereon with an amendment and recommend that the bill as amended do pass.

I. SUMMARY OF BILL

This bill is designed to prevent the imposition of a double tax in the case of the Federal and State unemployment taxes which arises because of a technical deficiency in the Federal tax laws. At the present time, due to a variation in the definition of employer between the Federal and State laws, cases can arise

[17] Public Law 87–321, page 341, this Bulletin.

where the usual credit for State unemployment taxes is not available where a trade or business changes hands within the first 20 weeks of a calendar year. This bill corrects the faulty operation of the Federal laws by making the usual credit available in such cases.

Last year Congress passed a similar bill (H.R. 6482) but it was vetoed by the President. The President indicated that he favored the purpose of the legislation but was vetoing it because it was retroactive. Your committee has very carefully considered the President's position in this respect but has nevertheless unanimously reported this bill with an effective date applicable to the calendar year 1951 and subsequent years. As indicated subsequently in this report, it has taken this position because of the belief that to do otherwise would seriously discriminate against a relatively small group of employers and result in unjust enrichment for the Federal Government.

II. COMMITTEE AMENDMENT

The House-passed bill was effective for calendar year 1951 and subsequent years. The Treasury Department objected to the retroactive feature of the House-passed bill. The Committee on Finance gave consideration to this objection by limiting the retroactivity to statutory mergers and consolidations. It was the belief of the Committee on Finance that in the case of statutory mergers and consolidations there was considerable legal basis for allowing the credit to the successor corporation since it was in effect the same taxpayer and the retroactive provision was merely a clarification of existing law.

III. GENERAL STATEMENT

Present law levies a Federal unemployment tax on employers of four or more, equal to 3.1 percent of the wages paid each employee up to a maximum of $3,000 per employee per calendar year. Credits of up to 2.7 percentage points out of this 3.1 percentage-point tax are allowed, however, for taxes paid to State unemployment funds. In addition, credits are allowed under an approved plan for unemployment taxes which would be paid to States if the employer did not have a good experience rating.

Since 1950, wages paid by a predecessor employer have been deemed to be paid by a successor with respect to the calendar year in which the successor succeeded to the business. Ordinarily this entitles the successor to a credit against its Federal unemployment tax for State unemployment taxes paid by its predecessor. However, the 1950 amendments have proved to be defective in certain respects and as a result the Federal Government does not always allow the credit to the successor where the predecessor has paid both the State and Federal unemployment tax. This problem can arise where a State and the Federal Government have different definitions of an employer.

The Internal Revenue Code defines an employer for purposes of the Federal unemployment tax as not including any person unless in 20 different calendar weeks the person employs at least four individuals. As a result, where one employer obtains the business of another before the end of the first 20 weeks of the year, in either a tax-free or taxable transaction, the Treasury Department has held that this means that the first business making the wage payments was not an "employer" for purposes of the Federal unemployment tax. However, 19 States do not have the 20-week requirement in their laws for purposes of defining an "employer." In addition, 27 other States have retained the 20-week test but alternatively determine liability for the unemployment tax on the basis of employment experience in the preceding year. The States which do not have this 20-week test and those which have an alternative base under which liability for tax is determined on the basis of the status of the person as "employer" in the preceding year are shown in tables 1 and 2, respectively.

TABLE 1.—*States which do not have a 20-week requirement in defining employer for unemployment tax purposes*

Alaska	Maryland	Pennsylvania
Arkansas	Massachusetts	Rhode Island
California	Nevada	Utah
Connecticut	New Mexico	Washington
District of Columbia	New York	Wyoming
Hawaii	Ohio	
Idaho	Oregon	

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TABLE 2.—*States which have retained the 20-week test in defining employer for unemployment tax purposes, but which alternatively base liability for tax on the status as employer in the preceding year*

Alabama	Kentucky	North Dakota
Arizona	Louisiana	Oklahoma
Delaware	Mississippi	South Carolina
Florida	Missouri	South Dakota
Georgia	Montana	Tennessee
Illinois	Nebraska	Texas
Indiana	New Hampshire	Virginia
Iowa	New Jersey	West Virginia
Kansas	North Carolina	Wisconsin

In these 46 States where there is a different basis from that under the Federal law for determining who is the "employer," the Federal credit for the State unemployment tax does not work properly. Thus, where there is a successor business before the end of the 20th week during the calendar year, the Federal tax must be collected from the successor business which is the only "employer" for Federal tax purposes. However, in 46 States the State tax is to be collected from the first business, with little or no State tax due from the second business. As a result, almost a full State unemployment tax may be collected from the first business and a full Federal unemployment tax from the second business, but since these are considered to be different employers, little, if any, of the Federal credit for State taxes is allowable.

The problem described above can be illustrated by an example showing how the crediting of the Federal tax is intended to work in the usual case and how it may result in a double tax in the situations with which this bill is concerned. In the usual case, the Federal Government imposes a tax equal to 3.1 percent of the first $3,000 paid any employee by an employer but then allows a credit of 2.7 percent of these wages where a State unemployment tax is paid. Thus, assuming at least $3,000 in wages, there is a $93 Federal tax but against this there is allowed an $81 credit, with the result that there is a net Federal tax in this case of $12 per employee. The State tax in this case may amount to as much as $81. If the business is transferred within the first 20 weeks of the year, however, quite a different result obtains. A State tax of up to $81 is paid by the first business. In addition, a full $93 Federal tax is imposed with respect to the second business. However, no credit against this Federal tax is available because of the technical difference as to which business is considered the initial "employer." As a result, instead of a combined Federal-State tax of up to $93 per employee, there may be a combined tax of $174 per employee.

Last year Congress recognized the unfairness of imposing a double tax in the type of situation described above and passed a bill (H.R. 6482) providing that where an employer acquired the business of another person and continued to employ part or all of the employees of this other person, the employer would be allowed the credit for the State unemployment taxes paid by the other person to the extent attributable to employees who went over with the business. This amendment was to apply to calendar years beginning on or after January 1, 1951, the effective date of the Social Security Amendments Act of 1950, which contained the defective language. However, this bill was vetoed by the President. In his message of June 3 (H. Doc. 411) he indicated that he vetoed this bill because—

> Strict avoidance of retroactive tax legislation, except in extraordinary and compelling circumstances not here in evidence, is essential to orderly tax administration, the Government's revenues, and the fair treatment of taxpayers.

Despite this veto, the President urged Congress at its earliest opportunity to enact new legislation without retroactive effect. In this connection he referred to the bill as having a desirable purpose which is thwarted under present law where a predecessor does not qualify as an "employer" for Federal tax purposes.

Your commitee has given careful reconsideration to this bill and on the basis of this consideration is again reporting this bill with an effective date in the case of statutory mergers and consolidations applicable to years beginning with the calendar year 1951. Your committee is taking this action because it believes that it is improper for the Federal Government to obtain a double tax in such situations. It concluded that not to grant relief from the double taxation in

these situations for this back period would represent unjust enrichment for the Federal Government. Not only is a double tax involved, but the burden of it is particularly heavy since it discriminates against a limited number of employers by imposing a double tax in their case while no similar double tax is imposed with respect to employers generally. Moreover, when the amendment was made in 1950 allowing credits to successors for payments made by predecessors, it was thought by your committee that double taxation in these cases was prevented. This belief was also shared by taxpayers who would not have made the transfers of business assets at the time they did had they known that the tax laws would be interpreted as resulting in the defective operation of the credit.

The bill does not change the definition of employer for purposes of the Federal unemployment tax. Instead, it provides for a credit (up to the usual maximum) where certain successor and predecessor employers are involved. A new subsection (sec. 3302(e)) provides that where an employer acquired during the calendar year substantially all of the property used in the trade or business of another person (or used in a separate unit of a trade or business of such person) and immediately after the acquisition employs in his trade or business one or more individuals who just before the acquisition was employed by the predecessor, then the employer may credit against his Federal unemployment tax for the year involved an amount equal to the credits it could have otherwise obtained if the predecessor had been recognized as the employer for Federal tax purposes. This treatment is available only where the predecessor is not recognized as an employer for the individuals involved for the calendar year in which the acquisition takes place.

This amendment insofar as it relates to statutory mergers and consolidations is made to the Internal Revenue Code of 1954 for the calendar year 1955 and subsequent calendar years. Provisions having similar effect are also deemed to be included in the Internal Revenue Code of 1939 for the calendar years 1951 through 1954. The amendment applies to all acquisitions of businesses after 1960 whether corporate or noncorporate.

[H.R. 2585] [18]
UNEMPLOYMENT TAX CREDIT

[Senate Report No. 868, Eighty-seventh Congress, First Session, Calender No. 850]

[September 5, 1961]

Mr. KERR, from the Committee on Finance, submitted the following report to accompany H.R. 2585.

The Committee on Finance, to whom was referred the bill (H.R. 2585) relating to the credits against the employment tax in the case of certain successor employers, having considered the same, report favorably thereon with amendments and recommend that the bill as amended do pass.

I. SUMMARY OF HOUSE BILL

This bill is designed to prevent the imposition of a double tax in the case of the Federal and State unemployment taxes which arises because of a technical deficiency in the Federal tax laws. At the present time, due to a variation in the definition of employer between the Federal and State laws, cases can arise where the usual credit for State unemployment taxes is not available where a trade or business changes hands within the first 20 weeks of a calendar year. This bill corrects the faulty operation of the Federal laws by making the usual credit available in such cases.

Last year Congress passed a similar bill (H.R. 6482) but it was vetoed by the President. The President indicated that he favored the purpose of the legislation but was vetoing it because it was retroactive. The House passed this bill in the same form as last year's bill which was vetoed. Your committee originally amended the House bill to provide that the retroactive provisions would apply only in the case of statutory mergers and consolidations of corporations.

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[18] Public Law 87-321, page 341, this Bulletin.

This was done in an effort to meet some of the objection to the House bill. The bill was first reported in this form.

Subsequent to the reporting of the bill, however, the Internal Revenue Service determined that the problem for prior years in the the case of statutory mergers and consolidations of corporations, could be handled administratively, under existing law, by revoking certain provisions of old rulings. Because of this change in position your committee felt that there was no need for applying the bill retroactively.

Accordingly, the committee agreed to ask that the bill be recommitted for the purpose of eliminating its retroactive feature.

II. COMMITTEE AMENDMENTS

The House-passed bill was effective for calendar year 1951 and subsequent years. Your committee's bill, as reported August 9, 1961 (S. Rept. 692, 87th Cong., 1st sess.), applied prospectively with respect to all business acquisitions, both corporate and noncorporate. It also applied to calendar year 1951 and subsequent years, but with respect only to statutory mergers and consolidations. Because the Treasury Department has now been able to administratively allow credit for prior years in cases of statutory mergers or consolidations, the bill was recommitted to the Committee on Finance on August 31, 1961, for the purpose of enabling the committee to eliminate the retroactive effect of the bill.

As the bill is now being reported it will apply prospectively only, and will apply to all business acquisitions, both corporate and noncorporate.

The committee also added to the bill an amendment which would provide that crushing and grinding are to be treated as mining processes in the case of clay and quartzite used in the manufacture of refractory products for open years beginning before January 1, 1961. This amendment would also provide that the value of the ground clay and quartzite shall be equal to 87½ percent of the average lowest price for which such clay is sold by the taxpayer during the taxable year.

III. GENERAL EXPLANATION OF UNEMPLOYMENT TAX AMENDMENT

Present law levies a Federal unemployment tax on employers of four or more, equal to 3.1 percent of the wages paid each employee up to a maximum of $3,000 per employee per calendar year. Credits of up to 2.7 percentage points out of this 3.1 percentage-point tax are allowed, however, for taxes paid to State unemployment funds. In addition, credits are allowed under an approved plan for unemployment taxes which would be paid to States if the employer did not have a good experience rating.

Since 1950, wages paid by a predecessor employer have been deemed to be paid by a successor with respect to the calendar year in which the successor succeeded to the business. Ordinarily this entitles the successor to a credit against its Federal unemployment tax for State unemployment taxes paid by its predecessor. However, the 1950 amendments have proved to be defective in certain respects and as a result the Federal Government does not always allow the credit to the successor where the predecessor has paid both the State and Federal unemployment tax. This problem can arise where a State and the Federal Government have different definitions of an employer.

The Internal Revenue Code defines an employer for purposes of the Federal unemployment tax as not including any person unless in 20 different calendar weeks the person employs at least four individuals. As a result, where one employer obtains the business of another before the end of the first 20 weeks of the year, in either a tax-free or taxable transaction, the Treasury Department has held that this means that the first business making the wage payments was not an "employer" for purposes of the Federal unemployment tax. However, 19 States do not have the 20-week requirement in their laws for purposes of defining an "employer." In addition, 27 other States have retained the 20-week test but alternatively determine liability for the unemployment tax on the basis of employment experience in the preceding year. The States which do not have this 20 week test and those which have an alternative base under which liability for tax is determined on the basis of the status of the person as "employer" in the preceding year are shown in tables 1 and 2, respectively.

TABLE 1.—*States which do not have a 20-week requirement in defining employer for unemployment tax purposes*

Alaska	Maryland	Oregon
Arkansas	Massachusetts	Pennsylvania
California	Nevada	Rhode Island
Connecticut	New Mexico	Utah
District of Columbia	New York	Washington
Hawaii	Ohio	Wyoming
Idaho		

TABLE 2.—*States which have retained the 20-week test in defining employer for unemployment tax purposes, but which alternatively base liability for tax on the status as employer in the preceding year*

Alabama	Kentucky	North Dakota
Arizona	Louisiana	Oklahoma
Delaware	Mississippi	South Carolina
Florida	Missouri	South Dakota
Georgia	Montana	Tennessee
Illinois	Nebraska	Texas
Indiana	New Hampshire	Virginia
Iowa	New Jersey	West Virginia
Kansas	North Carolina	Wisconsin

In these 46 States where there is a different basis from that under the Federal law for determining who is the "employer," the Federal credit for the State unemployment tax does not work properly. Thus, where there is a successor business before the end of the 20th week during the calendar year, the Federal tax must be collected from the successor business which is the only "employer" for Federal tax purposes. However, in 46 States the State tax is to be collected from the first business, with little or no State tax due from the second business. As a result, almost a full State unemployment tax may be collected from the first business and a full Federal unemployment tax from the second business, but since these are considered to be different employers, little, if any, of the Federal credit for State taxes is allowable.

The problem described above can be illustrated by an example showing how the crediting of the Federal tax is intended to work in the usual case and how it may result in a double tax in the situations with which this bill is concerned. In the usual case, the Federal Government imposes a tax equal to 3.1 percent of the first $3,000 paid any employee by an employer but then allows a credit of 2.7 percent of these wages where a State unemployment tax is paid. Thus, assuming at least $3,000 in wages, there is a $93 Federal tax but against this there is allowed an $81 credit, with the result that there is a net Federal tax in this case of $12 per employee. The State tax in this case may amount to as much as $81. If the business is transferred within the first 20 weeks of the year, however, quite a different result obtains. A State tax of up to $81 is paid by the first business. In addition, a full $93 Federal tax is imposed with respect to the second business. However, no credit against this Federal tax is available because of the technical difference as to which business is considered the initial "employer." As a result, instead of a combined Federal-State tax of up to $93 per employee, there may be a combined tax of $174 per employee.

Last year Congress recognized the unfairness of imposing a double tax in the type of situation described above and passed a bill (H.R. 6482) providing that where an employer acquired the business of another person and continued to employ part or all of the employees of this other person, the employer would be allowed the credit for the State unemployment taxes paid by the other person to the extent attributable to employees who went over with the business. This amendment was to apply to calendar years beginning on or after January 1, 1951, the effective date of the Social Security Amendments Act of 1950, which contained the defective language. However, this bill was vetoed by the President. In his message of June 3 (H. Doc. 411) he indicated that he vetoed this bill because—

> Strict avoidance of retroactive tax legislation, except in extraordinary and compelling circumstances not here in evidence, is essential to orderly tax administration, the Government's revenues, and the fair treatment of taxpayers.

Despite this veto, the President urged Congress at its earliest opportunity to enact new legislation without retroactive effect. In this connection he referred to the bill as having a desirable purpose which is thwarted under present law where a predecessor does not qualify as an "employer" for Federal tax purposes.

Your committee carefully reconsidered this bill and on the basis of such reconsideration the bill was originally reported to the Senate with an effective date, in the case of statutory consolidations and mergers, applicable to years beginning with the calendar year 1951. Your committee took this action because it believed that it was improper for the Federal Government to obtain a double tax in such situations, and that the Government would be unjustly enriched in the absence of legislation. Moreover, your committee felt that in case of statutory mergers or consolidations, the original employer, in effect, continued to exist under a new corporate structure.

Since the bill was reported, the Assistant Secretary of the Treasury informed the committee by letter dated August 30, 1961, that the Internal Revenue Service had determined that the successor corporation resulting from a statutory merger or consolidation is the same employer and taxpayer as the predecessor corporation within the meaning of the existing provisions of the Federal Unemployment Tax Act. The text of this letter is as follows:

TREASURY DEPARTMENT,
Washington, August 30, 1961.

HON. HARRY F. BYRD,
Chairman, Committee on Finance,
New Senate Office Building,
Washington, D.C.

DEAR MR. CHAIRMAN: On August 9, the Senate Finance Committee reported, with an amendment, H.R. 2585, relating to the credits against the employment tax in the case of certain successor employers. The amendment would apply the proposed successor employer rules retroactively to calendar years after 1950 in the case of statutory mergers and consolidations.

As noted in our report of August 9 on H.R. 2585, proponents of retroactive relief in the case of statutory mergers had presented certain legal arguments to the effect that the retroactive provision merely represented the correct interpretation of existing law. The report of the Committee on Finance also states that it was the belief of the committee that the retroactive provision was merely a clarification of existing law. On August 15, 1961, the Acting Chief Counsel of the Internal Revenue Service, after reconsideration of this legal issue, ruled that the successor corporation resulting from a statutory merger or consolidation is the same employer and taxpayer as the predecessor corporation within the meaning of the existing provisions of the Federal Unemployment Tax Act. On August 16, 1961, the Acting Commissioner of Internal Revenue expressed his agreement with this interpretation of existing law and also with the Chief Counsel's recommendation that prior rulings on this subject be modified accordingly. Consequently, the retroactive provision contained in the bill not only appears to be undesirable in principle but also is now unnecessary.

As we also noted in our report of August 9, the Internal Revenue Service, for administrative reasons, preferred a somewhat different technique for accomplishing the objectives of the bill on a prospective basis. However, the Service has informally advised us that the administrative problems involved in the present bill are not sufficiently great as to warrant modifying the bill at this time.

In view of the foregoing, the Treasury Department favors the enactment of H.R. 2585 if the unnecessary retroactive provision is deleted.

The Bureau of the Budget has advised the Treasury Department that there is no objection from the standpoint of the administration's program to the presentation of this report.

Sincerely yours,

STANLEY S. SURREY,
Assistant Secretary.

On the basis of this letter, it is the opinion of the committee that retroactive application of the amendment no longer is desirable. Accordingly, on August 31, 1961, the bill was recommitted to the committee and is now being reported on a prospective basis. As reported it will apply to all business acquisitions, both corporate and noncorporate, which occur in calendar year 1961 and thereafter.

The bill does not change the definition of employer for purposes of the Federal unemployment tax. Instead, it provides for a credit (up to the usual maximum) where certain successor and precessor [sic] employers are involved. A new subsection (sec. 3302(e)) provides that where an employer acquired during the calendar year substantially all of the property used in the trade or business of another person (or used in a separate unit of a trade or business of such person) and immediately after the acquisition employs in his trade or business one or more individuals who just before the acquisition was employed by the predecessor, then the employer may credit against his Federal unemployment tax for the year involved an amount equal to the credits it could have otherwise obtained if the predecessor had been recognized as the employer for Federal tax purposes. This treatment is available only where the predecessor is not recognized as an employer for the individuals involved for the calendar year in which the acquisition takes places.

IV. ELECTION AS TO BASE FOR DETERMINING PERCENTAGE DEPLETION DEDUCTION IN THE CASE OF CLAY AND QUARTZITE USED IN MAKING REFRACTORY PRODUCTS

To determine the percentage depletion allowance under present law, it is necessary to multiply the percentage rate applicable to the particular mineral by the value of the mineral at the point at which the mining process ends. This point is referred to as the "cutoff point." In the case of clay and quartzite used in the production of refractory products, it has generally been the administrative practice of the Internal Revenue Service to treat crushing and grinding as mining processes and to establish the cutoff point at the conclusion of these processes. However, as a result of the Supreme Court decision in *U.S.* v. *Cannelton Sewer Pipe Co.*, 364 U.S. 76 (1960), the Government now contends that the cutoff point with respect to such clay and quartzite occurs when the minerals are extracted from the grounds.

Your committee is of the opinion that, because of the past administrative practice of the Internal Revenue Service, taxpayers using clay and quartzite in the refractories industry should be given an election to use a cutoff point after crushing and grinding for taxable years beginning before January 1, 1961. Therefore, your committee has added an amendment to H.R. 2585 to provide such an election. No inferences should be drawn from this, however, as to the cutoff point for such clay or quartzite with respect to future years or with respect to past years if this election is not made.

Your committee's amendment also provides a method for valuing the clay or quartzite where the election is made. In past years in which the Internal Revenue Service generally allowed crushing and grinding as mining processes in the refractories industry, there was disagreement as to how the value of the clay and quartzite should be determined at this cutoff point. Taxpayers contended that the value of the ground minerals should be determined by reference to prices for which ground refractory clay and quartzite were sold for use as mortar. The Internal Revenue Service contended that since only small percentages of the minerals were sold for mortar, the mortar prices were not representative of the values for which ground refractory clay and quartzite could be sold generally. Therefore, the Service refused to accept these prices as determinative of the value at the cutoff point. Instead the Service sought to establish the value of the minerals in question by such methods as allocating the costs and profits attributable to the finished products between the taxpayer's mining and manufacturing operations. Under these methods, the determinations of value were usually substantially lower than the prices used by taxpayers to determine value. Due to the disagreement as to the method of determining the value of the minerals at the cutoff point, few cases in the refractories industry were settled, and many taxpayers have open years back to 1951.

Because of this dispute on the question of value, your committee is of the opinion that any legislation adopted in this area should not only provide for the allowance of crushing and grinding as mining processes for the refractories industry for past years, but should also provide a method of determining the value at this cutoff point. Such legislation is desirable from the standpoint of both the taxpayers and the Government because in substantial measure it will resolve the depletion issue for refractory products for past years.

It is understood that, out of the cases that were settled in the refractories industry, at least one case was settled on the basis of the full mortar price,

and several others were settled using values ranging from 71 to 87 percent of the mortar prices. In view of this range of settlements, your committee's amendment provides that, if the election is made, the taxpayer is to use a value of 87½ percent of the average lowest price for which he sold ground refractory clay or quartzite during the taxable year.

The election applies only to quartzite and clay used in the production of products generally recognized as refractory products by the refractories industry. This would include, for example, clay firebrick and special shapes, silica brick and shapes, refractory bonding mortars, etc. Furthermore, the election may be made only by a taxpayer who both mines the clay or quartzite and uses it in the production of refractory products.

If the election is made, crushing, grinding, and separation of the clay or quartzite from waste are to be treated as allowable mining process. In determining the price to which the 87½ percent referred to above is to be applied, the average lowest published price or the average lowest selling price at which the crushed and ground products are sold during the year is to be used. From this, gross income from the property is determined by multiplying this price by the number of tons of clay or quartzite used in refractory products sold during the year. In determining the price at which the sales are made exceptional, unusual, or nominal sales are to be disregarded. Thus, for example, if a taxpayer made an accommodation sale during the taxable year at other than the regular price, this sale is not to be used for purposes of your committee's amendment.

It is intended that one price be used with respect to all of the taxpayer's clay used in refractory products sold during the taxable year, and similarly that one price be used with respect to quartzite. If there was a change in the lowest selling price for ground clay during the taxable year, the two or more prices will be averaged according to the number of days during the taxable year that each was in effect to determine the average lowest price. The amendment also provides that if the taxpayer makes no sales of ground clay or quartzite, he is to use the average lowest recognized price for such minerals in his marketing area published in a publication of the industry.

Under your committee's amendment, the election must be made by the taxpayer on or before 60 days after the date of publication of final regulations under this provision. Once made, the election is irrevocable. The manner of making the election is to be prescribed by Treasury regulations.

[H.R. 2010] [19]
MEXICAN FARM LABOR PROGRAM

[Senate Report No. 619, Eighty-seventh Congress, First Session, Calendar No. 592]

[July 25, 1961]

MR. JORDAN, from the Committee on Agriculture and Forestry, submitted the following report together with supplemental views to accompany H.R. 2010.

The Committee on Agriculture and Forestry, to whom was referred the bill (H.R. 2010), to amend title V of the Agricultural Act of 1949, as amended, and for other purposes, having considered the same, report thereon with a recommendation that it do pass with an amendment.

HEARINGS

Hearings were conducted by the Subcommittee on Agricultural Research and General Legislation on S. 1466, S. 1945, and H.R. 2010. The hearings have been printed.

SHORT EXPLANATION

This bill, with the committee amendment, which is in the nature of a substitute, would amend title V of the Agricultural Act of 1949 to—

(1) incorporate in the act an existing appropriation act requirement that employers reimburse the United States, up to a $15 maximum, for all ex-

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[19] This publication of the Committee Report is restricted to excerpts involving internal revenue matters; Public Law 87–345, page 343, this Bulletin.

penses of the program, except salaries and expenses of personnel engaged in compliance activities;

(2) add working conditions to section 503(3) so that it will prohibit Mexican workers from being made available in any area unless reasonable efforts have been made to attract domestic workers at "wages, standard hours of work, and working conditions" comparable to those offered to Mexican workers;

(3) prohibit the furnishing to, or retention by, any employer of any Mexican—

(i) for employment in other than temporary or seasonal occupations or to operate or maintain power-driven machinery, except in specific cases to avoid undue hardship; and

(ii) unless the employer pays both domestic and Mexican workers not less than the prevailing wage paid in the area to domestic workers engaged in similar work;

(4) prohibit the furnishing of Mexican workers for some processing activities; and

(5) extend the program 2 years, until December 31, 1963.

HISTORY OF MEXICAN FARM LABOR PROGRAM

During World War II, and until 1951, Mexican workers were admitted into the United States for temporary employment in U.S. agriculture under various authorities.

In 1951, the Congress approved Public Law 78 (82d Cong.), which added title V to the Agricultural Act of 1949. The major features of this legislation are as follows:

1. Authorizes the negotiation of an agreement with the Republic of Mexico establishing procedures for the admission of Mexican nationals into the United States for temporary employment.

2. Authorizes the Department of Labor to (*a*) undertake a recruitment and placement function with respect to such workers, (*b*) assist workers and farmers to enter into contracts for agricultural employment, and (*c*) guarantee the payment of wages and transportation by farmer employers.

3. Requires employers who wish to employ Mexican workers to (*a*) indemnify the U.S. Government for its guaranty of their contracts, (*b*) pay into a revolving fund a fee for each worker to support the program financially.

4. Restricts the use of Mexican workers to areas where the Secretary of Labor certifies that (1) domestic workers, able, willing, and qualified are not available; (2) the employment of Mexican workers will not adversely affect the wages and working conditions of domestic agricultural workers similarly employed; and (3) reasonable efforts have been made to attract domestic workers at wages and hours comparable to those offered Mexican workers.

5. Eliminates bond requirement of general immigration statutes for such workers.

6. Provides that no such workers would be provided any employer who employed illegal aliens, either with knowledge or with reasonable grounds to believe they were here illegally.

7. Exempts such workers from social security and income tax provisions.

This statute has been implemented by an agreement with Mexico which sets forth in substantial detail the procedures, terms, and conditions of the contract of employment, and other matters.

Public Law 78 was scheduled to expire December 31, 1953. It has subsequently been extended on various occasions to December 31, 1955, June 30, 1959, June 30, 1961, and December 31, 1961.

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SECTION-BY-SECTION EXPLANATION

Section 1: The first section of the bill makes no substantive change in the law, but incorporates in the basic act covering the Mexican farm labor program provisions now carried in appropriation acts. The Departments of Labor, and Health, Education, and Welfare Appropriation Act, 1961, requires reimbursements under section 502(2) of the basic act to include all expenses of program operations, except contract compliance expenses. Section 502(2) requires employers of workers recruited under the act to reimburse the United States only for essential expenses incurred by it for the transportation and subsistence of

workers in amounts not to exceed $15 per worker. The first section of the bill amends section 502(2) to require reimbursement of all essential expenses, except salaries and expenses of personnel engaged in compliance activities, in amounts not to exceed $15 per worker.

Section 2: Section 503 of the basic act prohibits workers recruited under the act from being made available in any area unless the Secretary of Labor finds that—

> (1) sufficient domestic workers who are able, willing, and qualified are not available at the time and place needed to perform the work for which such workers are to be employed, (2) the employment of such workers will not adversely affect the wages and working conditions of domestic agricultural workers similarly employed, and (3) reasonable efforts have been made to attract domestic workers for such employment at wages and standard hours of work comparable to those offered to foreign workers.

Section 2 of the bill amends clause (3) just quoted to include "working conditions" along with wages and standard hours of work. The term "working conditions" is intended by the committee to refer to the physical conditions under which the work is performed, such as those concerned with sanitation and safety, and not to include terms of employment such as housing, transportation, subsistence, insurance, and work guarantees. Mexican nationals enter this country under an international agreement in accordance with the terms of a standard work contract. They are not free agents in this country. Because of this, a responsibility to remain with the employer with whom they contract is imposed upon them. They do not bring their families with them. They enter this country to do a particular job after which they return home. Domestic workers, on the other hand, are free to come and go as they please. They may seek other employment in or out of agriculture if they wish. It is not intended, therefore, to require guarantees from farmers as to housing, payment of transportation, and periods of work for workers who may not fulfill their end of the bargain.

Section 3: Section 3 adds two new sections to the basic act, sections 504 and 505.

The new section 504 prohibits the employment of any workers recruited under the act for other than temporary or seasonal employment, or to operate or maintain power-driven machinery. The Secretary of Labor may make exceptions from this prohibition in specific cases to avoid undue hardship. The purpose of the program is to supplement the domestic labor force in peak periods, such as at harvest time, when crops may be lost through a lack of sufficient workers. It is not intended to provide Mexican workers for year-round jobs which might well be filled by domestic workers. Nor is it intended to provide Mexican workers for the higher skilled jobs for which domestic workers can be found. While it may be difficult to find domestic workers for the so-called stoop labor jobs, there should be domestic workers available even in periods of peak employment for the more desirable jobs of operating or maintaining power-driven machinery. The prohibition of this section with respect to machinery, of course, extends only to employment to operate or maintain such machinery. It would not prohibit employment merely involving power-operated machinery, such as the placing of produce on trucks, or the placing of hand-cut produce on vegetable harvesters, nor would it prohibit a worker employed for other appropriate purposes from incidental, emergency maintenance work such as the repair of a flat tire.

The new section 505 prohibits workers recruited under the act from being made available to, or permitted to remain in the employ of, any employer unless he offers and pays both domestic and foreign workers not less than the prevailing wage paid in the area to domestic workers engaged in similar work. It was not the purpose of the committee to establish minimum wages for farmworkers or to authorize the Secretary of Labor to establish such minimum wages, and the bill does not do so. The establishment of minimum wages falls within the province of the Committee on Labor and Public Welfare, rather than this committee, and employees in agriculture have for good reason been exempted from the minimum wage provisions of the Fair Labor Standards Act. In the hearings there were complaints that in some areas Mexican workers were being paid less than domestic workers and that in other areas domestic workers were being paid less than Mexican workers. The agreement with Mexico provides that the Mexican workers be paid not less than the prevailing wage rate paid to domestic workers for similar work at the time the work is per-

formed. The new section 505 would require each employer of Mexican workers to pay his domestic workers, as well as his Mexican workers, not less than such prevailing wage, whatever it might be at that time. This new provision is not intended to alter the existing obligation of the Secretary of Labor under section 503(2) of the act not to make Mexican workers available in any area if their employment will adversely affect the wages and working conditions of domestic workers similarly employed, or to require the abandonment of any present policies or practices in the administration of section 503(2), and the new section 505 so provides.

Section 4: Section 4 prohibits the furnishing of Mexican workers for certain processing activities. It excludes from the definition of the agricultural employment for which workers may be recruited under the act—

> horticultural employment, cotton ginning, compressing, and storing, crushing of oilseeds, and the packing, canning, freezing, drying, or other processing of perishable or seasonal agricultural products.

This would leave covered by the act services or activities within the provisions of section 3(f) of the Fair Labor Standards Act of 1938 or section 3121(g) of the Internal Revenue Code (which by sec. 7852(b) of the Internal Revenue Code was made applicable in lieu of sec. 1426(h) of the Internal Revenue Code (of 1939)). Section 3121(g) includes the raising of horticultural commodities, cotton ginning, and a limited amount of packaging, processing, freezing, and storing for farm operators.

Section 5 extends the program 2 years until December 31, 1963.

SUPPLEMENTAL VIEWS

H.R. 2010 as amended by the Senate Agricultural Committee does improve Public Law 78 by prohibiting the use of Mexican nationals for employment in other than temporary or seasonal occupations or for employment in the operation and maintenance of power-driven machinery except in those cases in which prohibition would cause undue hardship.

Although these amendments improve the basic law, they will do little toward solving the economic, social, and moral problems raised by the operation of the Mexican farm labor program.

Migratory workers are among the most neglected and underprivileged groups in the American economy. Their wages are low, they suffer much from unemployment, they are not covered by unemployment compensation laws or by minimum wage laws, and they are generally denied the benefits of workmen's compensation laws. Because their work requires them to move from one area to another, they and their families do not have the advantage of services and facilities that normally go with stable membership in a community.

These basic difficulties of American migrants are intensified by the annual importation of 300,000 Mexican nationals under the Mexican farm labor program. The experience of 10 years of operation of the program has demonstrated that it does affect adversely wages, employment opportunities, and working conditions of domestic workers. This is the unqualified testimony of the Secretary of Labor, Mr. Goldberg, who has the responsibility for the administration of the program. He and the administration have supported extension of Public Law 78 on the condition that substantial reforms such as provided in S. 1945 are adopted. Secretary of Labor Mitchell last year opposed extension of Public Law 78 unless substantial reforms were approved.

Public Law 78 was enacted in 1951 at a time of labor shortage during the Korean conflict. It began as a temporary program, but it has been extended by Congress four times. During this period the farm labor force has declined, technological change in agriculture has continued at a rapid rate, and unemployment and underemployment have increased as rural problems. Yet at the same time the Mexican farm labor program has expanded greatly.

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We do not believe that anyone can accurately establish the extent of the need for this program under the existing practices. The Department of Labor authorizes Mexican nationals when a sufficient number of workers cannot be obtained at the prevailing wage in the area for the type of work. Where the prevailing wage is very low, the number of workers who are able and willing to work under those conditions is likely to be reduced. The most recent figures

(June 1961) of the Department of Labor show several counties in which wages of 30 to 50 cents per hour have been found to prevail among domestic workers. These rates are in areas and for work in which Mexican nationals are likewise employed.

The employer seeking additional employees at a time of labor shortage normally offers higher wages and better working conditions. Under Public Law 78 there is little incentive to do this.

We do not know what percentage of those who have left the farm labor force in the past 10 years would be willing to work in positions now filled by Mexican nationals if wages and working conditions were improved. As long as the present criteria are used to authorize the use of Mexican nationals, we cannot know the extent of the need.

The committee had before it a bill (S. 1945) which incorporated the recommendations of the Department of Labor and was supported by the Secretary of Labor and the administration. It contained major provisions which were not adopted by the committee.

One of these provisions would have limited the use of Mexican nationals to employers who have made reasonable efforts to attract domestic workers at terms and conditions of employment reasonably comparable to those offered Mexican nationals. Under the international agreement between the United States Government and the Republic of Mexico, Mexican nationals coming to this country under contract are guaranteed transportation costs, employment on three-fourths of the workdays in the contract period, subsistence when underemployed, housing, medical care, and compensation for injuries on the job, and health and accident insurance at reasonable cost. In addition, they are assured the wage rate that prevails among U.S. workers similarly employed and a minimum wage of 50 cents per hour. These are benefits not enjoyed by most domestic migratory workers.

S. 1945 also proposed a new test for adverse affect. Under terms of this provision, the employer would have been required to pay Mexican nationals no less than the average hourly farm wage in the State, or the national hourly farm wage average, whichever is the lesser. This would establish a clear, objective, and reasonable minimum base to assist the Secretary of Labor in determining whether Mexican nationals should be certified.

These two provisions should be adopted to provide very limited protection for American migrant workers. They are clearly consistent with the fundamental policy and intent of Congress as stated in section 503 of Public Law 78 which requires that the Secretary of Labor before approving the importation of Mexican nationals certify that there is a shortage of domestic workers and that—

> the employment of such workers will not adversely affect the wages and working conditions of domestic agricultural workers similarly employed.

The experience of the past 10 years has demonstrated that this intent has not been achieved. In large part the difficulty has resulted from the absence of a formula or of guidelines to determine when adverse effect has taken place. We do not believe Public Law 78 should be extended without providing the Secretary of Labor with additional directives necessary to protect domestic workers from such adverse effects.

EUGENE J. MCCARTHY.
WILLIAM PROXMIRE.
STEPHEN M. YOUNG.
PHILIP A. HART.
MAURINE B. NEUBERGER.

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The following provisions are not amended by the bill, but are related to the change in definition of "Agricultural employment" made by section 4 of the bill.

SECTION 3(f) OF THE LABOR STANDARDS ACT OF 1938

"Agriculture" includes farming in all its branches and among other things includes the cultivation and tillage of the soil, dairying, the production, cultivation, growing, and harvesting of any agricultural or horticultural commodities (including commodities defined as agricultural commodities in section 1141j(g) of title 12), the raising of livestock, bees, fur-bearing animals, or poultry, and any practices (including any forestry or lumbering operations) performed by a farmer or on a farm as an incident to or in conjunction with such farming operations, including preparation for market, delivery to storage or to market or to carriers for transportation to market.

(26 U.S.C. 3121(g))[20]

(g) Agricultural Labor.

For purposes of this chapter, the term "agricultural labor" includes all service performed—

(1) on a farm, in the employ of any person, in connection with cultivating the soil, or in connection with raising or harvesting any agricultural or horticultural commodity, including the raising, shearing, feeding, caring for, training, and management of livestock, bees, poultry, and fur-bearing animals and wildlife;

(2) in the employ of the owner or tenant or other operator of a farm, in connection with the operation, management, conservation, improvement, or maintenance of such farm and its tools and equipment, or in salvaging timber or clearing land of brush and other debris left by a hurricane, if the major part of such service is performed on a farm;

(3) in connection with the production or harvesting of any commodity defined as an agricultural commodity in section 15(g) of the Agricultural Marketing Act, as amended (46 Stat. 1550, § 3; 12 U.S.C. 1141j), or in connection with the ginning of cotton, or in connection with the operation or maintenance of ditches, canals, reservoirs, or waterways, not owned or operated for profit, used exclusively for supplying and storing water for farming purposes;

(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;

(B) in the employ of a group of operators of farms (other than a cooperative organization) in the performance of service described in subparagraph (A), but only if such operators produced all of the commodity with respect to which such service is performed. For purposes of this subparagraph, any unincorporated group of operators shall be deemed a cooperative organization if the number of operators comprising such group is more than 20 at any time during the calendar quarter in which such service is performed;

(C) the provisions of subparagraphs (A) and (B) shall not be deemed to be applicable with respect to service performed in connection with commercial canning or commercial freezing or in connection with any agricultural or horticultural commodity after its delivery to a terminal market for distribution for consumption; or

(5) on a farm operated for profit if such service is not in the course of the employer's trade or business or is domestic service in a private home of the employer.

As used in this subsection, the term "farm" includes stock, dairy, poultry, fruit, fur-bearing animal, and truck farms, plantations, ranches, nurseries, ranges, greenhouses or other similar structures used primarily for the raising of agricultural or horticultural commodities, and orchards.

[H.R. 2010][21]
MEXICAN FARM LABOR PROGRAM

[Conference Report No. 1198, Eighty-seventh Congress, First Session]

[September 15, 1961]

Mr. POAGE, from the committee of conference, submitted the following conference report to accompany H.R. 2010.

The committee of conference on the disagreeing votes of the two Houses on the amendment of the Senate to the bill (H.R. 2010) to amend title V of the Agricultural Act of 1949, as amended, and for other purposes, having met, after full

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[20] Under sec. 7852(b) of the Internal Revenue Code, the reference in sec. 507(l) of the Agricultural Act of 1949 to sec. 1426(h) of the Internal Revenue Code should be deemed a reference to sec. 3121(g) of the Internal Revenue Code.

[21] Public Law 87-345, page 343, this Bulletin.

and free conference, have agreed to recommend and do recommend to their respective Houses as follows:

That the House recede from its disagreement to the amendment of the Senate and agree to the same with an amendment as follows:

In lieu of the matter proposed to be inserted by the Senate amendment insert the following:

That section 502(2) of the Agricultural Act of 1949, as amended is amended to read as follows:

"(2) to reimburse the United States for essential expenses incurred by it under this title, except salaries and expenses of personnel engaged in compliance activities, in amounts not to exceed $15 per worker; and".

SEC. 2. Clause (3) of section 503 of such Act is amended to read as follows: "(3) reasonable efforts have been made to attract domestic workers for such employment at wages, standard hours of work, and working conditions comparable to those offered to foreign workers".

SEC. 3. Sections 504 through 509 of such Act are renumbered sections "505" through "510" respectively; the reference to "section 507" in section 508, renumbered as section "509", is changed to section "508"; and the following new section "504" is inserted after section 503:

"SEC. 504. No workers recruited under this title shall be made available to any employer or permitted to remain in the employ of any employer—

"(1) for employment in other than temporary or seasonal occupations, except in specific cases when found by the Secretary of Labor necessary to avoid undue hardship; or

"(2) for employment to operate or maintain power-driven self-propelled harvesting, planting, or cultivating machinery, except in specific cases when found by the Secretary of Labor necessary for a temporary period to avoid undue hardship."

SEC. 4. Section 505 of such Act, as amended, renumbered as section "506", is amended by adding at the end thereof the following:

"(d) Workers recruited under the provisions of this title shall not be subject to any Federal or State tax levied to provide illness or disability benefits for them."

SEC. 5. Paragraph (1) of section 507 of such Act, renumbered as section "508", is amended by changing the comma after the words "Internal Revenue Code, as amended" to a period and deleting the remainder of the paragraph.

SEC. 6. Section 509 of such Act, as amended, renumbered as section "510", is amended by striking "December 31, 1961" and inserting "December 31, 1963".

And the Senate agree to the same.

W. R. POAGE,
E. C. GATHINGS,
WATKINS M. ABBITT,
PAGE BELCHER,
CHARLES M. TEAGUE,
Managers on the Part of the House.

ALLEN J. ELLENDER,
OLIN D. JOHNSTON,
SPESSARD L. HOLLAND,
B. EVERETT JORDAN,
GEORGE D. AIKEN,
MILTON R. YOUNG,
BOURKE B. HICKENLOOPER,
Managers on the Part of the Senate.

STATEMENT OF MANAGERS ON THE PART OF THE HOUSE

The managers on the part of the House at the conference on the disagreeing votes of the two Houses on the amendment of the Senate to the bill H.R. 2010, to amend title V of the Agricultural Act of 1949, as amended, and for other purposes, submit the following statement in explanation of the effect of the action agreed upon and recommended in the accompanying conference report.

The House bill was a simple extension for 2 years of the existing provision of title V of the Agricultural Act of 1949, which provides for the Mexican farm labor program. The Senate amendment struck out all after the enacting clause of the House bill and substituted language consisting of six sections which extended the act for 2 years and made several substantive amendments therein.

The committee of conference has agreed to the Senate amendments with two major changes: (1) elimination of the subsection providing minimum wage rates other than those already provided for in the act and in the agreement with Mexico; and (2) modification of the provision relating to the use of Mexican workers to operate or maintain power-driven machinery so that this provision will apply only to power-driven, self-propelled harvesting, planting, or cultivating machinery.

Following is a section-by-section explanation of the substitute to the Senate amendment agreed to by the conferees:

SECTION-BY-SECTION EXPLANATION

Section 1.—The first section of the amendment makes no substantive change in the law, but incorporates in the basic act covering the Mexican farm labor program provisions now carried in appropriation acts. The Departments of Labor, and Health, Education, and Welfare Appropriation Act, 1961, requires reimbursements under section 502(2) of the basic act to include all expenses of program operations, except contract compliance expenses. Section 502(2) requires employers of workers recruited under the act to reimburse the United States only for essential expenses incurred by it for the transportation and subsistence of workers in amounts not to exceed $15 per worker. The first section of the amendment amends section 502(2) to require reimbursement of all essential expenses, except salaries and expenses of personnel engaged in compliance activities, in amounts not to exceed $15 per worker.

Section 2.—Section 503 of the basic act prohibits workers recruited under the act from being made available in any area unless the Secretary of Labor finds that—

> (1) sufficient domestic workers who are able, willing, and qualified are not available at the time and place needed to perform the work for which such workers are to be employed,
>
> (2) the employment of such workers will not adversely affect the wages and working conditions of domestic agricultural workers similarly employed, and (3) reasonable efforts have been made to attract domestic workers for such employment at wages and standard hours of work comparable to those offered to foreign workers.

Section 2 amends clause (3) just quoted to include "working conditions" along with wages and standard hours of work. The term "working conditions" is intended by the committee to refer to the physical conditions under which the work is performed, such as those concerned with sanitation and safety, and not to include terms of employment such as housing, transportation, subsistence, insurance, and work guarantees. Mexican nationals enter this country under an international agreement in accordance with the terms of a standard work contract. They are not free agents in this country. Because of this, a responsibility to remain with the employer with whom the contract is imposed upon them. They do not bring their families with them. They enter this country to do a particular job after which they return home. Domestic workers, on the other hand, are free to come and go as they please. They may seek other employment in or out of agriculture if they wish. It is not intended, therefore, to require guarantees from farmers as to housing, payment of transportation, and periods of work for workers who may not fulfill their end of the bargain.

Section 3.—Section 3 adds a new section 504 to the basic act. The new section prohibits the employment of any workers recruited under the act for other than temporary or seasonal employment or to operate or maintain power-driven self-propelled harvesting, planting, or cultivating machinery. The Secretary of Labor may make exceptions from these prohibitions in specific cases to avoid undue hardship.

As passed by the Senate, this section applied to all power-driven machinery. The conference substitute limits its application to power-driven self-propelled harvesting, planting, and cultivating machinery.

The purpose of the program is to supplement the domestic labor force in peak periods, such as at harvest time, when crops may be lost through a lack of sufficient workers. It is not intended to provide Mexican workers for year-round jobs which might well be filled by domestic workers. Nor is it intended to provide Mexican workers for the higher skilled jobs for which domestic workers can be found.

The prohibition of this section with respect to machinery, of course, extends only to employment to operate or maintain such machinery. It would not prohibit the incidental handling of such machinery or employment merely involving power-operated machinery, such as the placing of produce on trucks, or the placing of hand-cut produce on vegetable harvesters, nor would it prohibit a worker employed for other appropriate purposes from incidental, emergency maintenance work such as the repair of a flat tire.

Section 4.—Under the basic act and the agreement with Mexico entered into thereunder, illness and disability insurance is provided for Mexican workers. This section will provide that such workers shall not, in addition, be subject to any Federal or State tax levy to provide illness or disability benefits for them. The committee understands that California has recently enacted a law which would provide such benefits and that the State has requested that Mexican workers be exempted from this tax.

Section 5.—Section 5 prohibits the furnishing of Mexican workers for certain processing activities. It excludes from the definition of the agricultural employment for which workers may be recruited under the act—

> horticultural employment, cotton ginning, compressing, and storing, crushing of oilseeds, and the packing, canning, freezing, drying, or other processing of perishable or seasonal agricultural products.

This would leave covered by the act services or activities within the provisions of section 3(f) of the Fair Labor Standards Act of 1938 or section 3121(g) of the Internal Revenue Code (which by sec. 7852(b) of the Internal Revenue Code was made applicable in lieu of sec. 1426(h) of the Internal Revenue Code (of 1939)). Section 3121(g) includes the raising of horticultural commodities, cotton ginning, and a limited amount of packaging, processing, freezing, and storing for farm operators.

Section 6 extends the program 2 years until December 31, 1963.

W. R. POAGE,
E. C. GATHINGS,
WATKINS M. ABBITT,
PAGE BELCHER,
CHARLES M. TEAGUE,
Managers on the Part of the House.

[H.R. 4317] [22]
ANNUITIES TO WIDOWS AND DEPENDENT CHILDREN OF TAX COURT JUDGES

[House of Representatives Report No. 361, Eighty-seventh Congress, First Session]

[May 8, 1961]

MR. MILLS, from the Committee on Ways and Means, submitted the following report to accompany H.R. 4317.

The Committee on Ways and Means, to whom was referred the bill (H.R. 4317) to amend the Internal Revenue Code of 1954 and incorporate therein provisions for the payment of annuities to widows and certain dependents of the judges of the Tax Court of the United States, having considered the same, report favorably thereon without amendment and recommend that the bill do pass.

I. SUMMARY

H.R. 4317 provides a system of annuities for the surviving widows and dependent children of judges of the Tax Court of the United States. With minor technical modifications, the bill provides for these judges the same survivorship protection as is already available for judges of the other Federal courts. The maximum annuity payable to a widow under the system is 37½ percent of the judge's average salary over a 5-year period, or a maximum of $8,437.50 a year. This is obtained, however, only if the judge had 30 years of allowable service. To be eligible for this protection a judge must have contributed to a special fund 3 percent of his salary for each prior year's service.

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[22] Public Law 87–370, page 344, this Bulletin.

This bill has been reported unanimously by your committee and its enactment is favored by all of the interested Government agencies .

II. GENERAL STATEMENT

In 1953, Congress provided a retirement system for judges of the Tax Court of the United States (Public Law 219, 83d Cong., 1st sess.). That system was incorporated in section 1106 of the Internal Revenue Code of 1939 (now sec. 7447 of the 1954 Code). It was enacted because of the recognition that the civil service retirement system was inadequate and unsatisfactory for Tax Court judges, since the qualifications for appointment in this case require that they be men of maturity and experience prior to entering service. This meant that they would receive an inadequate civil service annuity in the usual case. The retirement system in effect since 1953 provides that a judge may retire after 18 years' service or after reaching the age of 70 if he has at least 10 years' service. Retired pay is the same as active pay if the judge retires after 24 years' service. Retired pay upon retirement with less than 24 years' service is a proportionately lesser amount. Retired judges may be recalled to active service, for which they receive full pay.

In 1956, Congress provided a survivor annuity system for members of the judiciary generally, including judges of the district courts of the territories who serve for a term of years (Public Law 973, 84th Cong., 2d sess.; sec. 376 of title 28, U.S.C.). That system includes judges of the courts of appeal, the district courts, the Court of Claims, the Court of Customs and Patent Appeals, the Customs Court, and the Court of Military Appeals. A special system covers the Supreme Court. Of all the Federal courts the Tax Court of the United States alone remains without an adequate system of survivorship protection.

Judges of the Tax Court today must depend upon the civil service retirement system for survivorship protection. As in the case of retirement protection, this system is inadequate to the needs of the judges. The survivor benefits of the civil service system are keyed to career employees who have served as such for most of their working lives. Judges, on the other hand, typically are not appointed to the bench until a relatively late point in their professional careers. Thus, generally, they are unable to build up an adequate level of survivorship benefits under the civil service system. Not only is the present absence of an adequate survivorship system a hardship insofar as the judges now on the court are concerned but it also imposes a serious problem in attracting qualified individuals to accept appointment to the court.

Your committee's bill provides for judges of the Tax Court the same survivorship protection as is already in effect for judges of the other Federal courts, with such minor, technical modifications as have proved necessary in view of certain differences in the situation of the Tax Court.

Under the bill, Tax Court judges may within 6 months after taking office (either after appointment or reappointment), or within 6 months after the date of becoming eligible for retirement under section 7447(b) of the 1954 Code, or within 6 months after date of enactment, elect to come under the system. Once such an election has been made, contributions of the judge at the rate of 3 percent of salary will be withheld from his salary and upon his death his widow and surviving dependent children will receive annuities. No provision for annuities is made in the case of dependent parents since there is no comparable provision in the existing judicial survivorship system. The annuity in each case will depend upon the years of public service of the judge. Provision is made for deposits into the Tax Court judges survivors annuity fund by the judge with respect to prior years' service. Such deposits will be based at the rate of 3 percent of the salary received in such prior years, plus interest. In case of failure of a judge to make such deposits with respect to prior service, the bill provides for a reduction in the amount of the annuity.

The annuity payable to a widow of a former Tax Court judge is computed by taking 1¼ percent of his average salary for the last 5 years prior to his death (or prior to his receiving retirement pay) multiplied by his number of years of service as a judge (and certain other service) and up to 15 years of other civilian service in the Government. To this is added three-fourths of 1 percent of his average salary multiplied by other "allowable" service (primarily civilian Government service not allowed above). The maximum annuity payable to a widow under the system is 37½ percent of the judge's average annual salary received during the last 5 years prior to his death, or prior to his receiving retired pay under section 7447(d), whichever first occurs. The present salary of a

Tax Court judge is $22,500 per annum. Thus, assuming in a given case that the average annual salary for the computation of a widow's annuity is $22,500, the maximum widow's annuity will be $8,437.50. In order to attain such a maximum, the judge will have to have had at least 30 years of allowable service as defined in the bill. If such service had been on the Tax Court at the present salary, the total contributions of the judge over the 30-year period at the 3 percent rate would be $20,250, without regard to any interest earned over the period involved.

The bill sets up a Tax Court judges survivors annuity fund into which the deposits of the judges electing coverage shall be made and from which the annuities shall be paid. The bill authorizes the appropriation of funds necessary to carry out its provisions.

III. TECHNICAL EXPLANATION OF THE BILL

The bill adds a new section (sec. 7448) to subchapter C of chapter 76 of the Internal Revenue Code of 1954 (relating to the Tax Court of the United States). References to subsections in the following paragraphs of this report refer to subsections of the proposed new section 7448. References to Public Law 973 are to the act of August 3, 1956, which provided a survivors annuity system for members of the judiciary.

Subsection (a)

Subsection (a) contains definitions of terms used in the section. Paragraphs (2) and (4) of this subsection make it clear that retired judges (whether under recall or not) may participate in the system. The references in the two paragraphs in question to compensation in lieu of retired pay are to pay received while serving on recall. The definitions of "widow" and "dependent child" are the same as in Public Law 973. Paragraph (6) defines a "widow" as a surviving wife who has been married to the judge for at least 2 years immediately before his death or is the mother of issue by the marriage, and who has not remarried. Paragraph (7) defines "dependent child" as an unmarried child under age 18 or incapable of self-support because of physical or mental disability. The definition includes a dependent stepchild or adopted child.

Subsection (b)

This subsection provides that a judge may elect survivorship coverage by filing a written election with the chief judge of the Tax Court within 6 months after the date on which he takes office after appointment or reappointment, or within 6 months after the date upon which he becomes eligible for retirement under section 7447(b), or within 6 months after the enactment of the new section 7448. In the case of the chief judge, his election shall be made in a manner prescribed by the Tax Court subject to the above requirements as to the time of filing. The provision that a judge may make an election within 6 months after becoming eligible for retirement under section 7447(b) has no counterpart in Public Law 973. However, it is necessary with respect to judges of the Tax Court because a judge of the Tax Court does not become eligible for retirement under section 7447 until he has served at least 18 years or, if 70 years of age, has served 10 years. Until such time, a judge of the Tax Court has no retirement protection unless he continues to contribute to the civil service retirement system. Since the bill provides that a judge electing its benefits must at the same time waive all civil service benefits, it would be unfair to require such an election prior to the time when the individual judge's retirement privileges under section 7447 have matured.

Subsection (c)

This subsection provides for a deduction of 3 percent from the salary of each judge electing to come under the section, including salary paid subsequent to retirement. The amounts so deducted are to be paid into a fund in the Treasury to be known as the "Tax Court judges survivors annuity fund." This subsection is identical to the comparable provision of Public Law 973 except for the name of the fund.

Subsection (d)

This subsection provides that a judge electing the benefits of the section shall deposit, with interest, to the credit of the fund, a sum equal to 3 percent of his salary received for past service as a judge, Senator, Representative, Delegate or Resident Commissioner in Congress and for any other civilian service of the

Government. The subsection provides that such past service deposits may be made in installments. The subsection also provides that, notwithstanding the failure of a judge to make such deposit, credit shall be allowed for the past service in computing his survivor annuity but that such annuity is to be reduced by an amount equal to 10 percent of the amount of the deposit which was not made, unless the widow elects to eliminate that service entirely from credit under subsection (n). The subsection provides that no deposit need be made for honorable service in the Armed Forces. As set forth above, the subsection is identical with the comparable provision of Public Law 973. In addition, the bill provides that no deposit shall be required for past service with respect to which deductions were actually made under the Civil Service Retirement Act. No comparable provision is contained in Public Law 973. However, the civil service retirement system was for many years the only retirement system available to judges of the Tax Court and, until enactment of this section, has been the only system affording them survivorship protection. As a result, a number of the judges of the Tax Court have been making substantial contributions at the regular 6½ percent rate to the civil service retirement system for many years. In order to elect the benefits of the system provided by this section, such judges must waive their rights to any benefits under the civil service system. It is not practical to provide for a transfer of amounts previously contributed by judges to the civil service fund from that fund to the new fund created by this section. Therefore, if it were not for the special provision referred to, a judge would be required to contribute again with respect to the same service. No similar problem was involved in connection with Public Law 973 because members of the judiciary generally were not afforded coverage under the civil service retirement system.

Subsection (e)

This subsection provides that the Secretary of the Treasury is to invest the Tax Court judges survivors annuity fund in interest-bearing Government securities. The subsection is identical to the comparable provision of Public Law 973.

Subsection (f)

This subsection provides that an individual account is to be kept for each judge of his contributions to the survivors annuity fund. The subsection is identical to the comparable provision of Public Law 973.

Subsection (g)

This subsection provides for the termination of all rights of a judge in the benefits provided by the section in cases where the judge's service terminates other than under section 7447, or section 1106 of the 1939 Code. In such a case, the judge will receive back the contributions which he has paid in, with interest. The last sentence of the subsection provides that if the service terminates because of nonreappointment but the judge is eligible for and elects retired pay at that time, his rights do not terminate and he remains under the system. The subsection differs from the comparable provision of Public Law 973 only as required by the special characteristics of the Tax Court retirement system.

Subsection (h)

This Subsection provides that, in case any judge electing the benefits of this section dies as a judge after rendering at least 5 years of civilian service as computed under subsection (n), for the last 5 years of which deposits or salary deductions have been made or the salary deductions required by the Civil Service Retirement Act actually have been made, annuities shall be paid to the survivors as follows:

(1) If survived by a widow but no dependent children, the widow shall receive an annuity deferred until after she reaches age 50 unless she has already reached that age;

(2) If survived by a widow and dependent children, the widow shall receive an immediate annuity and each dependent child shall also receive an annuity equal to one-half of the annuity of the widow but not more than $900 per year divided by the number of children or $360 per year, whichever is lesser.

(3) If survived by dependent children but no widow, each child shall receive an annuity equal to the widow's annuity (if she had survived) but not more than $480 per year.

The annuity amounts are computed as provided in subsequent subsections.

The subsection provides further that a widow's annuity shall terminate upon her death or remarriage. The annuity of a dependent child terminates upon the the child reaching age 18 unless the child is incapable of self-support by reason of mental or physical disability. In every case, a dependent child's annuity terminates at the child's death or marriage.

The subsection is identical to the comparable provision of Public Law 973.

Subsection (i)

This subsection provides that questions of dependency and disability arising under the section are to be determined by the chief judge subject to review only by the Tax Court, the decision of which shall be final and conclusive. Under Public Law 973, such questions are determined by the Director of the Administrative Office of the U.S. Courts subject to review by the Judicial Conference.

Subsection (j)

This subsection provides that, if a judge who has elected to come under this section dies in office (whether in regular active service or retired from such service under sec. 7447) before he has rendered 5 years of covered civilian service or after having rendered 5 years of such civilian service but has no survivor or survivors entitled to the benefits provided by the section or the right of all persons entitled to an annuity based upon his service has terminated before a valid claim therefor has been established, the total amount credited to the individual account of the judge in the survivors annuity fund, with interest to the date of death, shall be paid to the person or persons surviving in the following order of precedence:

(1) To the person designated by the judge in writing,
(2) If none, to his widow (regardless of how long married),
(3) If none, to his children and descendants,
(4) If none, to his parents,
(5) If none, to his executor or administrator, and
(6) If none, to his next of kin.

Determination as to the persons entitled as set out above shall be made by the chief judge.

In cases where the annuities of all persons entitled to an annuity upon the service of a judge terminate before the aggregate amount of the annuity paid equals the total amount credited to the individual account of such judge, the subsection also provides that the remaining balance, with interest to the date of death of the judge, shall be paid in the order of precedence set out above.

The subsection also provides that any accrued annuity remaining unpaid upon the termination (other than death) of the annuity of any person based upon the service of a judge shall be paid to such person. Any accrued annuity remaining unpaid upon the death of any person receiving an annuity based upon the service of a judge shall be paid in the following order of precedence:

(1) To the executor or administrator of the estate of such person;
(2) If there is no such executor or administrator, payment may be made to such individual or individuals as may appear in the sole judgment of the chief judge to be legally entitled thereto and such payment shall be bar to recovery by any other person.

This subsection is identical to the comparable provisions of Public Law 973, except for the necessary reference to section 7447.

Subsection (k)

This subsection provides that payments to minors or persons mentally incompetent or under other legal disability shall be paid to the guardian or other person legally vested with the claimant's care. The subsection provides that where no such guardian or other fiduciary has been appointed, the chief judge shall determine the person who is otherwise legally vested with the care of the claimant or his estate. With the exception of the reference to the chief judge, the subsection is identical with the comparable provision of Public Law 973.

Subsection (l)

This subsection provides that annuities are to be payable monthly and are not to be assignable or subject to attachment or other legal process. The subsection is identical to the comparable provision of Public Law 973.

Subsection (m)

This subsection provides for the computation of the annuities provided by the section. The annuity of a widow is based upon the judge's average annual salary for judicial and other allowable service during the last 5 years of such service prior to the judge's death or prior to his receiving retired pay under section 7447(d), whichever first occurs. Under Public Law 973, the average is of the service during the last 5 years prior to the judge's death only. However, under the Tax Court retirement system, a judge with less than 24 years' service cannot retire at full pay, a limitation not applicable to the judiciary generally. The change provided by your committee's bill will mean, for example, that in the case of a judge who serves on the Tax Court for 18 years at $22,500 per annum and then retires at 18/24 of that salary, the annuity for his survivor will be based upon an average salary of $22,500 rather than upon the lesser amount received subsequent to retirement. The annuity is to be the sum of the following:

(1) One and one-fourth percent of the average salary, as set out above, multiplied by the years of allowable service as a judge, or as a Senator, Representative, Delegate, or Resident Commissioner in Congress, as a member of the Armed Forces, and his years, not exceeding 15, of other civilian service within the meaning of section 3 of the Civil Service Retirement Act; and

(2) Three-fourths of 1 percent of the average salary, as set out above multiplied by the years of any other prior allowable service.

The annuity so computed and reduced in accordance with subdivision (d), if applicable, is not to exceed 37½ percent of the average annual salary.

The subsection is identical to the provisions of Public Law 973 except in two respects (other than the change referred to above with respect to the computation of average annual salary). Under Public Law 973, service as an employee of the legislative branch was entitled to the higher 1¼ percent credit factor while all other service (other than those specified such as a Member of Congress), is credited at the lower rate of three-fourths of 1 percent. The subsection removes this difference in treatment as between employment for the legislative branch and employment for the other branches of the Government. The subsection also differs from the comparable provision of Public Law 973 with respect to the computation of the maximum annuity payable under the section. Under Public Law 973, the maximum is determined by computing 37½ percent of the average annual salary and *then* reducing that amount because of any failure to make deposits for prior years. Under that provision, assuming that a judge had even 1 year of prior allowable service for which a deposit had not been made, he could never build up the maximum allowable annuity even though he contributed to the system for an infinite number of years. The modification contained in this subsection of the bill provides that the annuity, *after* reduction with respect to prior years for which a deposit is not made, shall not exceed 37½ percent of the average annual salary.

Subsection (n)

This subsection, subject to the provisions of subsection (d), establishes the years of service which are allowable as the basis for calculating the annuity. These years include years of service as a member of the U.S. Board of Tax Appeals and as a judge of the Tax Court, years of service as a Senator, Representative, Delegate, or Resident Commissioner in Congress, years of active service as a member of the Armed Forces not exceeding 5 years in the aggregate and not including any such service for which credit is allowed for the purposes of retirement or retired pay under any other provision of law, and years of any other civilian service within the meaning of section (3) of the Civil Service Retirement Act. This subsection is identical to the comparable provision of Public Law 973 except for the necessary references to the Tax Court and the U.S. Board of Tax Appeals.

Subsection (o)

This subsection provides that a widow may receive an annuity under this section and an annuity to which she is entitled under any other account but the same service shall not be used in computing both annuities.

Subsection (p)

This subsection provides that the chief judge shall submit to the Bureau of the Budget annual estimates of expenditures and appropriations necessary

for the operation of the survivors annuity fund. It also provides that the chief judge shall cause periodical actuarial examinations to be made of the survivors annuity fund and shall transmit the actuary's findings and recommendations to the Tax Court. Except for the substitution of the chief judge for the Director of the Administrative Office of the U.S. Courts and of the Tax Court for the Judicial Conference, this subsection is identical to the provisions of Public Law 973.

Subsection (q)

This subsection provides that, in the case of a judge who dies within 6 months after the date of enactment after having rendered at least 5 years of civilian service computed as prescribed in subsection (n), but without having made an election as provided in subsection (b), an annuity shall be paid to his widow and surviving dependents as provided by this section. The computation of the annuity in such cases will take into account all service as a judge and other prior allowable service but the reductions for nondeposit shall be made. The subsection is identical with the comparable provision of Public Law 973.

Subsection (r)

This subsection provides that any judge who elects the benefits of this section must, at the time of his election, waive all benefits under the Civil Service Retirement Act. No comparable provision is contained in Public Law 973.

Subsection (s)

This subsection authorizes the appropriation of the funds necessary to carry out the new section 7448.

[H.R. 4317] [23]

ANNUITIES TO WIDOWS AND DEPENDENT CHILDREN OF TAX COURT JUDGES

[Senate Report No. 730, Eighty-seventh Congress, First Session, Calendar No. 706]

[May 8, 1961]

MR. BYRD of Virginia, from the Committee on Finance, submitted the following report together with minority views to accompany H.R. 4317.

The Committee on Finance, to whom was referred the bill (H.R. 4317) to amend the Internal Revenue Code of 1954 and incorporate therein provisions for the payment of annuities to widows and certain dependents of the judges of the Tax Court of the United States, having considered the same, report favorably thereon with amendments and recommend that the bill as amended do pass.

I. EXPLANATION OF COMMITTEE AMENDMENTS

(a) *Amendments pertaining to the House bill.*—Your committee amended the substance of the House-passed bill in two respects to make the benefit computation under this bill, in the case of widows of Tax Court judges, identical with the formula under Public Law 973 of the 84th Congress relating to widows of Federal judges.

The first amendment provides that in computing the annuity for a widow of a Tax Court judge, service in the executive branch of the Government is to be taken into account at a rate of three-fourths of 1 percent just as under Public Law 973. Under the House bill, such service was credited at a higher rate, thereby providing a greater annuity for a widow of a Tax Court judge than for a widow of a Federal judge, even though both judges had identical service records. Because your committee believes that in such cases survivor annuities also should be identical, the House bill has been amended to accomplish this result.

The other amendment relates to the 10-percent reduction of benefits in the case of unpaid prior service deposits. Under your committee's amendment, this 10-percent reduction is to occur after the maximum annuity of 37½ percent of the

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[23] Public Law 87-370, page 344, this Bulletin.

judge's average salary for a 5-year period has been computed, just as under Public Law 973. Under the House bill this reduction applied before the maximum benefit was computed and in some cases this could have resulted in a higher benefit for widows of Tax Court judges than for widows of Federal judges.

(b) *Amendment to section 403(b).*—Section 403(b) of present law provides rules under which organizations described in section 501(c)(3) may purchase annuity contracts for their employees. In general, such a tax-exempt organization may contribute toward the purchase price of an annuity contract for an employee up to an amount equal to 20 percent of the employee's salary and even though the plan may not be a qualified plan under the Internal Revenue Code, contributions thus made by a section 501(c)(3) organization are not required to be included by the employee in his gross income for Federal income tax purposes.

The Internal Revenue Service has recently ruled that because public school systems of State or local governments are not organizations described in section 501(c)(3) they do not meet the statutory tests of section 403(b). Therefore, unless contributions are made under a qualified pension or annuity plan employees of public schools, colleges, and universities must include in their gross income, and pay tax on, amounts contributed by their employer toward the purchase price of their annuity contract.

The committee amendment provides that amounts paid to purchase annuity contracts for employees of a public school system will qualify for the exclusion from gross income in the same manner and to the same extent as amounts used to purchase contracts for employees of private organizations described in section 501(c)(3), including private schools. This amendment will make it unnecessary for public schools or State or local governmental units to file application with the Commissioner for classification as an organization described in section 501(c)(3) in order for it to purchase employee annuities under section 403(b). It did not seem reasonable to the committee to deny employees of a public school system the same benefit which is allowed employees of tax-exempt organizations when the Congress is prohibited under the Constitution from taxing such State activities.

Moreover, it will clarify the present practice under which some public school bodies have been granted the right to purchase annuity contracts for their employees under section 403(b) while others have been denied the same privilege. Thus, even though a public school, college, or university (including a land-grant college or university) is an integral part of a State or local government (and, therefore, not a sec. 501(c)(3) organization), under the amendment it will meet the requirements of section 403(b). A wholly owned State or municipal instrumentality, such as a separately organized school, college, or university, also will qualify.

The committee felt it was not reasonable to take the view that Congress ever intended that State or local governmental units should be required to file application with the Commissioner for classification as a tax-exempt organization when the Federal Government has no power under the Constitution to tax the State or local government in the first place. Since your committee viewed this amendment as a clarification of the law, it is made applicable to taxable years beginning after December 31, 1957, the same effective date as section 403(b).

(c) *Accident and health insurance contract premiums.*—Under present law life insurance companies are entitled to a special deduction of 2 percent of premiums attributable to group and accident and health contracts and group life insurance contracts for purposes of the phase 2 tax on underwriting income. The committee has modified present law to provide that individual accident and health contracts written by life insurance companies also will qualify for the special 2 percent deduction unless they are of the nonparticipating type and are issued or renewed for periods of 5 years or more, in which case present law already allows a deduction of 10 percent of the increase in reserves from nonparticipating contracts or, if greater, 3 percent of premiums attributable to nonparticipating contracts (other than group).

This amendment will be of special benefit to smaller life insurance companies which generally do not write substantial group accident and health contracts but which are active in the individual accident and health insurance market, where risks frequently are greater.

Your committee has also extended this special 2 percent deduction in computing underwriting income to casualty insurance companies writing accident

and health contracts. This amendment will eliminate whatever advantages the special deduction has given life insurance companies in selling this type of policy in competition with casualty companies. This amendment does not apply to mutual casualty insurance companies since under present law they are not taxable on their underwriting income and your committee does not believe their investment income should be reduced by a deduction clearly associated with their underwriting accounts.

This amendment will apply to taxable years beginning after December 31, 1960.

II. SUMMARY OF HOUSE BILL

H.R. 4317 provides a system of annuities for the surviving widows and dependent children of judges of the Tax Court of the United States. As amended, the bill provides for these judges the same survivorship protection as is already available for judges of the other Federal courts. The maximum annuity payable to a widow under the system is 37½ percent of the judge's average salary over a 5-year period, or a maximum of $8,437.50 a year. This is obtained, however, only if the judge had 30 years of allowable service. To be eligible for this protection a judge must have contributed to a special fund 3 percent of his salary for each prior year's service.

The bill has been reported unanimously by your committee and its enactment is favored by all of the interested Government agencies.

III. GENERAL EXPLANATION OF HOUSE BILL

In 1953, Congress provided a retirement system for judges of the Tax Court of the United States (Public Law 219, 83d Cong., 1st sess.). That system was incorporated in section 1106 of the Internal Revenue Code of 1939 (now sec. 7447 of the 1954 Code). It was enacted because of the recognition that the civil service retirement system was inadequate and unsatisfactory for Tax Court judges, since the qualifications for appointment in this case require that they be men of maturity and experience prior to entering service. This meant that they would receive an inadequate civil service annuity in the usual case. The retirement system in effect since 1953 provides that a judge may retire after 18 years' service or after reaching the age of 70 if he has at least 10 years' service. Retired pay is the same as active pay if the judge retires after 24 years' service. Retired pay upon retirement with less than 24 years' service is a proportionately lesser amount. Retired judges may be recalled to active service, for which they receive full pay.

In 1956, Congress provided a survivor annuity system for members of the judiciary generally, including judges of the district courts of the territories who serve for a term of years (Public Law 973, 84th Cong., 2d sess.; sec. 376 of title 28, U.S.C.). That system includes judges of the courts of appeal, the district courts, the Court of Claims, the Court of Customs and Patent Appeals, the Customs Court, and the Court of Military Appeals. A special system covers the Supreme Court. Of all the Federal courts, the Tax Court of the United States alone remains without an adequate system of survivorship protection.

Judges of the Tax Court today must depend upon the civil service retirement system for survivorship protection. As in the case of retirement protection, this system is inadequate to the needs of the judges. The survivor benefits of the civil service system are keyed to career employees who have served as such for most of their working lives. Judges, on the other hand, typically are not appointed to the bench until a relatively late point in their professional careers. Thus, generally, they are unable to build up an adequate level of survivorship benefits under the civil service system. Not only is the present absence of an adequate survivorship system a hardship insofar as the judges now on the court are concerned, but it also imposes a serious problem in attracting qualified individuals to accept appointment to the court.

Your committee's bill provides for judges of the Tax Court the same survivorship protection as is already in effect for judges of the other Federal courts, with such minor, technical modifications as have proved necessary in view of certain differences in the situation of the Tax Court.

Under the bill, Tax Court judges may within 6 months after taking office (either after appointment or reappointment), or within 6 months after the date of becoming eligible for retirement under section 7447(b) of the 1954 Code, or within 6 months after date of enactment, elect to come under the system. Once such an election has been made, contributions of the judge at the rate of 3 per-

cent of salary will be withheld from his salary and upon his death his widow and surviving dependent children will receive annuities. No provision for annuities is made in the case of dependent parents since there is no comparable provision in the existing judicial survivorship system. The annuity in each case will depend upon the years of public service of the judge. Provision is made for deposits into the Tax Court judges survivors annuity fund by the judge with respect to prior years' service. Such deposits will be based at the rate of 3 percent of the salary received in such prior years, plus interest. In case of failure of a judge to make such deposits with respect to prior service, the bill provides for a reduction in the amount of the annuity.

The annuity payable to a widow of a former Tax Court judge is computed by taking 1¼ percent of his average salary for the last 5 years prior to his death (or prior to his receiving retirement pay) multiplied by his number of years of service as a judge (and certain other service) and up to 15 years of service as an employee in the legislative branch of the Government. To this is added three-fourths of 1 percent of his average salary multiplied by other "allowable" service (primarily civilian Government service not allowed above, including service in the executive branch). The maximum annuity payable to a widow under the system is 37½ percent of the judge's average annual salary received during the last 5 years prior to his death, or prior to his receiving retired pay under section 7447(d), whichever first occurs. The present salary of a Tax Court judge is $22,500 per annum. This, assuming in a given case that the average annual salary for the computation of a widow's annuity is $22,500, the maximum widow's annuity will be $8,437.50. In order to attain such a maximum, the judge will have to have had at least 30 years of allowable service as defined in the bill. If such service had been on the Tax Court at the present salary, the total contributions of the judge over the 30-year period at the 3-percent rate would be $20,250, without regard to any interest earned over the period involved.

The bill sets up a Tax Court judges survivors annuity fund into which the deposits of the judges electing coverage shall be made and from which the annuities shall be paid. The bill authorizes the appropriation of funds necessary to carry out its provisions.

IV. TECHNICAL EXPLANATION OF THE BILL

The bill adds a new section (sec. 7448) to subchapter C of chapter 76 of the Internal Revenue Code of 1954 (relating to the Tax Court of the United States). References to subsections in the following paragraphs of this report refer to subsections of the proposed new section 7448. References to Public Law 973 are to the act of August 3, 1956, which provided a survivors annuity system for members of the judiciary.

Subsection (a)

Subsection (a) contains definitions of terms used in the section. Paragraphs (2) and (4) of this subsection make it clear that retired judges (whether under recall or not) may participate in the system. The references in the two paragraphs in question to compensation in lieu of retired pay are to pay received while serving on recall. The definitions of "widow" and "dependent child" are the same as in Public Law 973. Paragraph (6) defines a "widow" as a surviving wife who has been married to the judge for at least 2 years immediately before his death or is the mother of issue by the marriage, and who has not remarried. Paragraph (7) defines "dependent child" as an unmarried child under age 18 or incapable of self-support because of physical or mental disability. The definition includes a dependent stepchild or adopted child.

Subsection (b)

This subsection provides that a judge may elect survivorship coverage by filing a written election with the chief judge of the Tax Court within 6 months after the date on which he takes office after appointment or reappointment, or within 6 months after the date upon which he becomes eligible for retirement under section 7447(b), or within 6 months after the enactment of the new section 7448. In the case of the chief judge, his election shall be made in a manner prescribed by the Tax Court subject to the above requirements as to the time of filing. The provision that a judge may make an election within 6 months after becoming eligible for retirement under section 7447(b) has no counterpart in Public Law 973. However, it is necessary with respect to judges of the Tax Court because a judge of the Tax Court does not become eligible for retirement under

section 7447 until he has served at least 18 years or, if 70 years of age, has served 10 years. Until such time, a judge of the Tax Court has no retirement protection unless he continues to contribute to the civil service retirement system. Since the bill provides that a judge electing its benefits must at the same time waive all civil service benefits, it would be unfair to require such an election prior to the time when the individual judge's retirement privileges under section 7447 have matured.

Subsection (c)

This subsection provides for a deduction of 3 percent from the salary of each judge electing to come under the section, including salary paid subsequent to retirement. The amounts so deducted are to be paid into a fund in the Treasury to be known as the "Tax Court judges survivors annuity fund." This subsection is identical to the comparable provision of Public Law 973 except for the name of the fund.

Subsection (d)

This subsection provides that a judge electing the benefits of the section shall deposit, with interest, to the credit of the fund, a sum equal to 3 percent of his salary received for past service as a judge, Senator, Representative, Delegate or Resident Commissioner in Congress and for any other civilian service of the Government. The subsection provides that such past service deposits may be made in installments. The subsection also provides that, notwithstanding the failure of a judge to make such deposit, credit shall be allowed for the past service in computing his survivor annuity but that such annuity is to be reduced by an amount equal to 10 percent of the amount of the deposit which was not made, unless the widow elects to eliminate that service entirely from credit under subsection (n). The subsection provides that no deposit need be made for honorable service in the Armed Forces. As set forth above, the subsection is identical with the comparable provision of Public Law 973. In addition, the bill provides that no deposit shall be required for past service with respect to which deductions were actually made under the Civil Service Retirement Act. No comparable provision is contained in Public Law 973. However, the civil service retirement system was for many years the only retirement system available to judges of the Tax Court and, until enactment of this section, has been the only system affording them survivorship protection. As a result, a number of the judges of the Tax Court have been making substantial contributions at the regular 6½ percent rate to the civil service retirement system for many years. In order to elect the benefits of the system provided by this section, such judges must waive their rights to any benefits under the civil service system, including their right to refund of their civil service contribution. It is not practical to provide for a transfer of amounts previously contributed by judges to the civil service fund from that fund to the new fund created by this section. Therefore, if it were not for the special provision referred to, a judge would be required to contribute again with respect to the same service. No similar problem was involved in connection with Public Law 973 because members of the judiciary generally were not afforded coverage under the civil service retirement system.

Subsection (e)

This subsection provides that the Secretary of the Treasury is to invest the Tax Court judges survivors annuity fund in interest-bearing Government securities. The subsection is identical to the comparable provision of Public Law 973.

Subsection (f)

This subsection provides that an individual account is to be kept for each judge of his contributions to the survivors annuity fund. The subsection is identical to the comparable provision of Public Law 973.

Subsection (g)

This subsection provides for the termination of all rights of a judge in the benefits provided by the section in cases where the judge's service terminates other than under section 7447, or section 1106 of the 1939 Code. In such a case, the judge will receive back the contributions which he has paid in, with interest. The last sentence of the subsection provides that, if the service terminates because of nonreappointment but the judge is eligible for and elects retired pay at that time, his rights do not terminate and he remains under the system. The subsection differs from the comparable provision of Public Law 973 only as required by the special characteristics of the Tax Court retirement system.

Subsection (h)

This subsection provides that, in case any judge electing the benefits of this section dies as a judge after rendering at least 5 years of civilian service as computed under subsection (n), for the last 5 years of which deposits or salary deductions have been made or the salary deductions required by the Civil Service Retirement Act actually have been made, annuities shall be paid to the survivors as follows:

(1) If survived by a widow but no dependent children, the widow shall receive an annuity deferred until after she reaches age 50 unless she has already reached that age;

(2) If survived by a widow and dependent children, the widow shall receive an immediate annuity and each dependent child shall also receive an annuity equal to one-half of the annuity of the widow but not more than $900 per year divided by the number of children or $360 per year, whichever is lesser.

(3) If survived by dependent children but no widow, each child shall receive an annuity equal to the widow's annuity (if she had survived) but not more than $480 per year.

The annuity amounts are computed as provided in subsequent subsections.

The subsection provides further that a widow's annuity shall terminate upon her death or remarriage. The annuity of a dependent child terminates upon the child reaching age 18 unless the child is incapable of self-support by reason of mental or physical disability. In every case, a dependent child's annuity terminates at the child's death or marriage.

The subsection is identical to the comparable provision of Public Law 973.

Subsection (i)

This subsection provides that questions of dependency and disability arising under the section are to be determined by the chief judge subject to review only by the Tax Court, the decision of which shall be final and conclusive. Under Public Law 973, such questions are determined by the Director of the Administrative Office of the U.S. Courts subject to review by the Judicial Conference.

Subsection (j)

This subsection provides that, if a judge who has elected to come under this section dies in office (whether in regular active service or retired from such service under sec. 7447) before he has rendered 5 years of covered civilian service or after having rendered 5 years of such civilian service but has no survivor or survivors entitled to the benefits provided by the section or the right of all persons entitled to an annuity based upon his service has terminated before a valid claim therefor has been established, the total amount credited to the individual account of the judge in the survivors annuity fund, with interest to the date of death, shall be paid to the person or persons surviving in the following order of precedence:

(1) To the person designated by the judge in writing.
(2) If none, to his widow (regardless of how long married),
(3) If none, to his children and descendants,
(4) If none, to his parents,
(5) If none, to his executor or administrator, and
(6) If none, to his next of kin.

Determination as to the persons entitled as set out above shall be made by the chief judge.

In cases where the annuities of all persons entitled to an annuity upon the service of a judge terminate before the aggregate amount of the annuity paid equals the total amount credited to the individuals account of such judge, the subsection also provides that the remaining balance, with interest to the date of death of the judge, shall be paid in the order of precedence set out above.

The subsection also provides that any accrued annuity remaining unpaid upon the termination (other than death) of the annuity of any person based upon the service of a judge shall be paid to such person. Any accrued annuity remaining unpaid upon the death of any person receiving an annuity based upon the service of a judge shall be paid in the following order of precedence:

(1) To the executor or administrator of the estate of such person;

(2) If there is no such executor or administrator, payment may be made to such individual or individuals as may appear in the sole judgment of the chief judge to be legally entitled thereto and such payment shall be bar to recovery by any other person.

This subsection is identical to the comparable provisions of Public Law 973, except for the necessary reference to section 7447.

Subsection (k)

This subsection provides that payments to minors or persons mentally incompetent or under other legal disability shall be paid to the guardian or other person legally vested with the claimant's care. The subsection provides that where no such guardian or other fiduciary has been appointed, the chief judge shall determine the person who is otherwise legally vested with the care of the claimant or his estate. With the exception of the reference to the chief judge, the subsection is identical with the comparable provision of Public Law 973.

Subsection (l)

This subsection provides that annuities are to be payable monthly and are not to the assignable or subject to attachment or other legal process. The subsection is identical to the comparable provision of Public Law 973.

Subsection (m)

This subsection provides for the computation of the annuities provided by the section. The annuity of a widow is based upon the judge's average annual salary for judicial and other allowable service during the last 5 years of such service prior to the judge's death or prior to his receiving retired pay under section 7447(d), whichever first occurs. Under Public Law 973, the average is of the service during the last 5 years prior to the judge's death only. However, under the Tax Court retirement system, a judge with less than 24 years' service cannot retire at full pay, a limitation not applicable to the judiciary generally. The change provided by your committee's bill will mean, for example, that in the case of a judge who serves on the Tax Court for 18 years at $22,500 per annum and then retires at 18/24 of that salary, the annuity for his survivor will be based upon an average salary of $22,500 rather than upon the lesser amount received subsequent to retirement. The annuity is to be the sum of the following:

(1) One and one-fourth percent of the average salary, as set out above, multiplied by the years of allowable service as a judge, or as a Senator, Representative, Delegate, or Resident Commissioner in Congress, as a member of the Armed Forces, and his years, not exceeding 15, of service as an employee in the legislative branch of the Government; and

(2) Three-fourths of 1 percent of the average salary, as set out above multiplied by the years of any other prior allowable service, including service in the executive branch.

The annuity so computed is not to exceed 37½ percent of the average annual salary and is to be further reduced in accordance with subsection (d), if applicable.

Subsection (n)

This subsection, subject to the provisions of subsection (d), establishes the years of service which are allowable as the basis for calculating the annuity. These years include years of service as a member of the U.S. Board of Tax Appeals and as a judge of the Tax Court, years of service as a Senator, Representative, Delegate, or Resident Commissioner in Congress, years of active service as a member of the Armed Forces not exceeding 5 years in the aggregate and not including any such service for which credit is allowed for the purposes of retirement or retired pay under any other provision of law, and years of any other civilian service within the meaning of section (3) of the Civil Service Retirement Act. This subsection is identical to the comparable provision of Public Law 973 except for the necessary references to the Tax Court and the U.S. Board of Tax Appeals.

Subsection (o)

This subsection provides that a widow may receive an annuity under this section and an annuity to which she is entitled under any other account but the same service shall not be used in computing both annuties.

Subsection (p)

This subsection provides that the chief judge shall submit to the Bureau of the Budget annual estimates of expenditures and appropriations necessary for the operation of the survivors annuity fund. It also provides that the chief judge shall cause periodical actuarial examinations to be made of the survivors

annuity fund and shall transmit the actuary's findings and recommendations to the Tax Court. Except for the substitution of the chief judge for the Director of the Administrative Office of the U.S. Courts and of the Tax Court for the Judicial Conference, this subsection is identical to the provisions of Public Law 973.

Subsection (q)

This subsection provides that, in the case of a judge who dies within 6 months after the date of enactment after having rendered at least 5 years of civilian service computed as prescribed in subsection (n), but without having made an election as provided in subsection (b), an annuity shall be paid to his widow and surviving dependents as provided by this section. The computation of the annuity in such cases will take into account all service as a judge and other prior allowable service but the reductions for nondeposit shall be made. The subsection is identical with the comparable provision of Public Law 973.

Subsection (r)

This subsection provides that any judge who elects the benefits of this section must, at the time of his election, waive all benefits under the Civil Service Retirement Act. No comparable provision is contained in Public Law 973.

Subsection (s)

This subsection authorizes the appropriation of the funds necessary to carry out the new section 7448.

MINORITY VIEWS

The committee has, in our opinion, acted most unwisely in adding the provisions of the bill S. 397 as an amendment to the subject bill.

This amendment provides for the deduction of 2 percent of premiums on individual health and accident insurance by life insurance companies in determining their gain or loss from operations. This would correspond to a similar deduction in the Life Insurance Company Income Tax Act of 1959 for premiums on group health and accident business.

We doubt that there is a valid reason for allowing the 2 percent deduction in the case of group business, but the existence of this favoritism toward life insurance companies, as against other types of enterprises, has been seized upon by certain life insurance company officials as justification for a new, although related, privilege.

The Finance Committee, as it has so often done in the past when presented with an instance of unequal tax treatment, has chosen to equalize through liberalization rather than to pursue the more painstaking path of examining the justification for the bellwether provision.

Justification of an additional favoritism because of the existence of another constitutes the sole argument of the proponents of this bill. Since the special deduction is allowed for group business, and since, it is alleged, there are few essential differences between group and individual business in this field, then the special deduction should also be allowed for individual business. Or, as the leadoff witness for the life insurance companies expressed it, "Without going into any details, this 2-percent deduction would equalize the individual policy as against the group policy." Though this may be a true statement, it is not a valid argument.

Life insurance companies have shown no need for tax relief. This is not sought on the basis of need or relief of undue hardship. As an industry, life insurance companies are among the more lightly taxed.

In a quest for fairness and equity in the tax laws, it seems to us that the Finance Committee should, at least occasionally, consider the removal of a special privilege as a means toward equalization where unequal treatment now exists. The action of the committee in adopting this amendment has resulted only in a recommendation for the creation of two inequities, as against the taxpaying public, where only one existed before. We do not believe this to be a salutary process.

ALBERT GORE.
PAUL H. DOUGLAS.

[H.R. 4317] [24]

ANNUITIES TO WIDOWS AND DEPENDENT CHILDREN OF TAX COURT JUDGES

[Conference Report No. 1199, Eighty-seventh Congress, First Session]

[September 15, 1961]

Mr. MILLS, from the committee of conference, submitted the following Conference Report to accompany H.R. 4317.

The committee of conference on the disagreeing votes of the two Houses on the amendments of the Senate to the bill (H.R. 4317) to amend the Internal Revenue Code of 1954 and incorporate therein provisions for the payment of annuities to widows and certain dependents of the judges of the Tax Court of the United States, having met, after full and free conference, have agreed to recommend and do recommend to their respective Houses as follows:

That the Senate recede from its amendment numbered 4.

That the House recede from its disagreement to the amendments of the Senate numbered 1 and 2, and agree to the same.

Amendment numbered 3:

That the House recede from its disagreement to the amendment of the Senate numbered 3, and agree to the same with an amendment, as follows:

In lieu of the matter proposed to be inserted by the Senate amendment insert the following:

Sec. 3. (a) Section 403 (b) of the Internal Revenue Code of 1954 (relating to taxability of beneficiaries under annuities purchased by section 501(c)(3) organizations) is amended—

(1) by striking out subparagraph (A) of paragraph (1) and inserting in lieu thereof the following:

(A) an annuity contract is purchased—

(i) for an employee by an employer described in section 501(c)(3) which is exempt from tax under section 501(a), or

(ii) for an employee (other than an employee described in clause (i)), who performs services for an educational institution (as defined in section 151(e)(4)), by an employer which is a State, a political subdivision of a State, or an agency or instrumentality of any one or more of the foregoing,;

(2) by striking out "the employer described in section 501(c)(3) and exempt from tax under section 501(a)," in paragraph (3) and inserting in lieu thereof the following: "the employer described in paragraph (1)(A),"; and

(3) by inserting before the period in the heading of such subsection the following: "or Public School".

(b) The amendments made by subsection (a) shall apply with respect to taxable years beginning after December 31, 1957.

And the Senate agree to the same.

That the House recede from its disagreement to the amendment of the Senate to the title of the bill and agree to the same.

W. D. MILLS,
CECIL R. KING,
THOMAS J. O'BRIEN,
N. M. MASON,
JOHN W. BYRNES,
Managers on the Part of the House.

HARRY F. BYRD,
ROBT. S. KERR,
RUSSELL LONG,
JOHN J. WILLIAMS,
FRANK CARLSON,
Managers on the Part of the Senate.

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[24] Public Law 87-370, page 344, this Bulletin.

STATEMENT OF THE MANAGERS ON THE PART OF THE HOUSE

The managers on the part of the House at the conference on the disagreeing votes of the two Houses on the amendments of the Senate to the bill (H.R. 4317) to amend the Internal Revenue Code of 1954 and incorporate therein provisions for the payment of annuities to widows and certain dependents of the judges of the Tax Court of the United States, submit the following statement in explanation of the effect of the action agreed upon by the conferees and recommended in the accompanying conference report:

Amendments Nos. 1 and 2: The bill as passed by the House adds a new section 7448 to the Internal Revenue Code of 1954 providing annuities to widows and dependent children of judges of the Tax Court of the United States. This section is changed by Senate amendments numbered 1 and 2 to conform the benefit computations, in the case of widows and dependent children of Tax Court judges, to the formula provided by Public Law 973 of the 84th Congress relating to widows and dependent children of Federal judges. The House recedes.

Amendment No. 3: Senate amendment numbered 3 adds a new section to the bill relating to the taxability of amounts contributed by an employer which is a public school system for annuity contracts for its employees to provide the same treatment as applies under existing law in the case of annuity contracts purchased for employees by employers described in section 501(c)(3) of the 1954 Code which are exempt from tax under section 501(a) of such code.

The House recedes with an amendment. Under the conference agreement, the amendment (1) is to apply where an annuity contract is purchased for an employee who performs services for an educational institution (as defined in sec. 151(e)(4) of the code) by an employer which is a State, a political subdivision of a State, or an agency or instrumentality of any one or more of the foregoing, and (2) will not affect organizations which may qualify under existing law.

Amendment No. 4: Senate amendment numbered 4 added a new section to the bill relating to the treatment of accident and health insurance contract premiums by insurance companies. Under present law life insurance companies are, subject to certain limitations, entitled to a special deduction of 2 percent of premiums attributable to group and accident and health contracts and group life insurance contracts for purposes of the tax on underwriting income. Senate amendment numbered 4 would extend the special deduction to individual accident and health contracts written by life insurance companies. In addition, the amendment would provide a special 2-percent deduction in computing underwriting income of stock casualty insurance companies writing accident and health contracts. The Senate recedes.

The House recedes to the amendment of the Senate to the title of the bill.

W. D. MILLS,
CECIL R. KING,
THOMAS J. O'BRIEN,
N. M. MASON,
JOHN W. BYRNES,
Managers on the Part of the House.

[H.R. 8876] [25]
IDENTIFYING NUMBERS

[Senate Report No. 1102, Eighty-seventh Congress, First Session, Calendar No. 1083]

[September 21, 1961]

Mr. BYRD of Virginia, from the Committee on Finance, submitted the following report to accompany H.R. 8876.

The Committee on Finance to whom was referred the bill (H.R. 8876) to amend the Internal Revenue Code of 1954 to permit the use of identifying numbers, having considered the same, report favorably thereon without amendment and recommend that the bill do pass.

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[25] Public Law 87-397, page 348, this Bulletin.

I. SUMMARY OF BILL

The bill is designed to improve enforcement and collection of internal revenue taxes by facilitating the expanded use of automatic data processing equipment by the Internal Revenue Service and by enabling the Service to match information returns now filed with tax returns.

This bill provides that persons required to file tax returns may be required to record their account numbers on their tax returns. Similarly, persons filing information returns (such as those relating to dividends or interest) are to request the account numbers of persons with respect to whom information is supplied and include those numbers on the information returns they send to the Internal Revenue Service. Also, the bill requires that persons, with respect to whom the information returns are filed, are to supply their numbers to the person required to file the information returns.

The Internal Revenue Service has indicated that it intends to use social security numbers as the account numbers in order to minimize the number of persons having to be assigned new numbers. Also, to the maximum extent possible, applications for account numbers will be mailed to those who do not presently have such numbers in order to minimize the burden imposed on taxpayers.

The Treasury Department has recommended this bill and it has been reported unanimously by your committee.

II. REASONS FOR THE BILL

The taxpayer account number system provided by this bill is needed both to make possible a greatly expanded use of automatic data processing equipment and also to fully utilize the information documents presently coming into the Internal Revenue Service.

Taxpayer account numbers are basic to a satisfactory identification system for automatic data processing (or ADP) equipment. This has been established by the experience of business concerns such as utilities, insurance companies, and banks which have found account numbers essential in ADP operations.

Through the use of taxpayer account numbers and automatic data processing equipment the Internal Revenue Service hopes to develop a single file which would contain, in one place, information relative to all of the tax transactions involving a taxpayer. Such a file would contain first, the taxpayer's name, address, and account number. Second, it would contain references to other taxpayers with whom he was involved from a tax standpoint (for example, a cross-reference to an account number of the taxpayer's wife if she filed a separate return or a reference to a partnership account number for each member of the partnership). Third, the file would contain details as to income and deductions reported by the taxpayer for the current and prior years, as well as changes made in these items as the result of audits. Fourth, the file would contain information reported by others with respect to the taxpayer, such as withholding tax statements sent in by employers (form W2) and information returns on dividends, interest, etc. (forms 1099 and 1087). Fifth, the account would contain records of estimated and withheld taxes paid by the taxpayer, bills sent to him, payments received from him, balances due, etc.

The recording of this information in a single file for each taxpayer would make it possible for the Internal Revenue Service to reach objectives which can be only partially achieved today. First, this would make it possible to detect cases where the taxpayer failed to file the required returns by checking returns actually filed against his consolidated file. Second, in recording income and deductions in the file, the tax return itself could be mathematically verified and the amount due from the taxpayer, or refundable to him, could be determined as a byproduct. Third, the section of returns for audit examination could be made not only on the basis of the returns themselves, but also on the basis of returns for prior years and for other taxes. Fourth, the Service would be able to verify at high speed the income and credits reported by the employers and payors of dividends and interest with the amounts of such items reported or claimed by the taxpayer. Fifth, it would be possible to consolidate financial transactions with taxpayers even though they may relate to different taxes.

Taxpayer account numbers also are essential for proper identification of taxpayers on information documents. Identification by name and address has

led to an almost endless variety of errors and variations which make it difficult, if not impossible, to match the information documents with the tax returns. This can arise, for example, from varying ways of registering stock. For example, the taxpayer at one time may use his first name and middle initial, the next time his full name, and perhaps the next time give only his first and middle initials. Similarly, the address of the taxpayer may be his home address, a business address, a bank account address, or a stockbroker address. The use of names and addresses as means of identification is complicated still further by the fact that many married persons own stock independently but file joint returns and vice versa. Difficulties such as those touched on only briefly here have really limited the usefulness of the more than 100 million information documents presently received by the Internal Revenue Service. A positive identification in the form of account numbers will do much to remove this difficulty.

In view of the considerations outlined above, your committee has reported this bill providing for the use of account numbers for tax purposes in the same form as it passed the House. In doing so, however, your committee like the Committee on Ways and Means of the House believes the Service should work out a system involving the least possible burden to taxpayers in obtaining such account numbers. For this reason, the present social security numbering system will be used. Between 85 and 90 percent of all individual income tax returns presently filed already show a social security account number. Thus, for these taxpayers, it will not be necessary to obtain new account numbers. For persons not now having account numbers, applications to obtain the information necessary to assign them account numbers can be obtained from the Internal Revenue Service or local post office. Applications will be sent out to those filing declarations in 1962 in the case of those returns which are sent in without account numbers. For others not having such numbers, publicity will be sent out late in 1962 encouraging them to obtain applications for account numbers either from district directors' offices or from local post offices or banks. A further check will be made with respect to those filing regular income tax returns in the spring of 1963.

III. GENERAL EXPLANATION OF THE BILL

As indicated above, the account numbers to be used by the Internal Revenue Service are the presently existing social security numbers. The Service has estimated that about 24 million persons having some connection with the tax system either have never had social security numbers or have forgotten the numbers they once had. About half of this number will have to obtain numbers or request a search for their old numbers. It is estimated that the other half of this 24 million will not need numbers since they represent wives filing joint returns with husbands and either have no independent income amounting to $600 or more. In such cases the account numbers of the husbands will be sufficient.

There are two categories of social security numbers, each number consisting of nine digits. The first category is known as an "account" number and presently is issued to individual employees or self-employed persons. It is planned that account numbers will also be assigned to other individual filers of tax returns and persons receiving income required to be reported on information returns.

The second category of social security numbers is the "identification" number. These numbers presently are issued to employers having employees covered by social security or by withholding, and to businesses filing excise tax returns. The only new category which will have to obtain such numbers are businesses without employees which, nevertheless, distribute income to others.

Duplications will be prevented, where a taxpayer who already has a number mistakenly files for a second number through an automatic screening process already in use under the social security system. Also, in a similar manner, those who know they had numbers, but have forgotten them, can have such numbers searched out for them.

Under present law the Secretary of the Treasury has the specific authority to require the use of account or identification numbers only in the case of social security taxes and withholding taxes on wages (sec. 6011(b)). Moreover, certain sections of the code (for example sec. 6041) limit the identifying information required to be presented to the name and address of the recipient of the income or other payment.

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The first new section added by the bill (sec. 6109) has three basic requirements relative to account or identification numbers.

First, the new section provides that any person required to file a return statement or other document is to include in it such identifying number as may be prescribed. In this connection it is planned that all tax returns and declaration forms will provide that the filer show an account number in the case of individuals, or an identification number in the case of a business. In the case of a joint return, a second taxpayer account number would be required only if the second person has independent income of $600 or more, or is covered by social security or wage withholding or receives income, such as dividends or interest, from a payor who is required to report this payment on an information return. The requirement that account or identification numbers be supplied with respect to these returns (and also related statements and documents) is to apply to periods commencing after December 31, 1961. This means that numbers generally will not be required with respect to tax returns filed in 1962 since these usually relate to liabilities incurred in 1961. However, account or identification numbers will be required with respect to the declarations of estimated tax due on April 15, 1962, since these relate to the 1962 tax year.

The second requirement is that any person with respect to whom a return, statement, or other document is required to be filed by another person is to furnish this other person with such identifying number as may be prescribed. This requires the furnishing of these numbers by the recipients of dividend, interest and certain other payments. The recipient of the payment must supply his account number to the person making the payment.

The third requirement provides that any person required to file a return, statement, or other document with respect to another person is required to request from this other person, and include on his return, statement, or other document the identifying number if obtained. Thus, the employer will be required to include the numbers of employees on all wage withholding tax reports, and those filing information returns with respect to others will be required to include the latters' numbers on the information returns. This includes information on payments of interest and most other forms of income of $600 or more, returns with respect to dividend payments of $10 or more, returns with respect to patronage dividends of $100 or more, returns with respect to payments made by brokers, returns with respect to wage withholding, returns with respect to partnership income, returns with respect to common trust funds, returns with respect to exempt organizations, and certain other types of information returns. In addition, the bill provides that returns with respect to estates and trusts, although in part themselves tax returns, are also for this purpose to be treated as if they were information returns with respect to the beneficiaries of the estate or trust. This is provided so that it will be possible to relate to the estate or trust returns the returns of their beneficiaries which for tax purposes must report income received from the estates or trusts.

A limitation in the new section provides that in filing his tax return a person (except in the case of estates and trusts referred to above) will not be required to report the account numbers of other persons from whom he received income or to report the numbers of persons with respect to whom the taxpayer claims deductions, credits, etc. Thus, for example, it will not be necessary to relate medical expenses to the tax account numbers of the physicians involved nor will there be a requirement that dependents claimed on a return be identified by their number.

This second and third category of requirements, primarily concerned with information returns, will apply only with respect to returns, statements, or other documents relating to periods commencing after December 31, 1962. Thus, recipients of dividends, interest, and other forms of income with respect to which information returns are required will be required to supply their numbers to the banks or dividend disbursers only with respect to payments made by the banks or dividend disbursers in 1963 and subsequent years. This is designed to allow adequate time for the installation of the account number system.

A second new section (sec. 6676) added by the bill provides a penalty of $5 for each failure to supply an identifying number unless the person can show this failure is due to reasonable cause. This penalty will apply where the person required to make a return fails to supply his own number, where a person required to furnish his number to another person fails to do so, and where the person required to include the number of another on an information or other return which he is required to make with respect to this other person fails to

do so. This penalty will not apply, however, where there is reasonable cause for the failure to furnish or include the identifying number. Thus, for example, where A is required to furnish his number to B and fails to do so, B will be unable to include the number on an information return which he may be required to make with respect to A. This would be reasonable cause for such failure and the penalty would not apply to B. However, the penalty may apply to A unless he, too, can show reasonable cause.

IV. TECHNICAL EXPLANATION OF THE BILL

Subsection (a) of the first section of the bill amends subchapter B of chapter 61 of the Internal Revenue Code of 1954 (relating to miscellaneous provisions with respect to information and returns) by renumbering section 6109 as section 6110 and inserting after section 6108 a new section 6109.

Under the new section 6109(a)(1), the Secretary of the Treasury or his delegate is authorized by regulations to require any person who is required by statute or by regulations to make any return, statement, or other document to include therein the identifying number assigned to such person. This new authorization extends to all returns made for the purpose of disclosing the amount of tax for which a taxpayer is liable (regardless of the type of tax involved), and also to all information returns, statements, and other documents. Section 6109(a)(2) authorizes the Secretary of the Treasury or his delegate to prescribe regulations requiring a person with respect to whom a return, statement, or other document is required by statute or by regulations to be made by another person to furnish his identifying number to such other person. Section 6109(a)(3) authorizes the Secretary of the Treasury or his delegate to prescribe regulations requiring any person, who is required by statute or by regulations to make a return, statement, or other document with respect to another person, to request from such other person, and to include in the return, statement, or other document, the identifying number assigned to such other person.

Paragraph (1) of section 6109(b) constitutes a limitation on the authority granted by paragraphs (2) and (3) of section 6109(a). Pursuant to this limitation, and apart from the exception in paragraph (2) of section 6109(b), a return of any person with respect to his liability for tax, or any statement or other document in support of such a return, is not considered for purposes of paragraphs (2) and (3) of section 6109(a) as a return, statement, or other document with respect to another person. The phrase "a return of any person with respect to his liability for tax" is limited to a return made for the purpose of disclosing the amount of tax for which a taxpayer is liable as distinguished from returns made for other purposes. A statement or other document is considered to be in support of a return with respect to a person's liability for tax, for example, when the purpose of such statement or document is to substantiate an item of income or deduction appearing on the return. Thus, a taxpayer who claims personal exemptions for dependents on his income tax return will not have to include numbers identifying such dependents. Section 6109(b)(1) does not apply in respect of a return which is not a return made for the purpose of disclosing the amount of tax for which a taxpayer is liable, or any statement or other document substantiating an item appearing on such a return. Any such return, statement, or other document in which information is required about another person or persons, is considered to be a return, statement, or other document with respect to such other person or persons.

Paragraph (2) of section 6109(b) provides an exception to the limitation contained in section 6109(b)(1). Under this exception a return of an estate or trust with respect to its liability for tax, and any statement or other document in support thereof is, for purposes of paragraphs (2) and (3) of section 6109(a), considered as a return, statement, or other document with respect to each beneficiary of such estate or trust. Thus, each beneficiary's identifying number may be required to be included in any return, statement, or other document filed by the fiduciary of an estate or trust. For purposes of section 6109 the term "beneficiary" includes heirs, devisees, and legatees.

Subsection (b) of the first section of the bill amends subchapter B of chapter 68 of the 1954 code (relating to assessable penalties) by adding at the end thereof a new section 6676. Section 6676(a) imposes a civil penalty of $5 for each failure of a person to comply with any requirement for furnishing or including an identifying number under the circumstances set forth in the subsection unless

it can be shown that the failure was due to reasonable cause. Section 6676(b) specifically provides that the assessment or collection of any penalty imposed under subsection (a) shall not be subject to the deficiency procedures provided by subchapter B of chapter 63 of the code.

Subsection (c) of the first section of the bill contains technical amendments to conform the table of sections for subchapter B of chapter 61 of the code and for subchapter B of chapter 68 of the code to the amendments made by subsections (a) and (b) of the bill.

Subsection (d) of the first section of the bill contains effective date provisions. Paragraph (1) of the new section 6109(a), under which a person may be required to furnish his own number on a return, statement, or other document, is to apply in connection with returns, statements, and other documents relating to periods commencing after December 31, 1961. Paragraphs (2) and (3) of such section 6109(a), which relate to the furnishing of other persons' numbers, are to apply in connection with returns, statements, or other documents relating to periods commencing after December 31, 1962.

PART V

ADMINISTRATIVE AND MISCELLANEOUS MATTERS

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PART V

ADMINISTRATIVE AND MISCELLANEOUS MATTERS

STATEMENT OF ORGANIZATION AND FUNCTIONS[1]

This material supersedes the statement on organization published at 21 F.R. 10418–10432 [C.B. 1957–1, 679], as amended by 22 F.R. 245,[2] 22 F.R. 643,[2] 22 F.R. 1967,[2] 22 F.R. 4873,[2] 22 F.R. 6434,[2] 23 F.R. 3070 [C.B. 1958–2, 663], and 25 F.R. 1698 [C.B. 1960–1, 855].

1112 *Service organization.*—(1) The Internal Revenue Service is a component part of the Treasury Department. The Service is headed by the Commissioner of Internal Revenue who serves under the direction of the Secretary of the Treasury.

(2) The Internal Revenue Service consists of a National Office in Washington, D.C., and a field organization. The latter consists of 9 Internal Revenue regions, each headed by a Regional Commissioner who reports to the Deputy Commissioner, 62 Internal Revenue districts, each headed by a District Director, 4 service centers, each headed by a Director who reports to a Regional Commissioner, and a computer center under the direction of the Automatic Data Processing Division in the National Office. In addition, there are in the field 9 Regional Inspectors and 9 Regional Counsel, who report to the Assistant Commissioner (Inspection) and the Chief Counsel, respectively, in Washington, D.C.

(3) In administering the alcohol and tobacco tax and appellate functions direct from the regional office, the Regional Commissioner maintains and supervises several branch offices. The Alcohol and Tobacco Tax branch offices are headed by Supervisors in Charge who report to the Assistant Regional Commissioner (Alcohol and Tobacco Tax). The Appellate branch officers are headed by Associate Chiefs or Assistant Chiefs, Appellate Division, who report to the Assistant Regional Commissioner (Appellate) who also carries the title of Chief, Appellate Division. The Regional Counsel also maintain and supervise branch offices.

(4) In each Internal Revenue district there are a number of local offices in communities where concentration of work load in audit, collection, or intelligence activities requires the assignment of personnel. There are some 900 local offices.

(5) There are also 4 service centers, which are under the supervision of a designated Regional Commissioner. The service centers perform certain returns processing and revenue accounting functions

[1] 26 F.R. 6372.
[2] Reflected in the Statement of Organization and Functions as published in C.B. 1957–1, 679.

for district offices by use of tabulating and other electronic equipment; match tax information documents; mail blank returns; and perform other miscellaneous services, including payroll operations for the entire Service.

(6) The computer center is responsible for the creation, maintenance, and updating of business and individual tax accounts.

(7) Location of the Internal Revenue regional and district offices is given in Appendix A. The Alcohol and Tobacco Tax branch offices are shown in Appendix B; and the Appellate branch offices in Appendix C.

1113 *National Office.*—

1113.1 *Mission.*—The mission of the National Office is to develop broad nationwide policies and programs for the administration of the internal revenue laws and related statutes, and to direct, guide, coordinate, and control the endeavors of the Internal Revenue Service.

1113.2 *Basic organization.*—The principal offices which form the National Office are: The Office of the Commissioner, the Office of the Assistant Commissioner (Administration); the Office of the Assistant Commissioner (Inspection); the Office of the Assistant Commissioner (Operations); the Office of the Assistant Commissioner (Planning and Research); the Office of the Assistant Commissioner (Technical); the Office of the Chief Counsel; and the Director of Practice.

1113.3 *Office of the Commissioner.*—The Commissioner of Internal Revenue, in conformity with policies and delegations of authority made by the Secretary of the Treasury, establishes the policies and administers the activities of the Internal Revenue Service. The Office of the Commissioner consists of the Commissioner's immediate office, which includes the Deputy Commissioner and the Assistant to the Commissioner; and the Fiscal Management Division.

1113.31 *Deputy Commissioner.*—The Deputy Commissioner assists and acts for the Commissioner in planning, directing, coordinating and controlling the policies and programs and in giving executive leadership to the activities of the Internal Revenue Service. The Deputy Commissioner also supervises the Regional Commissioners of Internal Revenue, and makes allocations of funds and personnel to them.

1113.32 *Assistant to the Commissioner.*—The Assistant to the Commissioner reviews and takes final action for the Commissioner on documents involving technical matters prepared for the Commissioner's signature, including regulations, closing agreements, reports on proposed legislation, rulings, correspondence, authorizations to the Attorney General for initiating suits, compromises and reports to the Joint Committee on Internal Revenue Taxation involving refunds or credits of any income, war profits, excess profits, estate, or gift taxes in excess of $100,000. The Assistant to the Commissioner makes independent studies for the Commissioner.

1113.33 *Fiscal Management Division.*—The Fiscal Management Officer serves as the chief advisor to the Commissioner, the Deputy Commissioner, and the principal assistants on all matters concerning budget and the fiscal management of funds appropriated for the administration of the Internal Revenue Service. He is responsible for the development and coordination of financial management policies and budgetary programs. He develops and assists in the justifi-

cation of the Service's budget; advises on its execution; establishes procedures covering the accounting system for appropriated funds; and directs the budget and fiscal activities carried out at the National Office in connection with his responsibilities. The Division consists of two branches: Accounting Branch and Budget Branch.

1113.331 *Accounting Branch.*—The Accounting Branch develops, prescribes, and installs the Service's financial accounting system to produce timely and accurate data for budgetary and fiscal management purposes. It also collaborates with the Reports Division in developing and administering the financial reporting system.

1113.332 *Budget Branch.*—The Budget Branch develops the Service's budget in conformance with the established overall program policies through consultation and cooperation with the responsible operating officials. It prescribes budget procedures and directs the preparation of budget estimates for the Service; participates in the development of standards for the measurement of work necessary in the justification of estimates or the evaluation of financial plans; prepares requests for the apportionment and reapportionment of appropriations; allots funds in accordance with the approved financial plan and properly authorized revisions thereof; establishes the procedures and records necessary to properly reflect the execution of the budget; and collaborates with the Reports Division in developing and administering a reporting system reflecting the status of the budget and financial plan.

1113.4 *Office of Assistant Commissioner (Administration).*—The Assistant Commissioner (Administration) acts as the principal assistant to the Commissioner and the Deputy Commissioner in planning and coordinating the functions of personnel management; training; procurement and supply of facilities, services and property, printing and distribution; public information; and reports management. He is responsible for the development of Service policies and the establishment of procedures and standards governing those functions. He supervises the activities of the Facilities Management Division, the Personnel Division, the Public Information Division, the Reports Division and the Training Division of the National Office, and is responsible for functional supervision of these activities in the field.

1113.41 *Facilities Management Division.*—Develops, directs, coordinates and evaluates policies and programs for providing essential support activities for the operating divisions' primary programs and carries them out in the National Office. Its programs are designed to increase the effectiveness of the Internal Revenue Service, reduce its operating costs and improve taxpayer relations by tailoring Internal Revenue Service physical facilities and by providing support services to best meet the Service's total needs. These programs include paperwork, space, property and supply management, procurement and contracting, printing and distribution, national emergency planning, safety, and document and physical security. Develops the standards and procedures necessary for effective performance of its functions. Exercises the authority to settle claims arising out of the activities of the Internal Revenue Service under the Federal Tort Claims Act. This Division consists of: Emergency Planning, Office Services, Publications, and Standards and Programs Branches.

1113.411 *Emergency Planning Branch.*—Coordinates and develops the Service's plans and preparations to maintain the continuity of essential functions during a National Emergency and provides direction in drawing up an over-all plan taking into consideration the operating requirements of all activities of the Service. Administers broad programs, policies and plans to insure continuity of Service operations by preventing loss through fire, accident, theft, employee injury and breaches of security of buildings, facilities, equipment, documents and identification. Discharges the responsibilities of the Internal Revenue Service in connection with claims under the Federal Tort Claims Act.

1113.412 *Office Services Branch.*—Within the framework of the Service policies and procedures developed by the Division, plans, organizes, administers and reviews the support services for the National Office. These support services include procurement, contracting, property management, building maintenance, communications, supplies, transportation, travel, equipment and vehicle repairs, mail and messenger services, records administration activities and space assignment and utilization. Maintains liaison with other Government agencies, public utilities, private carriers, and other public and private organizations to coordinate and improve service in these activities.

1113.413 *Publications Branch.*—Develops and coordinates the policies, programs, procedures, and standards for all Internal Revenue Service printing programs and visual presentation services; plans and directs the requirements, production and distribution of all printing; provides for planning and reproduction of all types of visual presentations; develops policies, procedures, and standards for Internal Revenue Service field printing establishments and contract field printing and represents Internal Revenue Service in liaison with printing regulatory agencies in interpreting, coordinating, and administering Government-wide printing and publications policies; and provides the consultative services needed in these areas.

1113.414 *Standards and Programs Branch.*—Plans, develops, promotes, and coordinates specific standards and programs designed to increase the effectiveness of Internal Revenue Service office operations. These programs include: management of paperwork and records documentation—forms management, correspondence management, file systems, methods and equipment, data storage and retrieval, application of micro-photography, and records disposition; space management—space acquisition planning, space utilization, and space maintenance; the communications management program—mail and messenger systems, and electric and electronics systems; supply management program—the procurement, receipt, storage, and issue of material; a property management program—contracting, procurement, property accountability and utilization; and motor vehicle fleet management—acquisition, utilization and maintenance. Determines need for program emphasis and goals, develops the programs and promotes and coordinates their acceptance and implementation with other components of the Service. Standards, techniques, guidelines, and consultative services needed in these areas by the Service are provided by the branch. Collaborates with the Systems Development Division in all matters involving data storage and retrieval

and new systems using electric and electronic equipment, etc. Acts as liaison for Internal Revenue Service with Federal and State Governments and industry in coordinating and implementing Government-wide policies and procedures governing these program activities.

1113.42 *Personnel Division.*—The Personnel Division develops, coordinates, and evaluates the personnel policies and programs of the Service and carries them out in the National Office. The Division is responsible for Service programs for the recruitment, placement, and evaluation of qualifications of employees, position classification and wage administration, and employee relations, benefits, and services, including incentives, performance evaluation and discipline. It develops the standards and procedures necessary for the effective performance of these functions throughout the Service. It also carries out the personnel program for employees of the National Office. The Division consists of the following branches: Employee Relations Branch, Employment Branch, National Office Branch, and Position Classification Branch.

1113.421 *Employee Relations Branch.*—The Employee Relations Branch develops and coordinates policies, programs, procedures, and standards relating to adverse actions, appeals, grievances, employee conduct, discipline, employee incentives, benefits and services, relations with employee groups, leave, retirement, outside employment, social security, group insurance (both life and health benefits), performance evaluation, fitness for duty, health maintenance, and coordination of recreational and fund raising activities. The Branch participates in the evaluation of all Service personnel programs. It processes Incentive Award contributions requiring National Office approval, Gallatin Awards, and section 6(c) retirement cases. The Branch reviews and makes recommendations on disciplinary actions involving field employees, requiring National Office decision.

1113.422 *Employment Branch.*—The Employment Branch develops and coordinates policies, programs, procedures and standards relating to recruitment, selection and placement, qualification standards, in-service placements, promotion plans, career systems and manpower utilization, emergency relocation planning, pay administration, personnel records and hours of duty. The Branch participates in the evaluation of all Service personnel programs. It makes recommendations on employment cases for which authority has not been delegated to the Regions or the National Office Branch.

1113.423 *National Office Branch.*—The National Office Branch develops and executes policies, programs and procedures relating to recruitment, selection, placement, employee relations, position classification, discipline, performance evaluation, promotions, retirement, leave administration, incentive awards, and other aspects of a complete personnel program for National Office and certain field employees. The Branch classifies all National Office and certain field positions with the exception of those requiring Treasury or Civil Service approval.

1113.424 *Position Classification Branch.*—The Position Classification Branch develops and coordinates policies, programs, procedures and standards relating to the evaluation of positions and overall conduct of the position classification program. The Branch participates in the evaluation of all Service personnel programs. It classifies

positions and wage board jobs for which authority has not been delegated to the Regions or the National Office Branch, and adjudicates classification appeals.

1113.43 *Public Information Division.*—Plans, develops and coordinates the Service-wide policies and programs for providing information to the public through the press, radio, television and other informational, educational and professional media, to improve general knowledge and understanding of the Federal tax laws and their administration, for the primary purpose of encouraging and facilitating maximum compliance with the voluntary system of taxation. It counsels and advises the Commissioner and other levels of management where public interest or response is involved in the determination of Service policy and execution of tax programs; evaluates for the Commissioner the attitude of the public toward Revenue Service policy and programs and recommends corrective measures where indicated; conducts continuous studies of the Service's information program to identify and act on problems and opportunities for improvement; maintains liaison with and gives functional guidance to regional and district offices in the public information area; and carries out the public information program at the National Office.

1113.44 *Reports Division.*—The Reports Division, through consultation and cooperation with responsible operating officials, is responsible for the review and coordination of all reports used throughout the Revenue Service. It collaborates with other organizational elements of the Service in determining the type of information most meaningful to management and provides advisory service to operating officials on report content, format, frequency, etc. It develops report forms and procedures for timely and effective collection of data and receives and consolidates information into final report form. It is responsible for integrating and coordinating the analyses of reported data and evaluations of the progress of major programs made by other organizational elements, to provide overall appraisal of the Service's operations in terms of stated objectives, fund utilization, and interrelationships of the programs, for the use of responsible operating officials, the Deputy Commissioner, the Commissioner, and Treasury officials.

1113.441 *Reports Compilation Branch.*—The Reports Compilation Branch receives and consolidates information into final report form. It develops specifications for the compilation of data; maintains production planning and control for the preparation of reports; and maintains reports files, including all reports issued by the National Office. It integrates and coordinates the analysis of reported data and evaluations of the progress of major programs made by other organizational elements to provide overall appraisal of the Service's operations in terms of stated objectives, fund utilization, and interrelationships of the programs for the use of responsible management officials, the Deputy Commissioner, the Commissioner, and Treasury officials.

1113.442 *Reports Management Branch.*—The Reports Management Branch develops, coordinates and follows up on the policies, procedures and standards for a Service-wide reports management program; and provides leadership for an effective program. It examines reports for duplication, overlapping and conformity to standards;

assigns reports management symbols; and maintains a register of reports for the National Office. It provides advisory service to management officials on report content, format, frequency and distribution; and collaborates with other organizational elements of the Service in determining the type of information most meaningful to management. Through consultation and cooperation with responsible management officials, it coordinates the review of all reports used throughout the Service.

1113.443 *Reports Planning Branch.*—The Reports Planning Branch conducts continuing studies of reporting systems and methods to assure, in cooperation with other organizational elements of the Service, that the Service has the most current and efficient reporting system possible. This includes the planning and development of methods, procedures, and instructions and, in cooperation with other organizational elements of the Service, the development and improvement of integrated recurring reports which adequately inform top management of progress toward Service goals and objectives.

1113.45 *Training Division.*—The Training Division develops, evaluates and coordinates training throughout the Internal Revenue Service and formulates and recommends the overall training policies of the Service. The Division is responsible for planning and coordinating all interfunctional training programs, and in cooperation with the separate functions, identifies the need for and administers separate functional programs. It develops and administers the execution of Servicewide programs and evaluates their effectiveness. It is responsible for reviewing and evaluating the effectiveness and economy of training methods and training services in regional and district offices and service centers, and for the preparation of program reports of all training activities. It administers the teaching taxes program and coordinates the efforts of the concerned National Office divisions in their work related to this program. The Division administers a special budget allotment, used for the development of Servicewide programs, for the conduct of centralized courses, and for other training activities best administered centrally, and advises on training cost estimates for all Servicewide programs. The Division carries out the training policies and programs of the Service in the National Office. It consists of the following branches: Management Programs Branch, National Office Training Branch, and Technical Programs Branch.

1113.451 *Management Programs Branch.*—The Management Programs Branch is responsible for the development of training policies and programs for multifunctional application and for the "Teaching Taxes" program and for assuring that these policies and programs are carried out. In close collaboration with interested officials in all functional areas, it determines across-the-board training needs and develops programs in the fields of executive development, supervisory, management and communications training. It is responsible for the development and promulgation of evaluation and instructional techniques for all training programs and provides special assistance in these areas when appropriate. Working with appropriate National Office officials, it is responsible for the development of training plans and programs for meeting Servicewide training needs in nontechnical functional areas and for their implementation.

1113.452 *National Office Training Branch.*—The National Office Training Branch is responsible for carrying out in the National Office

training policies and programs as promulgated and for evaluating and reporting on all such programs. It assists all divisions in identifying training needs, provides training guidance in the preparation of program plans and materials unique to the functional area involved and either provides instructors or instructor training. It prepares and directs the execution of all National Office training agreements with the Civil Service Commission.

1113.453 *Technical Programs Branch.*—The Technical Programs Branch, in cooperation with functional divisions, is responsible for developing training policies and programs relating to the technical aspects of the five operating functions found in the regions and districts and for seeing that the policies and programs are carried out. It assists in the identification of training needs. With the assistance of the appropriate National Office and Regional officials, it is responsible for developing required training plans. After adoption of such plans by appropriate officials, it is responsible for seeing to it that all necessary training material is developed, in accordance with the best educational and psychological principles and practice, and distributed to the regions and districts together with all necessary procedural instructions and guides for the actual conduct of the training by the appropriate line organizations. With the assistance of appropriate personnel from the National Office and the regions, it provides leadership in the evaluation of established programs and for the effectuation of program changes indicated by the evaluations. It administers the correspondence training program and provides centralized grading service. It is also responsible for the development of all Servicewide audiovisual projects and aids used in connection with training. In addition, the Branch prepares and negotiates all Servicewide training agreements with the Civil Service Commission in the functional areas served and directs their execution.

1113.5 *Office of Assistant Commissioner (Inspection).*—The Assistant Commissioner (Inspection) acts as the principal assistant to the Commissioner in planning and carrying out the inspection program of the Internal Revenue Service. This includes the independent review and appraisal of all Internal Revenue Service activities as a basis for protective and constructive service to management, and the carrying out of a program for assisting management to maintain the highest standards of honesty and integrity among its employees. The Assistant Commissioner (Inspection) plans and directs the inspection program at both the national and regional levels. At the National Office level he supervises two divisions: the Internal Audit Division and the Internal Security Division, and at the regional level he supervises the Regional Inspectors.

1113.51 *Internal Audit Division.*—The Internal Audit Division has responsibility for conducting a program providing for an independent review and appraisal of the operations of the Internal Revenue Service. This review provides information on the condition of all the functional activities of the Service at the National, regional and district levels and is sufficient in scope to provide a basis for constructive management action by the Service officials responsible for the activities involved. The Division is also responsible for a systematic verification and analysis of financial transactions and a review and appraisal of the protective measures and controls estab-

lished at all operating levels. The organizational structure for program operations consists of the National Office Internal Audit Division, and the Regional Internal Audit Staffs which are headquartered in the same location as the Regional Inspectors. The Director of the Internal Audit Division under the general supervision of the Assistant Commissioner, Inspection is responsible for the development and execution of the Division's program.

1113.511 *Field Coordination Branch.*—The Field Coordination Branch is responsible for assuring that a uniformly high standard of internal audit performance at the regional level is maintained. Furnishes staff guidance at the top management level to Internal Audit Division personnel assigned to the Regional Inspectors. Carries out a program of review and evaluation of the activities of the Regional Internal Audit Staffs (including on-job visitations). Responsible for evaluating matters reported by the Regional Internal Audit Staffs concerning the Service's operations to determine their significance and that action is initiated to call important matters to the attention of the Commissioner, Assistant Commissioners or other principal officials. Responsible for an evaluation of the adequacy of the action instituted by operating officials at all levels to correct deficiences reported. Consults with top officials in the Offices of the Assistant Commissioners (Operations) and (Administration), the Fiscal Management Officer, and the Office of Chief Counsel on operating problems disclosed by the Internal Audit Division, which suggest a need for a revision in current operating instructions. Maintains liaison with National Office Internal Security Division on security cases pending in the regional offices.

1113.512 *Operations Branch.*—The Operations Branch is responsible for conducting periodic internal audits of National Office activities, including the annual audit of the Office of International Operations. Conducts special surveys and procedural studies as requested by the Treasury Department, the Commissioner or the Deputy Commissioner. Carries out special assignments on particular phases of operations requested by the Assistant Commissioner (Inspection) or the Director. Assists the Treasury Department in the annual audit of the Exchange Stabilization Fund and in the annual review of the Treasury agency inspection programs. Assists the General Accounting Office and the Treasury Department on various phases of audit work, such as inventorying Federal Reserve Notes stored in the vaults at the Bureau of Engraving and Printing. Responsible for conducting audits of regional and district offices as assigned by the Director. Carries out special assignments in cooperation with the Internal Security Division on cases requiring the specialized knowledge and training of personnel of the Internal Audit Division.

1113.513 *Program Development Branch.*—The program Development Branch is responsible for developing all of the division's policy and procedural instructions and guidelines, including specialized programs for staff development. These are necessary to maintain high professional standards of Internal Audit staff performance and to provide the most effective, up-to-date methods for the uniform execution of Internal Audit's Service-wide program. Develops special internal management procedures for the Internal Audit Division to ensure adequate control of its activities and to promote maximum

operational efficiency. Maintains a current knowledge of developments in electronic data processing and its applications to the Service's operations. Participates in the planning and development of the Service's A.D.P. system to evaluate basic controls and to determine their effect on Internal Audit's responsibilities. Develops procedures to utilize automatic data processing in carrying out principal segments of the Internal Audit Division's program. Maintains liaison with all divisions at the National Office level, including the Office of Chief Counsel, in order to determine operating problems or developments that should be given attention in carrying out the Internal Audit Division's program. In coordination with the Training Division, plans, develops and carries out the basic and advanced internal auditing training programs to assure the proper indoctrination of new staff members and the continuing professional growth of all Internal Audit Division personnel.

1113.52 *Internal Security Division.*—The Internal Security Division plans, develops, and controls the internal security program for the Internal Revenue Service so as to assist management in assuring the highest standards of honesty, integrity and security among Service employees and maintain public confidence in the integrity of the Service. The program includes personnel background investigations and investigations of complaints or allegations of misconduct or irregularities, including criminal, concerning Service employees. The program also includes background investigations of certain applicants for enrollment to practice before the Internal Revenue Service, investigations of charges against tax practitioners, formal investigations of accidents involving Service employees or property, investigations of complaints alleging discrimination, in violation of the Government Employment Policy and the maintenance of records and case files relating to investigations conducted. The Division also conducts such special investigations, studies, and inquires as required for the Commissioner, Office of the Secretary, or other components of the Treasury Department. The Division is composed of four branches: Complaint Case Coordination Branch, Investigations Branch, Planning and Programming Branch, and Security Case Coordination Branch.

1113.521 *Complaint Case Coordination Branch.*—The Branch controls and coordinates on a nation-wide basis the Internal Security Division function of investigating alleged violations of Federal criminal statutes and of the regulations and rules governing the conduct of Service personnel; charges against persons enrolled to practice before the Internal Revenue Service, and special investigations as required for the Commissioner and other components of the Treasury Department. The Branch maintains a continuing review and control of individual cases to: (a) Assure that the scope of the investigations and the evidence are sufficient to provide a basis for conclusions by management and/or the Department of Justice; (b) assure that established policies, procedures and techniques are being followed uniformly; (c) to promote uniformity in investigative coverage, form and quality of reports, and administrative and criminal dispositions; (d) develop data for improvement, simplification, and standardization of investigative operations; (e) develop information that will aid management in planning and programming Internal Security activi-

ties. The Branch maintains liaison on criminal matters with the Office of the Chief Counsel, other law enforcement segments of the Service, Federal Bureau of Investigation and other Federal law enforcement agencies.

1113.522 *Investigations Branch.*—The Branch, operating on a nation-wide basis, is responsible for conducting extremely confidential investigations of complaints and allegations of misconduct or irregularities concerning high level officials of the Service and other special investigations which by reason of their complexity or sensitivity, or because of their potential effect on the maintenance of public confidence in the integrity of the Service, demand special handling. The Branch, as the investigative branch of the Internal Security Division for National Office personnel, is responsible for conducting background investigations of applicants for, or incumbents of, positions in the Service, certain applicants for enrollment to practice before the Internal Revenue Service, and for applicants for positions with certain other components of the Treasury Department. In addition the Branch conducts investigations of alleged violations of Federal criminal statutes and rules and regulations governing the conduct of Service personnel; charges against persons enrolled to practice before the Internal Revenue Service; formal investigations under the Federal Tort Claims Act; Government Employment Policy complaint cases, and other special investigations as may be required for the Commissioner and other components of the Treasury Department. The Branch maintains liaison with the Regional Inspectors and Assistant Regional Inspectors (Internal Security) to coordinate joint activities and in special situations to render assistance in the handling of difficult investigations.

1113.523 *Planning and Programming Branch.*—The Branch is responsible for providing staff assistance to the Division Director in planning and programming the Internal Security Division program. This includes formulating policies; developing technical and administrative procedural instructions, including manual issuances and investigative handbook; conducting inspections of the management and operation of the Regional Internal Security Divisions; conducting special surveys of National Office Internal Security activities; developing and coordinating training programs for the Division; providing technical and staff assistance to the Treasury Law Enforcement Officer Training School; directing the maintenance of records and case files relating to investigations by the Division; compiling and analyzing reports of operational costs, workload data, and statistics concerning criminal and administrative actions resulting from Internal Security investigations; evaluating manual issuances or proposals originating outside Inspection which are pertinent to Internal Security functions; conducting special staff studies; and maintaining liaison with other branches of the Internal Security Division, the Internal Audit Division and other offices of the Service.

1113.524 *Security Case Coordination Branch.*—The Branch controls and coordinates on a nation-wide basis the Internal Security Division function of investigating the character and background of applicants for, or incumbents of, positions in the Service. The Branch reviews reports submitted by the National and field offices of the Internal Security Division concerning investigations conducted for

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the Internal Revenue Service, for certain other components of the Treasury Department and for the Director of Practice. These reports cover all character and security cases, all National Agency Check and Inquiry (NACI), and enrollee applicant cases in which unfavorable or questionable information is disclosed, formal investigations under the Federal Tort Claims Act, and Government Employment Policy complaint cases. The purpose of these reviews is to: (a) Assure that the high suitability and security requirements for Government employment and the investigative requirements of the Service have been met; (b) assure that policies and procedures are being followed uniformly; (c) develop factual data for improvement, simplification, and standardization of investigative operations; (d) promote nation-wide uniformity in the approach, operating techniques, and administrative results of character and background investigations; (e) develop information to aid management in planning and programming Internal Security activities. The Branch directs all investigative activities and coordinates administrative activities incidental to the issuance of Top Secret Defense Information Clearance letters to Service personnel and Confidential clearance letters to Service employees when required.

1113.6 *Office of Assistant Commissioner (Operations).*—The Assistant Commissioner (Operations) is the principal assistant to the Commissioner on all matters pertaining to the operations programs of the Service and in providing effective functional supervision of operations activities in the field. These include the collection of taxes, the audit and investigation of returns, criminal fraud investigations, the administrative system of tax appeals, the administration of laws relating to alcohol, alcoholic beverages, tobacco and firearms, and the implementation and operation of the IRS Automatic Data Processing System and for providing data processing services. The Assistant Commissioner (Operations) directs, coordinates and evaluates the work of the Operations Divisions of the National Office (Alcohol and Tobacco Tax, Appellate, Audit, Automatic Data Processing, Collection, and Intelligence) and the Office of International Operations.

1113.61 *Alcohol and Tobacco Tax Division.—Office of the Director.*—Develops and coordinates policies and programs with respect to, and administers and enforces the Internal Revenue laws relating to alcohol, alcoholic beverages, tobacco, and firearms, the Federal Alcohol Administration Act, the Liquor Enforcement Act of 1936, and related laws.

1113.611 *Executive Assistant.*—Provides staff assistance to the Director in the general management of the Alcohol and Tobacco Tax operations and in the formulation of policy and program plans in the areas of organization, personnel, financing planning, funds management, and appraisal of field operations; both on a continuing basis and through specific management studies. Develops and coordinates the Division-wide program for planned systematic visitation to apprise top management, through on-site evaluation, of the effectiveness of field office performance in both the program and management areas. Works with Assistant Regional Commissioners in evaluating program results in the regions. Provides required office management and administrative services for the National Office Division.

1113.62 *National Office Laboratory.*—Responsible for formulating, developing, and carrying out programs for the application of

scientific methods to the solution of problems of the Alcohol and Tobacco Tax and Tax Rulings Divisions of the Internal Revenue Service having impact on the collection of the revenue. Furnishes technical advice and assistance to officials of the Internal Revenue Service in the fields of chemistry and physics. Conducts research to improve and develop analytical techniques and to resolve technical problems by physical or chemical methods. Examines and analyzes samples, formulas and processes of permittees under the jurisdiction of the Alcohol and Tobacco Tax Division to determine taxable status and examines samples for the Bureau of Narcotics. Coordinates the National Office and Regional Laboratory Programs.

1113.613 *Basic Permit and Trade Practice Branch.*—Responsible for formulating, developing, and carrying out programs for the administration and enforcement of the Federal Alcohol Administration Act. Plans and conducts studies of industry trends in marketing which might have an impact on the programs of the Branch. Recommends revision or amendment of regulations and prepares notices of hearings thereon; analyzes and evaluates testimony developed at hearings; and drafts final regulations and such related forms or internal management documents as required. Makes rulings and interpretations of law and regulations for benefit of industry, regional offices, other Federal agencies, State agencies, and embassies of foreign governments. Collaborates with foreign governments in their development of control procedures abroad to supplement domestic controls established with respect to the importation of their products into the U.S. Acts on applications for interlocking directorates and for certificates of (or exemption from) label approval. Determines acceptability of alcoholic beverage advertising in all media and initiates punitive actions for violations of advertising provisions of law and regulatons. Maintains liaison with regional offices to appraise the effectiveness of Branch programs.

1113.614 *Enforcement Branch.*—Responsible for: Formulating and developing policies, programs, procedures, and regulations relating to the investigation, prevention and detection of willful and/or fraudulent violations of the Internal Revenue Liquor and Tobacco Laws, the Liquor Enforcement Act of 1936, the Federal Alcohol Administration Act, and the National and Federal Firearms Acts; control and coordination of the law enforcement activities of the Division with related functions of other Federal Agencies and with those of state authorities; adaptation of investigative techniques and procedures to the varying needs of different regions, to a diversity of state control laws and their fluctuating requirements and to the constantly changing social and economic conditions affecting the enforcement operations of the Division; providing guidance and training to field elements, for effective application of policies and programs; and appraising management of field offices, as it relates to their enforcement function, through a planned on-site evaluation program.

1113.615 *Permissive Branch.*—Responsible for developing the objectives of the Division in the administration of Internal Revenue laws relating to the production, processing, distribution, and use of alcoholic beverages, industrial alcohol, and related products. Devises policies and programs and designs the organizational structure to

achieve these objectives. Plans, develops, and prepares regulations, procedures, and rulings, and provides guidance and training to field elements, for effective application of policies and programs; and appraises management of field offices, as it relates to functional areas other than enforcement, through a planned on-site evaluation program.

1113.616 *Tobacco Tax Branch.*—Responsible for planning, developing, and expressing the program for the administration of the internal revenue laws relating to tobacco materials, tobacco products, and cigarette papers and tubes. Formulates policies, practices, procedures, and regulations relating to the manufacture and taxpayment or tax exempt disposition of tobacco products and cigarette papers and tubes, and to the handling of tobacco materials. Conducts analytical studies of the laws, regulations, policies, practices, and procedures, and appraises field operations, to determine the efficiency and effectiveness of the tobacco tax program. Formulates recommendations for revision of internal revenue laws in the tobacco tax area. Interprets laws and regulations, makes tax determinations, and issues rulings and instructions; prepares internal management documents and forms; analyzes recurring problems and develops solutions; and prepares final decisions in cases where the action of regional offices is protested or appealed.

1113.62 *Appellate Division—Office of the Director.*—Directs and supervises activities of the division which is responsible for planning, programming, guiding, and evaluating Servicewide Appellate operations. These operations consist of holding administrative hearings and deciding the disposition of cases in which the determination of a District Director has been protested or made the subject of a petition for review by the Tax Court. The cases involve income, profits, estate, gift, employment, and excise taxes (other than alcohol, tobacco, narcotics, firearms and wagering), offers in compromise, and refund claims and overassessments including an analysis of large refund cases before review by the Congressional Joint Committee on Internal Revenue Taxation. Supervises centralized operations consisting of the review and recommended approval or disapproval of final closing agreements for past taxable years, the disposition of issues in disputed Excess Profits Tax cases under section 722 of the 1939 Code, the furnishings of expert valuation advice and assistance, and the approval of certain administrative actions which have not been delegated to the field such as the transfer of cases and the reopening of cases previously closed by Form 870–AD or its equivalent.

1113.621 *Coordination and Management Staff.*—Develops and recommends operational policies, plans, programs, and basic procedures relating to the Appellate function. Assists and advises regional Appellate offices on technical and administrative problems to enable them more effectively to accomplish their objectives. Establishes and conducts a field visitation program, and maintains continuous field liaison to assure that established policies, programs, plans, and instructions are carried out in a uniform, effective manner. Performs coordination functions across regional lines and with other Service elements. Supervises task forces working on special projects such as training, position descriptions, office systems, and management improvement. Represents the Director in meetings of National Office and regional officials, and staff members serve on various committees

as designated. Reviews and appraises proposed staffing in field offices and evaluates personnel for the purpose of advising the Director when he is requested to give clearance approval on certain appointments.

1113.622 *Excess Profits Tax Council.*—Considers and holds administrative hearings in disputed Excess Profits Tax cases and issues arising under section 722 of the 1939 Code. Prepares interpretative rulings on section 722 matters. Furnishes assistance and advice to Chief Counsel and Regional Counsel in connection with the preparation and trial of section 722 cases before the Tax Court of the United States.

1113.623 *Operations Analysis Branch.*—Originates statistical analyses and graphic presentations with explanations and interpretations to disclose program status and progress with trends and deviations highlighted. These analyses serve as the basis for program direction and long range program planning for the Appellate activity. Collaborates with the Reports Division in the development, review, and improvement of the nationwide Appellate reporting and recordkeeping systems which provide the Director, his assistants, and staff with statistical information to assist them in evaluating management effectiveness in the regions. Issues instructions for changes and improvements in the systems and coordinates with other organizations on reporting and related matters. Assists in the analysis and evaluation of regional Appellate Division financial planning and budget execution. Plans and conducts a visitation program to keep advised of the adequacy and accuracy of the reporting and recordkeeping systems and assists the regional offices in solving problems involved in preparing and simplifying statistical reports.

1113.624 *Procedure and Closing Agreement Branch.*—Plans, directs, and administers the development, preparation, issuance, and interpretation of instructions necessary to implement policies, plans, programs and procedures relating to the Appellate function. Coordinates all procedural changes with other segments of the Service. Recommends changes in the Code of Federal Regulations for Appellate activities and, when necessary, publication in the FEDERAL REGISTER. Reviews all final closing agreements relating to tax liability for past years or matters in returns already filed, preliminary to acceptance by the Commissioner. Maintains liaison with the Joint Committee Division of the Chief Counsel's office on matters relating to cases requiring submission to the Congressional Joint Committee on Internal Revenue Taxation.

1113.625 *Settlement Analysis Branch.*—Reviews and analyzes reports on closed cases received from regional Appellate Divisions to test the quality of the decision reached, the uniformity of treatment of issues, and the compliance with procedural instructions or the need for clarifying advice. Identifies troublesome technical or administrative areas and recommends solutions to assist regional offices meet their objectives. Makes special studies, such as an analytical review of Session, Reconsideration, Affirmative Issue, and Fraud cases, to assist the Director and his staff in their current programming efforts and long range planning. Analyzes requests for technical advice, and prepares a digest of the reply or of the other technical communications, for dissemination to regional offices when information is of national interest.

Maintains the central files including sensitive case reports, and provides general administrative services for the Division.

1113.626 *Special Services Branch.*—Participates in the development of Service position and procedures in complex valuation matters. Helps to maintain uniformity of treatment of valuation issues throughout the regional Appellate Divisions by reviewing settlements, furnishing advice, and conducting training sessions. Furnishes expert advice and assistance to the National Office, regional Appellate Divisions, and Regional Counsel on difficult valuation problems. Provides expert witnesses to testify at trials involving complex valuation issues. Develops programs and techniques aimed at eliminating, to the greatest extent possible, the need for time consuming trials of valuation issues in the Tax Court or other courts.

1113.63 *Audit Division—Office of the Director.*—Develops, programs, evaluates, coordinates and guides audit enforcement activities (other than in the alcohol, tobacco, narcotics, firearms, and wagering tax areas) in furtherance of promoting and maintaining the most effective methods of audit operations in the National, Regional and District Offices.

1113.631 *Administrative Services Office.*—Performs or furnishes from a central source, varied administrative services relating to the Division as a whole which cannot be performed effectively at the Branch or other operating organizational levels.

1113.632 *Visitation Staff.*—Conducts planned systematic visitation program to field offices for on-site evaluation, guidance and assistance. Prepares objective analyses, reports and recommendations with respect to field operations for management appraisals and decisions.

1113.633 *Analysis Branch.*—Develops, studies, makes analyses and conducts test and research projects that will assist the Division Director in appraising the effectiveness of regional management operations. Also, in collaboration with the Reports Division, reviews existing management reporting and recording systems in the development of new systems or improvement of existing systems.

1113.634 *Management Branch.*—Identifies and drafts recommended basic policies of the Service as they relate to audit enforcement activities. Plans and develops, or assists in planning and developing, audit programs, systems or methods which will best achieve stated policies. Consults and coordinates with all offices engaged in planning projects affecting audit activities.

1113.635 *Operations Branch.*—Performs certain operating functions of the Audit Division considered administratively infeasible to decentralize. These fall in two general areas (1) coordination, review, and performance evaluation with respect to offers in compromise, including planning and programming therefor, and (2) coordination, control, and review of tax cases involving over-assessments (requiring Joint Committee review) and cases involving special features such as restricted interest, recomputations, jeopardy assessment, post review, and trial or settlement by the Department of Justice.

1113.636 *Procedures Branch.*—Develops and implements programs initiated in or through the Management and Analysis Branches. Provides procedural instructions for all phases of Regional and District operations, prepares forms to effect procedural uniformity,

and participates in studies and visits to evaluate existing procedures or effect their change.

1113.637 *Technical Development Branch.*—Establishes and maintains quality standards for the examination of returns through the study and development of audit methods and techniques to ensure that examining officers have the proper guides with which to conduct examinations effectively and efficiently. Determines all technical training needs of audit personnel, recommends appropriate training programs relative thereto, and develops various training courses and materials necessary for training the field office technicians. Maintains close contact with field offices, and consults and cooperates with the Office of the Assistant Commissioner (Administration), in connection with all training matters.

1113.638 *Uniform Audit Branch.*—Establishes and maintains quality standards for district and regional review of completed work; coordinates with the Technical Development Branch in the establishment and maintenance of quality standards for the examination of returns; and coordinates review activities between the districts and regions and with other National Office functions. Represents the Audit Division in matters involving legislation, regulations and rulings, or other technical matters. Handles communications and correspondence from taxpayers, tax practitioners, Members of Congress, and others, involving legal, factual and administrative questions that have arisen in specific cases as a result of the Service's administration of the Internal Revenue laws.

1113.64 *Automatic Data Processing Division—Office of the Director.*—Directs and supervises the activities of the division in the performance of its assigned responsibilities for development of programs, systems, methods and procedures for implementation and operation of the Internal Revenue Service Automatic Data Processing Plan, the accounting for the internal revenue, and the receipt and integrated processing of tax returns and payments. This includes the development of systems integrating manual, mechanical and electronic data processing operations, and the electronic processing of data in conformance with the administrative provisions of the Internal Revenue Code, in order to provide optimum processing service at a minimum cost and with a maximum of voluntary tax payments.

1113.641 *Administrative Office.*—Provides administrative services common to the entire division.

1113.642 *Visitation Staff.*—Responsible for a planned systematic visitation program for on-site evaluation, guidance and assistance; personal follow-up: coordinating and maintaining close liaison with each of the several branches of the division for the purpose of inquiring into specific field activities of special interest to each branch and keeping each fully apprised of conditions and developments in the field.

1113.643 *Analysis Branch.*—Reviews, analyzes, interprets, and evaluates program status and progress for the Division Director, his assistant and staff (including branch chiefs). Supervises and analyzes work planning and control systems. Reviews and evaluates proposed staffing and financial plans and develops recommendations for allocation of funds for field offices. Develops and recommends budgetary estimates. Collaborates with the Reports Division in the

development, review and administration of a field reporting system which provides management reports essential for the evaluation and measurement of activities in field offices. Confers and collaborates with officials of the Internal Revenue Service, the Treasury Department, and other government agencies, and visits field offices in the performance of these functions.

1113.644 *Management Branch.*—Coordinates the establishment of division objectives; develops policies, to achieve these objectives; provides assistance to field elements in the development of objectives and programs designed to effectively carry out policies and programs; and establishes management objectives in such areas as organization, staffing, communications, etc. Assures coordination and correlation of data processing programs and develops guidelines for the development and control of all programs utilizing electronic or electrical equipment. Staff members serve as representatives of the Director on standing and ad hoc committees and coordinate the activities of the division with other elements of the Service.

1113.645 *Operations Branch.*—The Operations Branch is responsible for the mechanical and automatic processing of such data as is required to be processed in the National Office.

1113.646 *Programming Branch.*—Responsible for systems application and programming required to process Internal Revenue data through electrical accounting and electronic data processing machines. This responsibility includes the analysis and design in detail of specifications necessary to perform approved programs by machine in all Service Centers and the Computer Center and the translation of such systems into machine instructions for all Service Centers and the Computer Center. These instructions must contain check points, validity and accuracy tests and required control print-outs. The Programming Branch is responsible for putting machine instructions into a confirmed readiness status by completely testing and debugging the routines by such processes as desk checking, machine testing, and volume and compatability testing and the preparation of detailed machine operating specifications. In addition, the branch is responsible for maintaining all program routines after they have become operational.

1113.647 *Systems Branch.*—Plans, directs and administers the development, preparation, issuance and interpretation of all systems and procedures necessary to implement policies and programs in all phases of district office, regional service center, and computer center accounting and processing activities. Such activities include all the operations performed in the receipt and processing of all tax payments and the receipt and processing of tax returns. Establishes and maintains the procedures manual and operations list for the district offices, the regional service centers, and the computer center to cover all the procedures and operations in the respective offices. Through field visits reviews the operation of existing systems and procedures to determine areas for improvement. Confers and collaborates with officials of the Internal Revenue Service, Department of the Treasury, General Accounting Office, and other governmental agencies in the performance of the above functions.

1113.648 *Computer Center.*—Responsible for the creation, maintenance and updating of business and individual tax accounts. Re-

ceives input data from Service Centers and processes against master file. Produces output data for use in issuing refund checks, bills, or notices; answering inquiries; making delinquency checks; detecting fraudulent refund claims; classifying returns for audit purposes; preparing reports; and other matters concerned with the processing and enforcement activities of the Service. Performs other machine data processing activties as required.

1113.65 *Collection Division—Office of the Director.*—Directs and supervises the activities of the Collection Division in the performance of its assigned responsibilities for collection of delinquent accounts, obtaining delinquent returns, and the processing and review of collection operations centralized in the National Office. This includes the development of collection and enforcement programs and systems for the effective discharge of the nationwide collection enforcement functions and the control and follow-up of such programs by means of analysis and on-site visitation of field activities.

1113.651 *Administrative Office.*—Provides administrative services common to the entire division.

1113.652 *Visitation Staff.*—Responsible for a planned systematic visitation program for on-site evaluation, guidance and assistance; personal follow-up coordinating and maintaining close liaison with each of the several branches of the Division for the purpose of inquiring into specific field activities of special interest to each branch and keeping each fully apprised of conditions and developments in the field.

1113.653 *Analysis Branch.*—Reviews, analyzes, interprets and evaluates program status and progress for the Division Director, his assistant and staff (including branch chiefs). Develops, supervises and analyzes work planning and control systems. Reviews and evaluates proposed staffing and financial plans and develops recommendations for allocation of funds for field offices. Develops and recommends budgetary estimates. Collaborates with the Reports Division in the development, review and administration of a field reporting system which provides management reports essential for the evaluation and measurement of collection enforcement activities in field offices. Confers and collaborates with officials of the Internal Revenue Service, the Treasury Department, and other government agencies, and visits field offices in the performance of these functions.

1113.654 *Management Branch.*—Plans, develops and establishes the immediate and long range objectives of the Collection Enforcement and Compliance Programs; plans the institution or maintenance of an effective and balanced collection Enforcement Program; studies and recommends improved methods for the organization and general management of collection enforcement functions; searches out and develops the most effective methods and techniques for use of enforcement personnel and prepares handbooks and other means of conveying guidance in these matters; identifies training needs, establishes the technical concepts to be presented in programs designed to meet these needs, and evaluates training programs in terms of improvement in operations and soundness of technical concepts; and reviews the effectiveness of Collection Enforcement and Compliance Programs to ascertain that objectives are being met and providing consultative services to National and Field officials regarding these

programs. Confers and collaborates with officials of the Internal Revenue Service and other government agencies relating to these functions. Confers with taxpayers and/or their representatives relating to collection matters.

1113.655 *Operations Branch.*—Reviews and processes all cases requiring approval of the Joint Committee on Internal Revenue Taxation (overassessments of $100,000 or more); adjustments of World War II Excess Profits Tax, adjustments of Post-War Credit; judgments of the District Courts and the Court of Claims; administrative settlements by the Department of Justice; and all interim allowances in respect to overpayments of tax under section 22(d)(6) of the 1939 Code (LIFO). In connection with the above, advises district directors in order that the administrative provisions of the Code relating to assessments, collections, abatements, credits, refunds, and restricted interests will be properly applied in the final settlement of the cases. Performs other functions retained by the National Office, such as: Offsets of claims and debts; redemption of government securities; etc. Administers the publicity provisions of the law and regulations with respect to applications to inspect returns and related documents by Congressional Committees, United States Government offices in Washington, and Governors of the various States or, in the case of returns in the custody of the National Office, by any person, and furnishes copies where appropriate. Certifies all copies of returns and related documents furnished applicants requiring the affixing of the Treasury Department Seal. Maintains master files of donors' card records received from Service field offices and advises such offices concerning prior year's gift information not available in the particular field office. Maintains files and services requests for returns from field and National Office personnel. Conducts correspondence and engages in conferences with taxpayers, other officials of the Service, the Department of Justice, and other governmental agencies regarding the above activities. Also, in connection with these activities, acts in an advisory capacity to other branches of the division in developing policies and procedures.

1113.656 *Systems Branch.*—Develops, maintains, and interprets systems, methods and procedures to effectuate policies and programs in all phases of district enforcement activity relative to collection of delinquent accounts and securing delinquent returns. Initiates new or revised procedures relating to the collection of delinquent accounts through office methods and the enforced collection of delinquent accounts and the securing of delinquent returns through assigned investigation. These activities include: determinations and acceptance of partial payment agreements, analysis of financial statements, locating assets of taxpayer, levy action, filing notices of lien, sale of seized and acquired property, legal action to enforce collection, filing proof of claims in insolvency and decedent estate proceedings, service of summons, writing off of uncollectible accounts, etc. Through field visits, reviews the existing operations and procedures to determine areas for improvement. Recommends procedural changes and ascertains that such proposed improvement assures integrated, efficient, and economical operations. Assists district offices in the installation of approved systems and procedures. Confers and collaborates with officials of the Internal Revenue Service and other government agen-

cies on procedures relating to these functions. Confers with taxpayers and/or their representatives relating to collection matters.

1113.66 *Intelligence Division—Office of the Director.*—Directs and supervises activities of the Intelligence Division and assists the Assistant Commissioner (Operations) in planning and coordinating the Intelligence program and activities in the field. Responsible for developing and assuring effective application of policies, programs, and procedures for investigations of alleged tax crimes (other than Alcohol and Tobacco tax crimes) and for other special investigations the Commissioner may direct. Also responsible for maintaining effective technical and advisory liaison with regional and district offices to coordinate Intelligence operations and direct certain investigations.

1113.661 *Administrative Office.*—The Administrative Office is responsible for: performing the office management and administrative services for the Intelligence Division of the National Office, including personnel, budget execution, fiscal management, space and equipment requirements, records retention and disposal, and travel authorizations; maintaining records and case files relating to investigations made by the Intelligence activity; handling the incentive awards program; and processing all mail. Serves as a focal point for Division contacts with the Personnel, Fiscal Management, and Facilities Management Divisions for administrative services.

1113.662 *Visitation Staff.*—The Visitation Staff is responsible for: a planned systematic visitation program for onsite evaluation, guidance and assistance; personal follow-up by assigned regions; coordinating with, and maintaining close liaison with each of the several branches of the division for the purpose of inquiring into specific field activities of special interest to each of the branches and keeping each fully apprised of conditions and developments in the field.

1113.663 *Analysis and Evaluation Branch.*—The Analysis and Evaluation Branch is responsible for: Appraising the effectiveness of field Intelligence management and investigative operations through studies, analyses and research projects, including the analysis of operations reports and internal audit reports; analyzing selected cases to determine their adequacy and effectiveness and compliance with prescribed policies, procedures and technical practices for nationwide uniformity including studies and tests at appropriate sites; identifying program, procedural, legislative and investigative technique deficiencies, forecasting trends, analyzing statistical data, preparing cost estimates; analyzing financial plans, reviewing field staffing recommendations and developing Intelligence Division recommendations for allocation of funds for Intelligence activities to field offices; developing work measurement and other statistical standards for use in determining effectiveness of Intelligence operations; planning and developing a reporting program; analyzing technical issuances, legal decisions and procedural releases and articles carried in professional journals, and such other research required to keep the field informed, primarily through the Intelligence Information Digest; making final Intelligence recommendations in cases where disagreements as to disposition exists between Regional Counsel and Assistant Regional Commissioner, Intelligence; and preparing releases and dealing with the Public Information Division regarding closed cases.

1113.664 *Investigative Techniques Branch.*—The Investigative Techniques Branch is responsible for: conducting continuous research and developing improved investigative techniques in the Intelligence operations; preparing investigative handbooks; identifying training needs and developing training programs; participating in the conduct of basic and refresher training in the field and in the National Office including Treasury enforcement training, and originating technical training material, all in collaboration with the Training Division; preparing technical information releases covering advanced techniques valuable in investigative work, including the use of technical devices and equipment, etc.; reviewing and evaluating field Intelligence training materials and courses to see that they correctly reflect the law, regulations, rulings, policies, practices and procedures; maintaining close liaison with the other branches, particularly with Planning and Procedures in developing standards for the selection, classification, and promotion of Intelligence personnel, and with the visitation staff to ascertain the effectiveness of the training program and training requirements and to plan for the development, inculcation and dissemination of new and advanced investigative techniques and other needs as required; and orienting enforcement officials of other Federal agencies and prominent tax officials of State and foreign governments concerning Intelligence techniques, procedures and practices.

1113.665 *Operations Coordination Branch.*—The Operations Coordination Branch is responsible for: coordinating investigative activities in selected current tax and wagering cases crossing regional boundaries or cases of national interest, and exercising direct supervision over special agents investigating cases which because of their sensitiveness or national interest have been brought under National Office control; coordinating with Chief Counsel, Department of Justice and others, actions to be taken in cases under investigation; maintaining liaison with other segments of the Internal Revenue Service, Congressional groups and other Government agencies; maintaining liaison with field investigative activities in specific cases, examining case files and reporting their status and continuing progress to the Commissioner and top Treasury officials; handling correspondence and inquiries from Congressional sources, Federal and State Government agencies, the press and the general public on specific cases; providing requested assistance to field personnel in resolving problems arising in the course of specific investigations; and processing information received from informants (or from other sources) concerning alleged violations of Internal Revenue laws.

1113.666 *Planning and Procedures Branch.*—The Planning and Procedures Branch is responsible for: providing staff assistance to Division Director in the establishment of Intelligence Division objectives, and in formulating, developing and coordinating plans and programs of the Intelligence Division consistent with the overall Service policy to achieve these objectives; consulting and cooperating with all offices engaged in projects of a planning or adminstrative nature affecting Intelligence operations; implementing plans and programs to achieve the basic policies; developing organizational and staffing standards for field Intelligence activities; assisting in developing standards for the selection, classification, and promotion of

Intelligence personnel; providing procedural guides and instructions for all Intelligence phases of Regional and District operations; reviewing field procedural issuances; participating in studies and visits to evaluate existing policies and procedures, recommend their change, and determine whether additional policies and procedures are required; appraising and developing proposed legislation relevant to Intelligence activities; and performing such other duties as the Director may assign.

1113.67 *Office of International Operations.—Director of International Operations.*—Has primary responsibility for the adminstration of the Internal Revenue laws in all areas of the world, outside the United States; and coordinates for the Service all foreign investigations and requests for information from foreign countries or U.S. possessions. Acts as Competent Authority for all operating provisions of tax treaties under delegation from the Commissioner of Internal Revenue.

1113.671 *Executive Assistant to Director.*—Coordinates the work programs and other activities of the foreign and Puerto Rico posts and International Operations personnel and other personnel temporarily assigned overseas on audit examinations, fraud and collateral investigations, or to temporarily assist the foreign representatives and such personnel as may be detailed for overseas assignment from the Audit or Intelligence Divisions. Coordinates audit, collection, delinquency, intelligence, conference and offers in compromise work items between the foreign posts and the Divisions of the Office of International Operations, other Service components and other Government agencies including determining whether action requested is feasible and whether it would be handled by foreign representatives, International Operations personnel on detail, other Government agencies or District personnel. To the extent provided by delegation, supervises and evaluates the work and performance of foreign representatives. Makes certain that foreign representatives have a sound, realistic program (for their territory) that ties into overall Service objectives in the International area. Keeps director informed of trends in the foreign area, which will be employed in program development for the operation as a whole. Takes affirmative steps to maintain morale of personnel located at foreign posts. Exercises broad vision in determining proper utilization of information obtained from foreign representatives. Assists the Director in the performance of the functions of the Competent Authority under tax treaties principally involving non-automatic exchange of information and consideration of double taxation claims. Coordinates the foreign travel of personnel of the Internal Revenue Service. Maintains liaison with the State, Defense, Commerce and Interior Departments, with Customs and the Office of International Finance concerning overseas operating matters. Plans and coordinates the Annual Taxpayer Assistance, Audit and Delinquency Program abroad and plans and coordinates, in conjunction with the military services, the Annual Military Assistance and School Program for overseas military personnel.

1113.672 *Operational Research Staff.*—Accumulates and analyzes data concerning foreign tax laws, U.S. Tax Treaties, U.S. tax law changes, revenue rulings and statements of Service policy. Prepares guidance memoranda for International Operations use. Coordinates

and reviews guidance memoranda prepared in the Office of International Operations. Reviews drafts of proposed tax conventions and regulations thereunder and prepares comments thereon regarding the administrative and operational feasibility of the conventions and regulations; prepares analytical studies of technical problems and tax avoidance schemes in the international area for the purpose of disclosing tax law provisions that are weak, ineffective, inconsistent or unjust; prepares plans and programs to combat tax avoidance and evasion in the international area; prepares legislative and regulatory recommendations for the Office of International Operations; reviews or prepares suggested tax forms and other material for the use of taxpayers under the jurisdiction of the Office of International Operations and coordinates technical matters having reference to proposed legislation and similar matters with the various Divisions of the National Office and other Government agencies. Accumulates or programs for the accumulation of data designed to show such information as extent, nature, location of U.S. taxpayer business and trust interest outside of United States, progress and disposition of cases in this area as well as similar data relative to foreign business entities ostensibly doing business in United States. Develops and/or operates procedure designed to accumulate data on receipt and disposition of information relative to foreign business operations of concern to U.S. which is received from Foreign Post Representatives. All such information shall be in such form that periodic or special requests for reports on the subject can be readily provided. Acts on assignments received by Director from Assistant Commissioner, Operations, or other National Office officials or components, of a program or planning nature.

1113.673 *Administrative Office.*—Performs all necessary administrative management activities, including development of personnel and budget and fiscal programs, cost estimates, quarterly allocations and control of funds, records management, space and equipment utilization. Coordinates and controls, in conjunction with the Facilities Management Division, the printing requirements and distribution of special tax forms required by the Office of International Operations and the distribution of all tax forms to embassies and consulates.

1113.674 *Collection Division.*—Receives all tax returns and related work items accruing from the International Program; processes alien returns, returns of citizens residing abroad, Puerto Rican and Virgin Island returns, returns of certain foreign corporations and the withholding returns filed by agents making income payments to foreign addresses; accepts and deposits remittances received with all such returns; performs all accounting operations incident to the control of these returns, including the issuance of bills, processing of claims, scheduling of refunds, and maintenance of general ledger; administers the provisions of tax treaties authorizing the automatic and other exchange of tax information between the United States and foreign countries; administers Section 6316 of the 1954 Code authorizing, under certain conditions, the acceptance of foreign currencies in payment of United States tax liabilities; collects delinquent accounts of taxpayers residing abroad; develops procedures relating to the collection of delinquent tax from citizens abroad and non-resident aliens; and maintains liaison with the State and Defense Departments

and the Bureau of Accounts concerning Collection matters. Provides advice and guidance on collection where performed by the Foreign Posts and personnel detailed overseas.

1113.6741 *Returns, Receipts and Taxpayer Service Branch.*—Receives, safeguards and deposits all funds tendered to International Operations in Washington, D.C., in payment of Internal Revenue taxes. Receives, controls, examines, processes and has final custody of tax and information returns (except estate and gift) filed with International Operations in Washington, D.C. Receives and opens all ordinary mail addressed to International Operations in Washington, D.C. Stamps, sorts and routes such mail to its proper destination. Receives and answers inquiry letters from withholding agents regarding withholding problems. Receives, examines and transmits all correspondence and documents containing informational exchanges under the tax treaties to and from the various treaty countries, and prepares all statistical reports required for the purpose of evaluating the extent of compliance with treaty provisions and value of the information exchanged. Certifies all amounts withheld at source from income of non-resident aliens and claimed as credits on their final returns. Determines penalties and computes interest on other than individual returns. Mathematically verifies other than individual returns filed with International Operations in Washington, D.C., and completes all prepayment credit adjustments. Provides taxpayer service to U.S. citizens residing abroad and nonresident aliens primarily through correspondence and occasionally through office interviews when the taxpayer is vising Washington, D.C. Provides advice to the Chief of the Collection Division on return, receipts and taxpayer service activities in Puerto Rico.

1113.6742 *Revenue Accounting Branch.*—Performs revenue accounting services on all classes of tax returns filed with the Division in Washington, D.C. Issues statements of tax due, installment notices, and taxpayers' delinquent account assembly forms. Processes all claims for refund or abatement filed, prepares schedules of overassessment, and determines interest allowable thereon. Certifies to taxpayers' payments on Form 899. Examines and allows tentative carryback adjustments and claims within the $10,000 limitation. Compiles statistical reports and records. Maintains controls on blocked refund checks due taxpayers in "Iron Curtain" countries. Verifies mathematically individual tax returns and processes individual tax returns received with remittances. Makes appropriate closing action on all audit adjustment cases. Provides advice to the Chief of the Collection Division on revenue accounting activities conducted in Puerto Rico.

1113.6743 *Delinquent Accounts and Returns Branch.*—Effects collection of delinquent accounts of: Citizens residing or doing business abroad (primarily by correspondence, and through levy on assets in the United States); Aliens residing abroad (primarily by correspondence, and through levy on assets in the United States); Military personnel having APO and FPO addresses (primarily by correspondence and through Payroll Deduction procedures). Obtains delinquent returns of non-resident taxpayers on the basis of Form 14 investigations and conducts delinquency surveys in overseas areas by correspondence. Maintains liaison with the Executive Assistant to

the Director of International Operations to effect collection of TDA's and to obtain delinquent returns through the foreign posts and personnel traveling overseas; the Military Services, concerning delinquent military taxpayers and the serving of levies on overseas military personnel; the State Department, concerning collection of delinquent accounts from citizens residing abroad. Provides advice to the Chief of the Collection Division on delinquent accounts and returns work conducted in Puerto Rico.

1113.6744 *Puerto Rico Collection Branch.*—Is responsible for the performance of all collection work in Puerto Rico and the Virgin Islands which involves primarily the administration of the FICA and Social Security tax laws but also includes collection activities involved in the income and other tax provisions of the Internal Revenue Code as they apply to Puerto Rico and the Virgin Islands. Receives, deposits and conducts appropriate accounting for all tax payments; receives and maintains custody of all tax returns; processes and verifies tax returns and other tax documents; determines interest due and makes appropriate tax refunds; collects delinquent accounts by distraint, seizure, sale, etc., and secures delinquent returns by canvassing and other methods. Sells Alcohol Tax stamps and collects Alcohol and Tobacco Tax taxes in Puerto Rico.

1113.675 *Audit Division.*—Is responsible for the direction of all audit examinations accruing from the International Program conducted by correspondence audit in Washington, D.C., and the examinations conducted by Revenue Agents assigned to Washington, excepting while examining officers are assigned outside the continental limits of the United States during which time they will be subject to the general supervision of the Executive Assistant; provides advice and guidance on audit work performed by the Foreign and Puerto Rico posts. Makes certain that Internal Revenue agents manpower will be applied to the most significant civil enforcement cases in the international area (whether the assignment originates from information received through the Executive Assistant coordinating the Foreign Posts, informant material or classification of returns) and will be responsive to information received from the Executive Assistant in this regard. Is responsible for the maintenance of good relations with the several regions and districts and is responsive to their requirements for assistance in the foreign area. Is responsible for the returns classification, conference coordination and audit service functions. Is responsible for the review of all reports of audit examinations and the preparation of tax determination letters. Directs the conduct of examinations of estate and gift tax returns. Directs programs for the exchange of estate and gift tax data with foreign governments under the tax conventions.

1113.6751 *Review Staff.*—Is responsible for reviewing for technical accuracy and policy and procedure adherence, reports of examination on income, estate and gift, and miscellaneous taxes and offers in compromise. Prepares and issues all preliminary letters and statutory notices. Receives taxpayer protests, refers protests to the Conference Coordinator and closes protested cases to the Appellate Division upon recommendation of the Conference Coordinator. Furnishes technical advice to foreign and Puerto Rico posts and all audit examining personnel, considers special problems relating to specific

cases and prepares recommendations thereon. Considers technical questions submitted by taxpayers, foreign and Puerto Rico posts, other personnel of the Office of International Operations and issues determination letters thereon.

1113.6752 *Conference Coordinator.*—Reviews informal conference notification letters and related materials on required audit cases in which the taxpayer has requested an informal conference. Assigns all informal conference cases to personnel in accordance with established procedures and practices. Conducts conferences in the more difficult cases or in cases in which he may be particularly qualified. Considers cases in which the Review Staff has taken exception to the informal conference decisions of other informal conferees, for the purpose of coordinating with the Chief, Review Staff, on difficult technical issues. Screens all protests filed by taxpayers in response to 30- or 60-day letters for the purpose of deciding whether further action is required by the examining units prior to reference of the case to the Appellate Division for consideration. To the extent time permits, undertakes special assignments received from the Director through the Chief, Audit Division.

1113.6753 *Chief Classifying Officer.*—Is responsible for planning and executing the audit classification program including the selection of returns to be examined and the determination of the organizational units where the returns can best be examined. Is responsible for the planning and execution of procedures involving the classification of other documents used in connection with examinations such as transferred cases from other districts, information reports, etc.

1113.6754. *Service Branch.*—Controls all income, estate and gift, and miscellaneous tax returns received for audit or investigation; routes work to appropriate units; reproduces completed reports; provides typing services for the Audit Division; effects closing action on examined cases; assembles audit production and statistical data and maintains controls on statutory expirations.

1113.6755 *Field Audit Group.*—Conducts audit examinations by examining the books and records of taxpayers in the United States and foreign countries or through correspondence with the taxpayer or his representative on foreign corporations and other foreign business entities and U.S. citizens residing abroad and nonresident aliens with large incomes and complex tax problems. Obtains information on suspected delinquent taxpayers and obtains other tax information while in overseas areas. Upon referral by the Conference Coordinator holds conferences with taxpayers in Washington and foreign areas.

1113.6756 *Estate and Gift Tax Group.*—Conducts examinations by correspondence or field visitation in the United States or overseas when necessary of estate tax returns of U.S. citizens who died while residing abroad or non-resident aliens with substantial property or income in the U.S. and gift tax returns filed by nonresident aliens or U.S. citizens residing abroad. Administers the program for exchange of estate and gift tax data with foreign governments under the tax conventions including the certification of the correctness of the tax determinations and the payment of estate and gift tax liability thereon on returns of Districts involving substantial property or income in foreign tax treaty countries. Initiates correspondence relating to all

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Federal estate and gift tax returns filed by, or due to be filed by, nonresident citizens and aliens. Holds taxpayer conferences and considers protests upon referral by the Conference Coordinator relative to recommended estate and gift tax determinations. Prepares determination letters in reply to correspondence from taxpayers and foreign governments relating to estate and gift tax matters.

1113.6757 *Office Audit Group A.*—Conducts office audit type examinations by correspondence and office interview techniques on (1) tax returns, claims, and offers in compromise filed by nonresident aliens and U.S. citizens residing abroad involving difficult and complex issues; and (2) selected foreign corporations. Holds informal conferences with taxpayers or their representatives in Washington, D.C., upon referral by the Conference Coordinator. Prepares tax returns for, and audits books of, foreign corporations and alien individuals whose property is in custody of the Alien Property Custodian and conducts conferences on these matters.

1113.6758 *Office Audit Group B.*—Conducts office audit type examinations by correspondence and office interview techniques of income tax returns and claims filed by non-resident aliens and U.S. citizens residing abroad. Examines offers in compromise and excise tax claims. Holds informal conferences with taxpayers or their representatives in Washington, D.C., upon referral by the Conference Coordinator.

1113.676 *Intelligence Division.*—Responsible for the conduct of the intelligence function in the Office of International Operations, reviewing and evaluating information items, conducting (subject to general supervision of Executive Assistant while outside continental limits of the United States) fraud investigations and surveys in overseas areas and preparing investigation reports of findings together with recommendation for or against criminal prosecution for tax evasion. Provides advice and guidance to the foreign and Puerto Rico posts and other personnel traveling overseas on intelligence procedures, practices and legal requirements to prove tax evasion. Provides staff service to the Executive Assistant on matters to be referred to Foreign Posts in the Intelligence area and, in this activity, is responsible for maintenance of good working relationships with functional supervisor as well as other Service components. While conducting investigations abroad may perform audit and collection functions in the areas visited. Holds conferences with taxpayers in foreign areas, particularly where no Revenue Service Representatives are stationed, on intelligence matters. Coordinates tax evasion matters with the National Office Intelligence Division, Chief Counsel and other segments of the National Office.

1113.677 *Foreign Posts.*—Pursuant to broad annual programs developed in Headquarters office, initiates such actions in the assigned areas as are necessary to establish and maintain satisfactory levels of voluntary compliance. Develops information indicating possible tax evasion, delinquency or noncompliance and completes action thereon or forwards the information to Washington for further development. Conducts audits of income, estate and gift tax returns of a type justifying field investigation or contact abroad and conducts investigations on tax evasion cases. Effects collection of delinquent taxes when personal contact or investigation abroad is required. Obtains

information on audit, intelligence and collection matters for other service component on collateral requests. Holds taxpayer conferences and effects settlements in cases involving timely and delinquent income, estate and gift tax returns, claims, offers in compromise, etc., particularly in those cases referred abroad by International Operations headquarters for such purposes. Under specific direction, assists the Director in the exercise of the Competent Authority provisions of tax treaties by holding preliminary discussions with the foreign government representatives on the settlement of issues in specific cases involving double or discriminatory taxation and forwards information to Washington, D.C. Maintains close liaison with foreign governments in tax treaty, enforcement, exchange of information, technical and other highly complex matters. Maintains close liaison with U.S. military authorities and taxpayer groups in the area and develops and implements with their assistance comprehensive programs relating to enforcement, taxpayer assistance and school programs, taxpayer-education releases, and similar measures designed to assure a high level of compliance. Is responsible for the development and maintenance of desirable public relations, initiating appropriate taxpayer-education programs in the area. Furnishes technical assistance to taxpayers with regard to both current and delinquent income, estate and gift tax matters.

1113.678 *Puerto Rico Post.*—Audits tax exempt Puerto Rican corporations to uncover diversions of profits from the related interests and associates in the U.S. and submits reports to the Executive Assistant to the Director of International Operations. Conducts all required Internal Revenue Service functions in Venezuela, Colombia, the Guianas and other countries of the Caribbean area on visitation trips from Puerto Rico including holding taxpayer conferences, taking necessary action to assure compliance with the tax laws, maintaining liaison with U.S. military authorities and taxpayer groups in the area and contacting the foreign taxing authorities for the purpose of exchanging information. Obtains information in Puerto Rico and the Virgin Islands on estate and gift tax returns filed or due to be filed in the area to assist the Estate & Gift Tax Group in the determination of estate and gift tax liabilities. Audits employment tax returns of Puerto Rican residents and income tax returns of U.S. Government employees and Puerto Rican residents deriving income from sources outside Puerto Rico. Provides administrative direction to and services for the Puerto Rico Collection Branch.

1113.7 *Office of Assistant Commissioner (Planning and Research).*—The Assistant Commissioner (Planning and Research) acts as the principal assistant to the Commissioner in the coordination of plans and policies, research, statistics, and systems development; and consults with and advises the Commissioner, the Deputy Commissioner, the Assistant Commissioners, and other principal officials regarding the basic policies of the Service. The Assistant Commissioner (Planning and Research) represents the Commissioner on these matters in relations with the Treasury Department, the Congress, other Government agencies and outside organizations. He discharges these primary responsibilities in cooperation with the appropriate Assistant Commissioners (or other principal officials), each

of whom exercises related responsibilities within his own functional area. The Assistant Commissioner (Planning and Research) is responsible for and supervises the activities of four divisions: Plans and Policy Division, Research Division, Statistics Division, and Systems Development Division.

1113.71 *Plans and Policy Division.*—The Plans and Policy Division develops and administers a system integrating the plans of all Service activities into a comprehensive Master Plan and monitors the implementation of the Master Plan. The Division participates in the formulation of the basic policies and organization of the Service; develops and administers systems whereby top management reviews and confirms current Service policies and organization and approves modifications thereto, and administers the internal management document system and reviews issuances for conformance to basic policies of the Service.

1113.72 *Research Division.*—The Research Division conducts advanced research (independently or in conjunction with other offices) into the Federal tax system to develop new approaches to improve the Service's operations and to reduce the compliance burden on the taxpayer; directs such research, within the framework of tax policy determined by the Treasury Department; and furnishes leadership and coordination for the program of Federal-State cooperation in the field of tax administration. The Division actively participates with the appropriate staffs of the Treasury Department and the Assistant Commissioner (Technical) in the preparation of legislative proposals and regulation revisions resulting from the research conducted; designs and carries out surveys, studies, polls, and other forms of research to provide the Service with the basic data needed for the formulation of operating programs and plans; and prescribes the nature and content of statistical analyses made by other offices but required for the research functions of the Division.

1113.73 *Statistics Division.*—The Statistics Division conducts research and prepares statistics with respect to the operation of the income tax laws as required annually by the Internal Revenue Code to provide basic information for tax studies and legislation by the Congress and its committees, for administrative use by the Secretary of the Treasury and the Commissioner of Internal Revenue, and for the Federal benchmark statistical programs on income, wealth, and finance; and performs other related research and statistical functions. The Division consists of the Income, Finance, and Wealth Branch, the Statistical Techniques Branch, and the Operations Branch.

1113.731 *Income, Finance, and Wealth Branch.*—The Income, Finance, and Wealth Branch performs statistical and economic research with respect to the operations of the income tax laws as required by the Internal Revenue Code. It identifies and analyzes actual and prospective needs of users of income, wealth, and financial data reported on tax returns. The Branch plans, evaluates, and modifies these needs to develop an integrated statistical program and prepares specifications for data preparation. It interprets, analyzes, and presents the resulting statistics through publications of the Internal Revenue Service, such as the "Statistics of Income" series, and in consultation with appropriate policy and management officials.

1113.732 *Statistical Techniques Branch.*—The Statistical Techniques Branch conducts research in sampling and other statistical techniques to achieve efficiency in producing the program of the Division. It designs samples and prepares estimates of the tax-return population and workload. It reviews the application of the sampling specifications, conducts variance analyses, and makes other evaluations of the adequacy of the data. It conducts research in the development and adaptation of equipment, techniques, and personnel to the solution of specific problems of the Division. It develops and maintains statistical standards for application to the Division's program.

1113.733 *Operations Branch.*—The Operations Branch develops operational plans for use in producing the statistics required by the program of the Division, and prepares related procedures, forms and instructions. It coordinates the scheduling and processing of the work performed at decentralized locations. It programs for and uses electronic data processing machines as well as other equipment and processes in producing the required tabulations. It evaluates the statistics produced in terms of original specifications, costs, and procedures.

1113.74 *Systems Development Division.*—The Systems Development Division is concerned both with electronic systems and other systems. It conducts a continuing program relative to the availability and capability of electronic data processing systems and other electronic or automation equipment and systems, the feasibility and adaptability of electronic equipment to specific Service tasks, and the development of special modifications for Service purposes. The Division reviews and coordinates projects of other offices involving the adaptation of electronic equipment and participates in the selection and installation of electronic equipment and systems. With respect to other systems, the Division examines and makes recommendations for improvement or extension of internal systems (such as those relating to reporting, processing, accounting, enforcement, records management, and communications), reviews and coordinates system-improvement efforts of other offices, and initiates and develops projects of its own; furnishes other offices of the Service, on request, advisory and consultative services on systems problems; studies possibilities of integrating paperwork and data-handling systems and equipment; and surveys, develops and tests equipment used or usable by the Service.

1113.8 *Office of Assistant Commissioner (Technical).*—The Assistant Commissioner (Technical) acts as the principal assistant to the Commissioner in providing basic principles and rules for the uniform interpretation and application of the tax laws (other than alcohol, tobacco, and certain firearms taxes). His duties include the preparation and issuance of rulings and advisory statements to the public and Revenue officials, the preparation of regulations and other tax guide materials, responsibility for the development and the technical content of all tax return forms and instructions (other than those dealing with Alcohol and Tobacco taxes and the National Firearms Act), the direction of programs for clarification and simplification of tax rules, and the negotiation of tax treaties and agreements with foreign governments. He also is responsible for developing legislative proposals and for the coordination of the Service's legisla-

tive program; for preparing formal reports to the Secretary giving the Service's views on pending or proposed legislation; and for providing technical assistance to the Department, Congressional Committees, and drafting groups in connection with tax legislation. The Assistant Commissioner (Technical) is responsible for and supervises the activities of four divisions: International Tax Relations Division, Special Technical Services Division, Tax Rulings Division, and Technical Planning Division.

1113.81 *International Tax Relations Division.*—The International Tax Relations Division engages in the negotiation of tax treaties and agreements with foreign governments. It cooperates with the State Department and with Congressional committees in procedures leading to the ratification of such treaties and agreements, and conducts programs for treaty administration and relations with foreign tax officials.

1113.82 *Special Technical Services Division.*—The Special Technical Services Division conducts special studies of tax problems aimed at reducing areas of controversy, promoting uniformity, and establishing the position of the Service on technical issues. It prepares tax guides for the public and summaries of technical developments for Service personnel, develops certain tax law materials for employee training purposes and for the high school "Teaching Taxes" program, and reviews tax guide material prepared outside the Service. The Division provides expert technical advice and assistance to all levels of the Service, and to the Department, on the engineering and valuation aspects of tax administration, including legislation, regulations, litigation, taxpayer rulings, formal and informal advice to field and other Service organizations, and related professional and technical activities. It also post reviews a sample of closed field cases involving engineering and valuation issues. It replies to and makes determinations on engineering questions submitted by Service offices and taxpayers which do not involve the establishment of precedents, and makes determinations on requests of taxpayers to change accounting methods for depreciation and obsolescence. The Division is the central point of contact between Technical and Operations on field audit operations involving engineering problems and programs, including training of engineers. The Division conducts a program for the selection and preparation for publication of precedent rulings, decisions, procedures, policy announcements, and other statements in the Internal Revenue Bulletin. The Division prepares and issues replies to communications which relate to general technical information and provides technical research and reference materials and services for National Office personnel. The Division Director is responsible for and supervises the activities of six branches: Technical Reference Branch, Technical Projects Branch, Bulletin Branch, Appraisal Branch, Court Defense Branch and Natural Resources Branch.

1113.821 *Technical Reference Branch.*—The Technical Reference Branch serves as the liaison office for Congressional correspondence within the jurisdiction of the Assistant Commissioner (Technical) and controls the overall correspondence program of that office, except as to those legislative, regulations, and forms matters which are handled by the Technical Planning Division. It issues replies to communications which relate primarily to general technical informa-

tion, and analyzes and directs the flow of all other inquiries and requests for rulings or advice to the appropriate Technical Organization units, or other National Office units. It operates as the principal point of contact between the Public Information Division and the Technical Organization in determining the material to be made available for public inspection under section 6104 of the Code. It provides technical research and reference material and services for National Office personnel; and maintains and services the closed correspondence files and records of the Tax Rulings Division and the Special Technical Services Division.

1113.822 *Technical Projects Branch.*—The Technical Projects Branch has the responsibility for conducting special studies of major technical tax problems, including reappraisals of current rules and practices and the resolution and clarification of complex technical issues, in order to establish the position of the Service, reduce controversy, and promote uniformity. It prepares and issues comprehensive tax guide material for the public (including "Your Federal Income Tax," "Tax Guide for Small Business," "Farmer's Tax Guide," and numerous others). It prepares periodic summaries of technical developments for the guidance of Service personnel (including "Tax Briefs for Revenue Agents and Office Auditors" and the "Annual Technical Review Institute"), and develops certain tax law technical materials for training Service personnel and for the high school "Teaching Taxes" program. It reviews for the National Office such tax guide material prepared outside the Service as it is within the policy of the Service to review; and conducts other similar technical projects.

1113.823 *Bulletin Branch.*—The Bulletin Branch conducts the program for the publication of precedent rulings, decisions, procedures, and other materials in the weekly Internal Revenue Bulletin, the authoritative source for official Service pronouncements. In this program, which provides a means of taxpayer education and information to field offices designed to promote uniform application of an adherence to tax laws and regulations, the Branch selects, analyzes, correlates, and prepares materials for publication; selects Actions on Decisions with respect to which a public expression of the position of the Service is necessary or desirable and prepares appropriate announcements expressing that position; develops standards for the publication of material and takes action to resolve differences regarding publication recommendations; and prepares Bulletin indexes and index-digests for research and reference use throughout the Service.

1113.824 *Appraisal Branch.*—Provides advice and assistance throughout the Service, including Chief Counsel, on engineering and valuation questions arising in the industrial, public utilities, real estate, and commercial fields. This includes preparation of rulings, technical advice memorandums, furnishing advice and assistance in legislation and regulations matters, passing on taxpayer requests to change methods of accounting for depreciation and obsolescence, giving informal advice to field offices on professional and technical engineering problems, post-audit review, on a sample basis, of cases involving engineering issues, and giving direct engineering and valuation assistance, on request, to regional and district offices on open cases involving engineering and valuation issues of considerable im-

portance or complexity, and in the classification of returns involving engineering issues. The Branch also prepares, jointly with the Audit Division, engineering training material, including a Handbook, and prepares and presents material on professional and technical engineering developments at engineering institutes. It also assists the Audit Division in its responsibilities for planning and coordinating the engineering aspects of the audit program, including assistance in the evaluation of field engineering staffing requirements. It prepares material for a periodic engineering coordination digest calling attention to important tax engineering matters.

1113.825 *Court Defense Branch.*—Provides expert advice and assistance to Chief Counsel and Department of Justice in development and preparation of cases involving engineering and valuation issues for trial or pre-trial settlement. Staff members serve as expert witnesses in court or, as necessary, procure expert witnesses in support of Government's position, and assist Government counsel in presentation of cases in Court and in negotiating settlements. The Branch also prepares, jointly with the Audit Division, engineering training material, including a Handbook, and prepares and presents material on professional and technical engineering developments at annual engineering institutes.

1113.826 *Natural Resources Branch.*—Provides advice and assistance throughout the Service, including Chief Counsel, on engineering and valuation questions arising in the oil and gas, mining, and timber and pulp and paper industries. This includes preparation of rulings, technical advice memorandums, furnishing advice and assistance in legislation and regulations matters, passing on taxpayer requests to change methods of accounting for depreciation and obsolescence, giving informal advice to field offices on professional and technical engineering problems, post-audit review, on a sample basis, of cases involving engineering issues, and giving direct engineering and valuation assistance, on request, to regional and district offices on open cases involving engineering and valuation issues of considerable importance or complexity, and in the classification of returns involving engineering issues. The Branch also prepares, jointly with the Audit Division, engineering training material, including a Handbook, and prepares and presents material on professional and technical engineering developments at annual engineering institutes. It also assists the Audit Division in its responsibilities for planning and coordinating the engineering aspects of the audit program, including assistance in the evaluation of field engineering staffing requirements. It prepares material for a periodic engineering coordination digest calling attention to important tax engineering matters.

1113.83 *Tax Rulings Division.*—The Tax Rulings Division prepares and issues rulings, advisory letters, and tax memorandums on income, excess profits, estate, gift, employment and withholding taxes, and excise taxes (other than alcohol, tobacco, and certain firearms taxes) setting forth the position of the Service for the guidance of taxpayers, Revenue employees, and others. The Division Director is responsible for and supervises the activities of eight branches: Corporation Tax Branch, Employment Tax Branch, Estate and Gift Tax Branch, Excise Tax Branch, Exempt Organizations Branch, In-

dividual Income Tax Branch, Pension Trust Branch, and Reorganization and Dividend Branch.

1113.831 *Corporation Tax Branch.*—The Corporation Tax Branch issues rulings with respect to the application of Federal income and profits taxes to corporation matters generally, including those relating to consolidated returns of affiliated groups. It resolves issues applicable to both corporate and noncorporate taxpayers in the field of amortization of emergency and grain storage facilities (sections 168 and 169 of the Code); mitigation of effect of renegotiation of war contracts or disallowance of reimbursement (section 1481); LIFO inventory (section 472); requests for permission for change in accounting periods and methods (except methods of accounting for depreciation or obsolesence, for which see Manual subsection 1113.82); Farmers Cooperatives and tax treatment as to patrons (sections 521–522–61); Involuntary Conversions (sections 1033 and 1071); Taxation of Regulated Investment Companies and their shareholders (sections 851 to 855); and Research and Experimental Expenditures (section 174). The Branch also makes determinations with respect to earnings and profits and the taxable status of distributions.

1113.832 *Employment Tax Branch.*—The Employment Tax Branch issues rulings with respect to the application of the tax imposed by the Federal Insurance Contributions Act, the Railroad Retirement Act, Federal Unemployment Tax Act, and the withholding provisions of the Federal income tax, all of which are included in Chapters 21–25, inclusive, of the Code. This Branch also has jurisdiction of questions under the Self-Employment Contributions Act other than those concerning the definition of net earnings from self-employment (sections 1401–1403) and the application of the provisions of subtitle F of the Code. In cases where organizations are determined to be of the type described in section 501(c)(3) of the Code, the Branch issues rulings as to the organizations' status under sections 3121(b) and 3306(c) of the Code.

1113.833 *Estate and Gift Tax Branch.*—The Estate and Gift Tax Branch issues rulings with respect to the application of Federal estate and gift taxes, related statutes, and estate and gift tax treaties as to donors and estates.

1113.834 *Excise Tax Branch.*—The Excise Tax Branch issues rulings with respect to all Federal excise taxes other than alcohol, tobacco, and certain firearms taxes, including determinations under sections 4216 and 4218 of the Code as to the constructive sales price of certain articles subject to manufacturers' excise taxes. The excise taxes comprise a variety of taxes which may be identified generally as sales taxes imposed upon manufacturers, producers, or importers; sales taxes imposed upon retailers; documentary stamp taxes; admissions, cabaret, and dues taxes; transportation taxes; communication taxes; and miscellaneous excise, occupational, and regulatory taxes.

1113.835 *Individual Income Tax Branch.*—The Individual Income Tax Branch issues rulings with respect to the application of Federal income taxes and related statutes applicable to noncorporate taxpayers (including partnerships, estates, and trusts). The Branch also considers issues involving corporate contributions (section 170 of the Code); cooperative housing corporations (section 216); restricted

stock option plans adopted by corporations for its employees (section 421); and withholding of tax on foreign corporations (section 1442).

1113.836 *Pension Trust Branch.*—The Pension Trust Branch issues rulings and reviews field determination letters as to the qualification of pension, profit-sharing, and stock bonus plans under section 401, and exemption of employees' trusts under section 501 of the Code; rules on collateral matters involving taxability of beneficiaries under sections 402 and 403, and employer deductions under section 404, and related issues; and determines whether transactions prohibited by section 503 have been engaged in.

1113.837 *Exempt Organizations Branch.*—The Exempt Organizations Branch issues rulings (and reviews field determination letters) to organizations, trusts, etc., with respect to the exemption from income tax under sections 501 and 521 of the Code, and the responsibilities of exempt organizations for the filing of annual information returns under section 6033, and their liability for unrelated business income tax under section 511; and determines whether they have engaged in prohibited transactions under section 503 or have unreasonably accumulated, or misused, income under section 504; and performs other duties relating to its responsibility for coordinating the work of the Branch with other branches whose work may be affected by the rulings and letters of exemption from income tax. The Branch issues group rulings to organizations described in section 501(c) of the Code, and also has jurisdiction as to the status of certain organizations as agencies or instrumentalities of the United States, a State, or political subdivision thereof or the District of Columbia. The Branch also makes determinations as to whether certain exempt-status information should be withheld from public inspection under section 6104(a)(1)(B) of the Code.

1113.838 *Reorganization Branch.*—The Reorganization Branch issues rulings with respect to the taxable status of exchanges and distributions in connection with corporate reorganizations, organizations and liquidations, and with respect to the distribution of stock dividends and redemptions. It also determines whether distributions, redemptions, exchanges, or transfers referred to in sections 306(b)(4), 367, and 1492 of the Code are in pursuance of a plan having as one of its principal purposes the avoidance of Federal income taxes.

1113.84 *Technical Planning Division.*—The Technical Planning Division conducts a program for issuance and revision of tax regulations, reviews all new or amendatory regulations, and undertakes the initial drafting of certain projects; develops the technical content of tax return forms and instructions and coordinates the preparation of such forms and instructions through the National Office Tax Returns Forms Committee; coordinates the legislative program of the Service, develops recommendations for and provides analyses and technical assistance in connection with new or amendatory tax legislation, and provides related services; and maintains a technical liaison program with Regional and District offices. The Division Director is responsible for and supervises the activities of four branches: Income Tax Branch, Tax Returns Forms and Instructions Branch, Technical Programming Branch, and Wage and Excise Tax Branch.

1113.841 *Technical Programming Branch.*—The Technical Pro-

gramming Branch is responsible for planning the performance of the functions of the Internal Revenue Service with respect to legislation, regulations, and tax return forms and the related instructions. It maintains a technical liaison program with the Regional and District offices through which it conducts a continuing survey for the purpose of determining areas involving income tax abuses and inequities, the quality and effectiveness of the regulations and tax return forms, the views of operational personnel concerning new or amendatory legislative and regulatory proposals. It develops, and keeps currently up to date with changing conditions, an over-all program and detailed programs coordinated in these fields. Its representatives arrange and conduct public hearings on proposed regulations which are held as required by the Administrative Procedure Act. The Branch receives and coordinates the requests from the Secretary's staff and Congressional committees for technical assistance on legislation and other matters over which the Division has jurisdiction.

1113.842 *Income Tax Branch.*—The Income Tax Branch is responsible for carrying out the legislative and regulations programs of the Division as they relate to income taxes and to the administrative provisions of general application. In these areas it researches and conducts analytical studies in relation to proposed and pending legislation, prepares formal reports to the Secretary on specific legislative recommendations, drafts all amendments to the Service's Statement of Procedural Rules, drafts or reviews new and amendatory regulations and Treasury decisions and other rules of general application, and reviews other technical materials referred to it for study and comment. It provides technical advice and assistance as requested to the Tax Return Forms and Instructions Branch in the development of forms and instructions in the areas within its jurisdiction. It also provides technical assistance to the Treasury Department, Congressional committees, legislative drafting groups, and to other Divisions of the National Office.

1113.843 *Wage and Excise Tax Branch.*—The Wage and Excise Tax Branch is responsible for carrying out the legislative and regulations programs of the Division as they relate to excise, employment, estate, and gift taxes. In these areas it researches and conducts analytical studies in relation to proposed and pending legislation, prepares formal reports to the Secretary on specific legislative recommendations, drafts or reviews new and amendatory regulations and Treasury decisions and other rules of general application, and reviews other technical materials referred to it for study and comment. It provides technical advice and assistance as requested to the Tax Return Forms and Instructions Branch in the development of forms and instructions in the taxing areas within its jurisdiction. It also provides technical assistance to the Treasury Department, Congressional committees, legislative drafting groups, and to other Divisions of the National Office.

1113.844 *Tax Return Forms and Instructions Branch.*—The Tax Return Forms and Instructions Branch is responsible for initiating, developing, and revising the technical content of all tax return forms, instructions, schedules, and related publications in connection with income, employment, excise, estate, and gift taxes. It coordinates the

direction and operation of the Tax Return Forms Committee in planning, reviewing, and approving tax return forms material. It also provides technical assistance to other offices within the Service, to the Treasury Department, and to Congressional committees.

1113.9 *Office of the Chief Counsel.*—The Chief Counsel, as Assistant General Counsel of the Treasury Department, serves as a member of the Commissioner's executive staff and as counsel and legal officer to the Commissioner on all matters pertaining to the administration and enforcement of the internal revenue laws and related statutes. The key officials under his supervision are: Assistant to the Chief Counsel, Associate Chief Counsel (Litigation), Associate Chief Counsel (Technical), two Assistants Chief Counsel (Litigation), and Assistant Chief Counsel (Technical).

1113.91 *Assistant to the Chief Counsel.*—The Assistant to the Chief Counsel supervises and coordinates all legal management work of the Chief Counsel's Office (the National Office and all field offices); establishes and maintains appropriate standards of professional competence by members of the legal staff of the office and evaluates their legal competence; analyzes the workload of the office, and determines the distribution of personnel available to handle the workload. He exercises general supervision of all matters relating to administration and management in the office of the Chief Counsel. Unless the Chief Counsel otherwise designates, he performs the duties of the Chief Counsel during the absence of the Chief Counsel.

1113.92 *Associate Chief Counsel (Litigation).*—The Associate Chief Counsel (Litigation) plans and directs the policies and programs pertaining to the civil and criminal litigation of the Internal Revenue Service. He exercises direct supervision of the Assistant Chief Counsel (Litigation) and general supervision of the Tax Court, Refund Litigation, Joint Committee, Collection Litigation, Enforcement, and Alcohol and Tobacco Tax Legal Divisions. He serves as the principal legal adviser to the Assistant Commissioner (Operations).

1113.921 *Assistant Chief Counsel (Litigation).*—An Assistant Chief Counsel (Litigation) assists the Associate Chief Counsel (Litigation) in controlling and coordinating the policies and programs pertaining to Tax Court, Refund Litigation and Joint Committee work. He exercises direct supervision of the Directors of the Tax Court, Refund Litigation, and Joint Committee Divisions, and general supervision of the work of Regional Counsel in Tax Court and Joint Committee matters.

1113.9211 *Tax Court Division.*—The Tax Court Division develops policies, programs, and procedures relating to the disposition of tax cases pending in the Tax Court of the United States; supervises and coordinates the defense and settlement of such cases to assure uniform treatment; coordinates and reviews Tax Court matters prepared in the regional offices, including the review of briefs to be filed with the Tax Court and recommendations of field offices for acquiescence or nonacquiescence in adverse Tax Court decisions; prepares recommendations to the Department of Justice for the Commissioner's appeals to the Courts of Appeals and prepares petitions and records on review in such cases; makes recommendations to that Department regarding offers in compromise or settlement and prepares recommendations for

or against filing petitions for writs of certiorari to the Supreme Court in such cases. It supervises and handles the trial of excess profits tax refund cases.

1113.9212 *Refund Litigation Division.*—The Refund Litigation Division performs all necessary legal service on behalf of the Internal Revenue Service in connection with taxpayers' suits for refund of taxes (except alcohol and tobacco taxes). It determines and coordinates the legal position of the Service in such suits and incorporates such determinations in recommendations to the Department of Justice with respect to the defense of such suits, the acceptance or rejection of settlement proposals, and appeals and petitions for certiorari from adverse court decisions. The Division performs all necessary legal services on behalf of the Service in connection with all civil litigation affecting the Service and not within the responsibility of any other Division.

1113.9213 *Joint Committee Division.*—The Joint Committee Division is responsible for the review of proposed refunds or credits exceeding $100,000. In such cases, the allowance is reviewed by the Chief Counsel's office. These cases include overpayments of income, excess profits, estate, gift, and miscellaneous taxes proposed for allowance, and allowances already made of tentative adjustments of income and excess profits taxes. Any deficiencies coupled with such tax reductions under review are likewise subject to review. In certain cases a report is prepared for the Joint Committee on Internal Revenue Taxation as required by section 6405 of the Internal Revenue Code.

1113.922 *Assistant Chief Counsel (Litigation).*—An Assistant Chief Counsel (Litigation) assists the Associate Chief Counsel (Litigation) in controlling and coordinating the policies and programs pertaining to Collection Litigation, Enforcement, and Alcohol and Tobacco Tax work. He exercises direct supervision of the Directors of the Collection Litigation, Enforcement and Alcohol and Tobacco Tax Legal Divisions, and general supervision of the work of Regional Counsel in Collection Litigation, Enforcement, and Alcohol and Tobacco Tax matters.

1113.9221 *Collection Litigation Division.*—The Collection Litigation Division supervises and coordinates legal work of Regional Counsel on Collection Litigation matters. It reviews certain offers in compromise (except those concerning alcohol, tobacco and firearms taxes). It handles legal work concerning (a) cases under section 77, Chapter X and Chapter XII of the Bankruptcy Act, (b) claims or suits for refund of amounts paid as processing taxes, and (c) the preparation of formal opinions on the above matters. In the cases listed above and in certain Regional Office cases the Collection Litigation Division prepares or reviews recommendations to the Department of Justice concerning questions of (a) certiorari, appeal and petition for review, (b) offers in settlement, and (c) waiver or release of a right to redeem under 28 U.S.C. 2410. Similarly, the Division considers recommendations that the Commissioner authorize or sanction affirmative action in (a) insolvency cases (including decedents' estate proceedings), (b) suits for foreclosure of mortgages or other liens and suits to quiet title where the United States is named as a party defendant, (c) cases involving appointment of a receiver in aid of

foreclosure of Federal tax liens, (d) suits for the collection of taxes, and (e) suits for the enforcement of summonses.

1113.9222 *Enforcement Division.*—The Enforcement Division handles and prepares for final decision those criminal tax cases referred to the Chief Counsel by Regional Counsel or by the National Office. It considers cases in which the Regional Commissioner and the Director of the Intelligence Division of the Office of the Assistant Commissioner (Operations) do not concur in recommendations of Regional Counsel involving prosecution. The Division prepares acquiescence memorandums or protest letters on decisions by the Department of Justice or United States Attorneys against prosecution and recommendations to the Department of Justice respecting appeals of court decisions in criminal tax cases. It also prepares law opinions in cases involving penalties or other legal questions with respect to criminal cases or investigations or with respect to the disclosure of information. The Division coordinates with the Department of Justice or interested branches of the Service any questions involving investigations or actions respecting the civil aspects of pending criminal cases. It reviews and prepares for action enrollee and disbarment cases referred to the Chief Counsel by the Director of Practice, and represents the latter in the trial of cases before Hearing Examiners.

1113.9223 *Alcohol and Tobacco Tax Legal Division.*—The Alcohol and Tobacco Tax Legal Division handles the legal work arising in connection with the administration of laws pertaining to alcohol and tobacco taxes and various regulatory laws pertaining to alcohol and firearms, enforcement of which is vested in the Internal Revenue Service, and handles the legal work arising from administrative claims against the United States and Service employees under the Federal Tort Claims Act arising out of acts of Service employees. It maintains general supervision over the legal work involving alcohol and tobacco taxes performed in the office of Regional Counsel. It provides advisory service in the drafting and reviewing of alcohol and tobacco tax laws; and prepares or reviews regulations issued under the alcohol and tobacco tax laws, and rulings and opinions on alcohol and tobacco tax matters. The Division advises the Regional Counsel, when requested, concerning legal matters considered by them. It handles the legal work in connection with the appeal of cases to the Washington level, and refers cases, considered at the Washington level, to the Department of Justice for prosecution, with necessary recommendation and information thereon.

1113.93 *Associate Chief Counsel (Technical).*—The Associate Chief Counsel (Technical) plans and directs the policies and programs of the Office with respect to legislation, regulations, and interpretative rulings and opinions pertaining to the laws administered by the Internal Revenue Service. He exercises direct supervision of the Assistant Chief Counsel (Technical) and general supervision of the Legislation and Regulations Division and the Interpretative Division. He serves as the principal legal adviser to the Assistant Commissioner (Technical).

1113.931 *Assistant Chief Counsel (Technical).*—The Assistant Chief Counsel (Technical) assists the Associate Chief Counsel (Technical) in controlling and coordinating the work of the Office with

respect to legislation, regulations, and interpretative rulings and opinions pertaining to the laws administered by the Internal Revenue Service. He exercises direct supervision of the Directors of the Legislation and Regulations Division and the Interpretative Division, and serves as principal legal advisor to the Directors of the Internal Revenue Service Technical Planning and Tax Rulings Divisions.

1113.9311 *Legislation and Regulations Division.*—The Legislation and Regulations Division, upon request, participates and provides technical assistance in the development and drafting of internal revenue legislation and reviews as to legal form and substance recommendations for new and amendatory legislation. The Division cooperates with the Internal Revenue Service Technical Planning Division in the development of the Service's program for the preparation of new and revised regulations, including Treasury decisions, and in accordance with the approved program undertakes initial preparation of most regulations. It reviews as to legal form and substance all proposed regulations and Treasury decisions, except those pertaining to alcohol and tobacco tax matters. Representatives of the Division participate in public hearings on proposed regulations.

1113.9312 *Interpretative Division.*—The Interpretative Division reviews as to form and legality interpretations of internal revenue statutes and regulations and other law and legal materials bearing upon the administration of the Internal Revenue Service except those relating to: (a) Alcohol, tobacco and firearms matters; (b) criminal tax investigations and prosecutions; (c) lien and collection matters, including those involving bankruptcies, receiverships and other insolvencies; (d) administrative matters; (e) disclosure matters; and (f) summons enforcement matters. The Division prepares formal opinions of the Chief Counsel in assisting him in carrying out his functions as legal advisor to the Commissioner in the technical area. The Division is also responsible for the legal review of closing agreements.

1113.(10) *Director of Practice.*—The Director of Practice processes the applications to practice before the Treasury Department, except those relating to customhouse brokers. He is also responsible for the consideration of and action upon charges that any enrolled person has violated any provision of the laws or regulations governing practice before the Department. The Director of Practice, under the supervision of the Secretary of the Treasury, is a part of the Internal Revenue Service organization.

1114 *Office of Regional Commissioner.*—

1114.1 *Mission.*—The mission of the Office of Regional Commissioner is to execute the broad nationwide policies and programs for the administration of the internal revenue laws, to carry out appellate and alcohol and tobacco tax programs at the regional level, and direct and coordinate the functions and activities of the district offices within the region.

1114.2 *Basic organization.*—The principal organization components of the typical Office of the Regional Commissioner are the immediate office of the Regional Commissioner, the Administration Division, the Alcohol and Tobacco Tax Division, the Appellate Division, the Audit Division, the Collection Division and the Intelligence Divi-

sion. An Assistant Regional Commissioner is at the head of each division.

1114.3 *Regional Commissioner.*—The Regional Commissioner administers within an assigned regional area the collection, audit, intelligence, appellate, alcohol and tobacco tax, and administration programs of the Internal Revenue Service. He carries out Service policies and programs in conformity with delegations of authority and, in this connection, establishes regional standards and programs to assure proper and effective implementation of Service-wide policies and programs within his region. The Regional Commissioner supervises and coordinates the work of the staff of the regional office and the District Directors within his region to assure that work is processed in an orderly and timely manner, and that proper and equable emphasis is placed and directed toward the accomplishment of current program objectives. As the principal field official, he evaluates the effectiveness of Service policies and programs, and advises the National Office as to the need for revising such policies and programs to bring about improved operations or Service.

1114.4 *Assistant Regional Commissioner (Administration).*—The Assistant Regional Commissioner (Administration) acts as the principal assistant to the Regional Commissioner in planning, coordinating and evaluating the administration activities of the Service under the jurisdiction of the Regional Commissioner to assure that administration policies and programs are properly executed. In conformity with the administration policies, and programs established by the National Office, he develops regional standards and other measures necessary to implement most effectively the administration program of the Service which includes budget and fiscal management, personnel administration, training, public information, property and records management, use of facilities, printing and reproduction, and reports management. He also coordinates organization planning and advises and makes recommendations to the Regional Commissioner thereon; and furnishes guidance for and coordinates management programs. He provides the Regional Commissioner with results of evaluations and other information upon which to base his administration of the regional administration programs and recommends improvements and adjustments therein needed to bring about and sustain a high level of performance in administration activities within the region. Under the Regional Commissioner he serves as the primary source of information to the National Office as to the effectiveness of administration policies, programs, procedures and standards in terms of regional and district requirements, provides reports and factual information upon which the National Office can base administration policy and program considerations, and recommends appropriate action with respect to problems encountered in observing and evaluating administration operations. Within the limits of his delegated authority, he provides the Regional Counsel and Regional Inspector with such administrative services as they may require in the performance of their duties. He is responsible for and supervises the activities of four branches: Facilities Management Branch, Fiscal Management Branch, Personnel Branch, and Training Branch.

1114.41 *Facilities Management Branch.*—The Facilities Management Branch coordinates, evaluates and carries out region-wide pro-

grams for providing essential support activities designed to increase the effectiveness of the region, reduce its operating costs and improve taxpayer relations. Develops within the broad guidelines established by the National Office standards and procedures for such matters as the management of paperwork; space; property and supply; procurement and contracts; production, storage, and distribution of forms and publications initiated within the region and distribution and requirements of National Office forms and publications; emergency planning for civil defense; fire and safety, document and property security; and processes all claims arising within the region under the Federal Tort Claims Act.

1114.42 *Fiscal Management Branch.*—The Fiscal Management Branch performs, coordinates and evaluates budgeting, administrative accounting and financial reporting (other than for revenue collections) for the region, including the preparation of the financial plan within over-all budget limitations, submission of budget data, allotment of funds, maintenance of accounts, preparation of payrolls and examination of vouchers. This Branch participates in longrange planning involving expenditures for personnel, equipment, adminstrative services, space and similar items.

1114.43 *Personnel Branch.*—The Personnel Branch develops and evaluates the regional personnel program and standards relating to recruitment and selection, employee relations, disciplinary actions, performance evaluation, promotions, in-service placements, incentive awards, records, reports and other aspects of a complete personnel program, within the framework of broad Service policies, programs and procedures established by the National Office, and conducts the personnel program for the regional office. It conducts the position classification program for the region. This Branch represents the region in contacts with employee groups and the Regional Directors of the Civil Service Commission.

1114.44 *Training Branch.*—The Training Branch provides leadership and coordination to the regional training programs and evaluates and reports on all such programs. It coordinates the regional execution of nationwide training programs; gives advice on all training programs conducted within the region; and assists in their development from the standpoint of training techniques. It participates in and coordinates the development of regional training programs to meet training needs that cut across organizational lines, such as supervisory training and training in clerical skills.

1114.5 *Assistant Regional Commissioner (Alcohol and Tobacco Tax).*—The Assistant Regional Commissioner (Alcohol and Tobacco Tax) acts as the principal assistant to the Regional Commissioner in planning, directing, and coordinating the alcohol and tobacco tax activities of the Service under the jurisdiction of the Regional Commissioner for the execution of Service policies and programs established by the National Office. He is responsible to the Regional Commissioner for the administration and enforcement of internal revenue laws relating to alcohol, alcoholic beverages and products, and tobacco and tobacco products; and related laws, including the Federal Alcohol Adminstration Act, the National and Federal Firearms Acts and the Liquor Enforcement Act of 1936. This includes the supervision and control, under Federal laws, of units of the lawful liquor

and tobacco industries located within the region. Under the Regional Commissioner he serves as the primary source of information to the National Office as to the effectiveness of alcohol and tobacco tax policies, programs, procedures and standards in terms of regional requirements, provides reports and factual information upon which the National Office can base alcohol and tobacco tax policy and program considerations and recommends action with respect to problems encountered in alcohol and tobacco tax operations. He supervises the activities of two branches, Enforcement Branch and Permissive Branch, and all branch offices located within the region.

1114.51 *Enforcement Branch.*—(1) The Enforcement Branch coordinates and evaluates the alcohol and tobacco tax enforcement activities, including those relating to retail liquor dealers, to assure that throughout the region the policies and programs are properly executed with equal emphasis and uniform effort and that the investigative work is pursued in an orderly and timely manner.

(2) In conformity with alcohol and tobacco tax enforcement policies and programs established by the National Office, it develops regional programs, standards and other measures necessary to implement most effectively the investigative program relating to violation of the internal revenue laws and other statutes relating to alcohol, alcoholic beverages and products, tobacco and tobacco products and firearms.

(3) The Branch also directs and performs investigations of all major criminal cases throughout the region and provides functional advice and guidance to branch officers on enforcement matters.

1114.52 *Permissive Branch.*—(1) The Permissive Branch coordinates and evaluates the alcohol and tobacco tax permissive activities to assure that throughout the region the policies and programs are properly executed with equal emphasis and uniform effort and that the work is processed in an orderly and timely manner.

(2) In conformity with alcohol and tobacco tax permissive policies and programs established by the National Office, it develops regional programs, standards and other measures necessary to implement most effectively the control and supervision of the legally qualified liquor and tobacco industries and permittees.

(3) The Branch exercises jurisdiction over the qualification of plants and premises and issuance of permits, and examines and/or audits reports relating to plant operations submitted by proprietors and Government employees. In regions where there are no branch offices (combination), it also directs the activities of all permissive employees, provides advice and guidance to the industry, and supervises its operations through the direction and assignment of storekeeper-gaugers and inspectors. In regions where there are branch offices (combination) the Branch provides advice and guidance to the industry in matters beyond the scope of the branch office, and provides functional advice and guidance to branch offices (combination) on permissive matters.

1114.53 *Branch Offices.*—(1) Branch offices, headed by Supervisors in Charge, direct the permissive and/or enforcement activities within assigned areas of jurisdiction. Those that direct permissive and enforcement activities are known as Combination Offices and those

that direct only enforcement activities are known as Enforcement Offices.

(2) In the regulatory or permissive field Combination Offices provide advice and guidance to the industry and supervise its operations through the direction and assignment of storekeeper-gaugers and inspectors. The activities of the industry supervised include production, storage, tax payment, disposition and use of alcoholic liquors and tobacco by qualified permittees and registrants.

(3) In the enforcement field all branch offices engage in the investigation, prevention, and detection of willful and/or fraudulent substantive violations of the internal revenue liquor and tobacco laws, the Federal Alcohol Administration Act, the Liquor Enforcement Act of 1936, the National and Federal Firearms Acts, the regulations promulgated thereunder and related statutes. This involves the apprehension of violators against such laws; the submission of evidence adduced to United States Attorneys for criminal prosecution and forfeiture action and/or to Regional Commissioner's office for administrative action; the seizure, custody, forfeiture and disposition of real and personal property; the enforcement of the laws and regulations for the control of the flow of raw materials intended for use in the illicit manufacture of distilled spirits; and the inspection of retail liquor dealer establishments.

1114.6 *Assistant Regional Commissioner (Appellate).*—The Assistant Regional Commissioner (Appellate) acts as the principal assistant to the Regional Commissioner in planning, directing, coordinating and evaluating the appellate activities of the Service under the jurisdiction of the Regional Commissioner within the broad framework of policies and programs established by the National Office. He is responsible to the Regional Commissioner for a program of hearing and undertaking final settlement of taxpayers' appeals from determinations of tax liability made by District Directors within the region involving income, profits, estate, gift, and employment taxes, and excise taxes except those imposed on alcohol, wagering, narcotics, firearms, and tobacco. He is responsible for a program of hearing and, with concurrence of Regional Counsel, undertaking final settlement of certain cases docketed in the Tax Court; and for a program of final review for the Commissioner in cases involving overassessments or overpayments in excess of $100,000 requiring review by the Chief Counsel or the Joint Committee on Internal Revenue Taxation. His program includes the hearing of administrative appeals in cases involving offers in compromise. In that capacity, he represents the Commissioner of Internal Revenue and exercises the authority of his office pursuant to, and within the limits of, a delegation of authority from the Regional Commissioner. Under the Regional Commissioner he serves as the primary source of information to the National Office as to the effectiveness of its appellate policies, programs, procedures, and standards in terms of regional requirements, provides reports and factual information upon which the National Office can base its appellate policy and program considerations, and recommends action with respect to problems encountered in appellate operations. He supervises the activities of all appellate branch offices in the region.

1114.61 *Appellate Branch Offices.*—The basic settlement work of the Appellate Division is performed in branch offices of the Division which are headed by Associate Chiefs or Assistant Chiefs who report to the Assistant Regional Commissioner (Appellate). The branch office conducts hearings and makes final determinations, within the limits of its delegated authority, on cases involving income, profits, estate, gift, and employment taxes and excise taxes, except those imposed on alcohol, wagering, narcotics, firearms and tobacco, in which taxpayers have requested appellate consideration. The branch office conducts hearings and, with the concurrence of the Regional Counsel, effects settlement of cases which have been docketed in the Tax Court before the opening date of the session at which the case is calendared for trial, or of any pre-trial hearing of or report session thereon. It makes the final review for the Commissioner in all cases involving overassessments or overpayments in excess of $100,000 which are subject to review by the Chief Counsel or the Joint Committee on Internal Revenue Taxation. The branch office considers protested offers in compromise and makes recommendations on final closing agreements.

1114.7 *Assistant Regional Commissioner (Audit).*—The Assistant Regional Commissioner (Audit) acts as the principal assistant to the Regional Commissioner in planning, coordinating and evaluating the audit activities of the Service under the jurisdiction of the Regional Commissioner to assure that policies and programs are properly executed, that audit work is processed in an orderly and timely manner, that equal emphasis is placed and uniform effort directed toward the accomplishment of the current audit program objectives, and that required standards for audit uniformity are being maintained. In conformity with audit policies, and programs established by the National Office, he develops regional programs, standards, and other measures necessary to implement most effectively the audit program of the Service which includes the selection of returns for audit, their examination and investigation, the determination of tax liabilities and penalties where applicable, a regional review of selected cases closed by the district offices, the administrative disposition of offers in compromise, and tax assistance to taxpayers. He provides the Regional Commissioner with results of evaluation and other information upon which to base his administration of the regional audit program and recommends improvements and adjustments in audit operations needed to bring about and sustain a high level of performance within the region. Under the Regional Commissioner he serves as the primary source of information to the National Office as to the effectiveness of policies, programs, procedures and standards in terms of regional and district requirements, provides reports and factual information upon which the National Office can base policy and program considerations, and recommends appropriate action with respect to problems encountered in observing and evaluating audit operations.

1114.8 *Assistant Regional Commissioner (Collection).*—The assistant Regional Commissioner (Collection) acts as the principal assistant to the Regional Commissioner in planning, coordinating and evaluating the collection activities of the Service under the jurisdiction of the Regional Commissioner to assure that policies and programs are properly executed, that collection work is processed in an

orderly and timely manner, and that equal emphasis is placed and uniform effort directed toward the accomplishment of the current collection program objectives. In conformity with collection policies, and programs established by the National Office, he develops regional programs, standards and other measures necessary to implement most effectively the program of the Service for the collection and accounting of revenue, including the collection of delinquent accounts and the securing of delinquent returns. He provides the Regional Commissioner with results of evaluations and other information upon which to base his administration of the regional collection program and recommends improvements and adjustments in collection operations needed to bring about and sustain a high level of performance within the region. Under the Regional Commissioner he serves as the primary source of information to the National Office as to the effectiveness of collection policies, programs, procedures and standards in terms of regional and district requirements, provides reports and factual information upon which the National Office can base collection policy and program considerations and recommends appropriate action with respect to problems encountered in observing and evaluating collection operations.

1114.9 *Assistant Regional Commissioner (Intelligence).*—The Assistant Regional Commissioner (Intelligence) acts as the principal assistant to the Regional Commissioner in planning, coordinating and evaluating the intelligence activities of the Service under the jurisdiction of the Regional Commissioner to assure that policies and programs are properly executed, and that the intelligence work is processed in an orderly and timely manner. In conformity with intelligence policies, and programs established by the National Office, he develops regional programs standards and other measures necessary to implement most effectively the intelligence program of the Service which includes the investigation of alleged tax fraud, certain other civil and alleged criminal violations of tax laws (except alcohol, tobacco and certain firearms tax cases), and such other special investigations as the Commissioner may direct. He provides the Regional Commissioner with results of evaluations and other information upon which to base his administration of the regional intelligence program and recommends improvements and adjustments in intelligence operations needed to bring about and sustain a high level of performance within the region. Under the Regional Commissioner he serves as the primary source of information to the National Office as to the effectiveness of intelligence policies, programs, procedures and standards in terms of regional and district requirements, provides reports and factual information upon which the National Office can base intelligence policy and program considerations and recommends appropriate action with respect to problems encountered in observing and evaluating intelligence operations. He supervises the review of special agents' reports of investigation submitted by the district offices in the region, approves or disapproves recommendations for prosecution, and provides for conferences when required with taxpayers, their representatives, representatives of the Regional Counsel and the Appellate Division relative to cases investigated.

1114.91 *Review and Conference Staff.*—(1) The Review and Conference Staff plans and directs the critical review of district office

reports pertaining to alleged criminal violations of the internal revenue laws, which contain recommendations for criminal prosecution and/or ad valorem penalties, to determine that the conclusions and recommendations are sound and conform to existing policies; and recommends to the Assistant Regional Commissioner (Intelligence) the action to be taken on each such report.

(2) The Staff post reviews selected non-prosecution case reports prepared at the district level and unnumbered case disposals to determine that an appropriate, uniform basis for disposal existed. Where deficiencies are disclosed through such activities, the Staff suggests corrective measures.

(3) Through continuing analysis of district office reports the Staff provides the Assistant Regional Commissioner (Intelligence) with information which will assist him in evaluating investigative techniques employed and the extent of procedural and technical uniformity in the intelligence activity throughout the region.

(4) The Staff consults with and advises intelligence personnel at regional and district office locations on difficult and unusual issues, interpretations of regulations, rulings, tax laws and court decisions; also, as to the conduct of investigations, rules of evidence and Service policies. The Staff undertakes special assignments and investigations as directed by the Assistant Regional Commissioner (Intelligence).

1115 *Office of Regional Inspector.*—There are nine Regional Inspectors, one in each internal revenue region. The Regional Inspector, who operates under the direct supervision of the Assistant Commissioner (Inspection), is responsible for the conduct throughout the region of both the internal audit and internal security programs.

1115.1 *Assistant Regional Inspector (Internal Audit).*—Under the supervision of the Regional Inspector, the Assistant Regional Inspector (Internal Audit) is responsible for the conduct of the internal audit program throughout the region. The internal audit, which includes verification of financial transactions and analyses of operating practices and procedures, serves as the basis for informing appropriate officials of the manner in which operations are being carried out and responsibilities are being discharged and as a basis for necessary changes in policies, practices and procedures.

1115.2 *Assistant Regional Inspector (Internal Security).*—The Assistant Regional Inspector (Internal Security) is responsible for the conduct of the internal security program throughout the region. The program, which provides management with a factual basis for making decisions, includes personnel background investigations and investigations of complaints and allegations of misconduct or irregularities concerning Service employees. The program also includes background investigations of certain applicants for enrollment to practice before the Internal Revenue Service, investigations of charges against tax practitioners, formal investigations of accidents involving Service employees or property, and investigations of complaints alleging discrimination in violation of the Government Employment Policy. In addition, he is responsible throughout the region for the conduct of special investigations, as directed by higher authority, for the Office of the Secretary and other components of the Treasury Department.

1116 *Office of Regional Counsel.*—(1) There are nine Regional Counsels, one in each internal revenue region. The Regional Counsel, who operates under the Chief Counsel for the Internal Revenue Service, serves as the principal legal advisor to the Regional Commissioner, and directs a staff of attorneys engaged in furnishing legal advice and performing legal services connected with the Tax Court, enforcement, collection litigation and alcohol and tobacco tax programs. The Regional Counsel, with the concurrence of the Regional Commissioner, settles tax cases docketed in the Tax Court of the United States, and represents the Commissioner in the trial of such cases before the Tax Court.

(2) Tax Court Matters: The Regional Counsel (or his delegate) furnishes legal advice to the Assistant Regional Commissioner (Appellate); represents the Commissioner in the trial of cases before the Tax Court and is responsible for answers, motions and stipulations with respect to all petitions in tax cases, recommends acquiescence or nonacquiescence and appeal from adverse decisions; considers and approves or disapproves, with the concurrence of the Appellate Division, the settlement of cases docketed in the Tax Court prior to session status, and approves or disapproves such settlement of cases in session status; and considers and concurs with the Appellate Division, or disapproves, the elimination of the ad valorem fraud penalties in cases not docketed in the Tax Court and considers statutory notices of deficiencies proposed by the Appellate Division prior to issuance.

(3) Enforcement Matters: The Regional Counsel's office is responsible for the performance of legal services in the field in connection with criminal cases arising under the internal revenue laws. The office reviews recommendations of prosecution in criminal cases received in the field, and prepares and refers such cases (other than alcohol and tobacco tax cases) to the Department of Justice or, where authorized by the Department of Justice, directly to United States Attorneys, or, where prosecution is not deemed warranted, prepares criminal action memoranda setting forth the reasons against the prosecution and closes such cases with the concurrence of the Assistant Regional Commissioner (Intelligence). On request, the office furnishes aid and assistance to United States Attorneys in criminal tax proceedings in the United States District Courts and Courts of Appeal.

(4) Collection Litigation Matters: Each Regional Counsel through his collection litigation staff handles legal work with respect to (a) cases under the Bankruptcy Act (except railroad reorganizations, corporate reorganizations, and real property arrangements under section 77, Chapter X and Chapter XII, respectively, of the Bankruptcy Act) and other insolvency cases including decedents' estate proceedings; (b) Federal tax liens in suits for foreclosure by mortgagees or other lien-holders and in suits to quiet title; (c) applications filed for the discharge of property from Federal tax liens or for the release of such liens; (d) the review and handling of certain offers in compromise; (e) recommendations as to the taking of affirmative action, whether by way of a separate suit or intervention in pending proceedings (with the exception of alcohol, tobacco and firearms matters not relating to proceedings under the Bankruptcy Act, liens, receiverships and other insolvencies); (f) the defense of injunction suits to restrain

the assessment or collection of Federal taxes (except with respect to alcohol, tobacco and firearms matters); (g) the assessment and collection of taxes; (h) suits for recovery of erroneous refunds; and (i) enforcement of summonses.

(5) Alcohol and Tobacco Tax Matters: The Regional Counsel's office gives legal advice on request to the Assistant Regional Commissioner (Alcohol and Tobacco Tax) and to his staff on administration and enforcement of the laws and regulations pertaining to liquor, tobacco and firearms. The office reviews and makes recommendations, upon request, regarding claims for refund, abatement and drawback of liquor, tobacco and firearms taxes, for the redemption of stamps, and for damages, and with respect to petitions for mitigation or remission of forfeiture, offers in compromise, and proposed tax assessments. Upon request, the office assists United States Attorneys by preparing libels of information, indictments, briefs, stipulations and other legal documents required in litigation, and by aiding in the prosecution and defense of suits. The office also handles the legal work in connection with administrative proceedings involving the issuance, suspension, revocation or annulment of liquor and tobacco permits, including the preparation of the necessary opinions, notices and pleadings and the presentation of the Government's case at both formal and informal hearings.

1117 *Service centers.*—

1117.1 *General.*—(1) There are three Internal Revenue Service Centers—designated as the Northeast Service Center, the Midwest Service Center, and the Western Service Center. The Northeast Service Center, located at Lawrence, Massachusetts, serves all district offices in the Boston, New York and Philadelphia Regions. The Midwest Service Center, located at Kansas City, Missouri, serves all district offices in the Cincinnati, Chicago and Atlanta Regions. The Western Service Center, located at Ogden, Utah, serves all district offices in the Omaha, Dallas and San Francisco Regions, except Honolulu. These Service Centers process income tax returns and related documents through the use of electronic data processing machines and other high-speed processing devices and systems.

(2) Within the structure of the Internal Revenue Service, the three Service Centers have organizational status comparable to that of the district offices. Each Service Center operates under the line supervision of a Service Center Director, who is responsible to a Regional Commissioner of jurisdiction in the same manner in which a District Director is responsible to a Regional Commissioner. The Service Center Director is responsible for budget, fiscal and personnel operations of the center and for supervising the execution of the Service Center's work programs. He also participates with the National Office, through the Regional Commissioner, in planning, coordinating and evaluating experimental projects to develop improved techniques and methods for processing work of the Internal Revenue Service.

(3) The Regional Commissioners at Boston, Cincinnati and San Francisco, exercise line supervision over the Northeast, Midwest and Western Service Centers, respectively. The Regional Commissioner is responsible to the National Office for the execution of the Service Center's program and for recommending adjustments to or modifications of the program. The Regional Commissioner also supervises

the Service Center Director in coordinating and maintaining liaison with the several Regional Commissioners, District Directors, and the National Office in carrying out the programs prescribed for the centers.

(4) A fourth service center, designated as the Atlanta Service Center and oriented to the ADP systems, is in the process of activation.

1117.2 *Programs.*—(1) The work programs performed in each Service Center are prescribed and assigned by the National Office.

(2) Programs assigned the Service Centers include the processing, analysis, and accounting control of income tax returns, estimated tax returns, wage and excise tax returns, farmers' gas tax refund claims, withholding tax documents, tax information documents, the mailing of income tax forms to individual taxpayers, the transcription of statistics information for the National Office Statistics Division, the preparation and certification of payrolls covering the salaries of employees throughout the Internal Revenue Service, and the preparation of special classification reports for the National Office Audit Division. These programs are not all-inclusive, and additional pilot studies and permanent assignments are made at the discretion of the National Office with a view of (a) obtaining the benefits of data processing systems or mechanization in new work areas and/or (b) equalizing the total workload among the four Service Centers.

1117.3 *District Office—Service Center Functions.*—The district offices served by the centers receive the returns filed by the taxpayers, deposit all remittances, and settle all questions about the returns (including notices of change of address) before sending the returns to the centers for processing. They also endorse all notices of tax due issued by the center on which payment is made, and send them to the center for posting. The center, in turn, lists the returns on assessment lists, sends out even notices to taxpayers, prepares check-issue cards for the Regional Disbursing Office, sends out bills (first notices) on taxable-assessable and underpaid returns, prepares taxpayer delinquent account assemblies and unit ledger cards and turns over unpaid accounts to District Directors, all under proper memorandum accounting controls. These service center operations are performed in the name of the appropriate District Director.

1117.4 *Service Center Organization.*—

1117.41 *General.*—In order to process this high volume and complex workload through the use of high speed devices and mass production techniques, each Service Center has been organized functionally into operating divisions with top level planning and program coordination being exercised from the Office of the Director. A Planning and Scheduling Staff has been developed in each center to assist the Director in the execution of these duties. Service Center divisions which reflect this functional alignment are as follows: Transcription and Document Processing Division, Accounting and Control Division, Data Processing Division, Payroll and Reports Division and Administration Division.

1117.42 *Transcription and Document Processing Division.*—The Transcription and Document Processing Division is responsible for the transcription portion (key punching) of all work programs assigned the center. Examples of these programs include the transcription of income tax returns, farmers' gas tax refund claims, and

the National Office payroll and fiscal reports program. In addition, this division is responsible for the manual processing of income information and tax documents programs; the sorting of mail address slips; the assembly and distribution of school teaching kits throughout the Nation; and such other programs as may be assigned which require manual processing. The work of the division is performed by the Review and Transcription Branch (key punching) and by the Document Processing Branch (manual processing).

1117.43 *Accounting and Control Division.*—The Accounting and Control Division is responsible for the review, inspection and placing under production control of returns and declarations preparatory to their processing in the Service Center; the sorting of returns into audit and statistical categories; the disposition of documents upon completion of Service Center processing; the conducting of "error inspection" activities involving the detailed examination of those returns and declarations which in the process of computation have been designated as possible error cases; the screening, perfection, and preparation of necessary correspondence with reference to the Farmers' Gas Tax Refund Program; implementation of the returns examination portion of the National Office Statistics Division Program; execution of the mail labeling portion of the Income Tax Forms Mailing Program; the establishment and maintenance of appropriate memorandum accounting controls reciprocal to general ledger accounts maintained by district offices served by the center; the establishment and maintenance of controls over all open accounts receivable up to and including taxpayer delinquent account status; the establishment of appropriate accounts covering refund disbursements; the balancing and reconciling of tabulated listings of registers and schedules prepared in the Data Processing Division; the certification of refund vouchers to the Regional Disbursing Office; the certification of assessment certificates for amounts of tax due and billed by the service center; the furnishing to district offices of appropriate journals and schedules of work processed for entry in general and subsidiary ledgers; the establishment, control, and balancing of estimated tax accounts and quarterly payments thereto throughout the tax year; and the preparation of required accounting reports. The work of the division is performed by the Documents Control and Analysis Branch and the Accounting Branch.

1117.44 *Data Processing Division.*—(1) The Data Processing Division is responsible for the mathematical verification and computation of tax and balance; preparation of assessment lists; identification of potential pre-refund audit returns; establishment through electronic or tabulating processes of tax accounts receivable and the maintenance of such accounts, including trial balancing; issuance of bills and notices to individual income taxpayers, including those of delinquent accounts and delinquent returns; identification of overpaid returns, association of appropriate check-issue cards, and the preparation of related refund vouchers; pre-addressing and prepunching blank income tax returns for mailing to individual taxpayers; establishment of index cards for individual taxpayers and their proper arrangement for use in district offices; development of basic statistical data for use on a national basis with respect to tax returns received and processed; computation and register listing of

payrolls covering salaries of Internal Revenue Service employees; preparation of quarterly estimated tax bills and the recording of payments made on them; division participation in the production of reports; and the performance of machine applications required by other programs as assigned.

(2) The Division undertakes and evaluates experimental projects developed by the Office of the Director in conjunction with the Regional Office of jurisdiction and/or the National Office in an effort to improve or extend mass processing techniques. The work of the division is performed by the Electronic Computing Branch and the Recording Branch.

1117.45 *Payroll and Reports Division.*—(1) The Payroll and Reports Division is responsible for the payment of salaries of Internal Revenue Service employees, the accuracy and timeliness of such payments, the furnishing of time and attendance cards and accounting and budgetary information, the planning and coordination of the activities of this Division, with those of other Service Center Divisions, and the assistance to the National Office and regional representatives in installing any new procedures, techniques and programs. The Division is organized into the Reports and Control Branch and the Payroll Branch. However, in accordance with the concept of functional organization, electronic accounting operations and other services are provided this Division by the Transcription and Document Processing Division ad the Data Processing Division.

(2) The Payroll and Reports Division exists only in the Northeast and Western Service Centers. The northeast Service Center processes payrolls for approximately 60 percent of the national total of Internal Revenue Service employees and the Western Service Center processes payrolls for the remaining 40 percent.

1117.46 *Administration Division.*—The Administration Division provides the personnel, training, budget and fiscal, procurement and supply, records and communications services, and other administrative services (within the limitations of the Service Center Director's delegated authority) necessary to the effective operation and management of the Service Center. It coordinates the Service Center management improvement and incentive awards programs and other special projects. The division is responsible for the recruitment and placement functions at the center, and conducts the employee relations program. It participates in and coordinates the development of Service Center training programs to meet local training needs. It carries out the space program of the center and conducts periodic surveys to assure effective space utilization. It procures, requisitions, issues, and assures effective utilization of equipment, property and office supplies, and provides communications and duplicating services. It administers documents and property security, safety and records management programs in the center.

1118 *Office of District Director.*

1118.1 *Mission.*—The mission of the office of the District Director is to administer the internal revenue laws within an internal revenue district in conformance with Service policies and programs of the National and regional offices.

1118.2 *Basic organization.*—The principal organizational components of the typical district office are the immediate office of the Dis-

trict Director, the Audit Division, Collection Division, Intelligence Division and Administration Division.

1118.3 *District Director.*—The District Director administers, within an internal revenue district, the collection, audit, intelligence and administrative programs of the Internal Revenue Service. He is responsible for the determination of tax liability, the assessment of such liability, the scheduling and certification of refunds, and the investigation of certain criminal and civil violations of internal revenue tax laws (except those relating to alcohol, tobacco and firearms). He is also responsible for the collection and deposit of all internal revenue taxes.

1118.4 *Audit Division.*—The Audit Division administers a district-wide audit program involving the selection and examination of all types of Federal tax returns (except those involving alcohol, tobacco, and firearms taxes), claims, offers in compromise, informants' claims for rewards, and related activities including the examination and approval of pension trust plans and the issuance of determination letters. The audit program involves the selective classification of returns for field and office audits, the conduct of informal conferences in cases involving disagreement between the internal revenue agents and taxpayers, participation with special agents of the Intelligence Division in the conduct of tax fraud investigations and a program of assistance to taxpayers during the annual filing period. The Audit Division consists of the Field Audit Branch, Office Audit Branch, Service Branch and the Review Staff.

1118.41 *Field Audit Branch.*—(1) The Field Audit Branch conducts field examinations relative to all types of taxes (except alcohol, tobacco, and firearms) to determine correct liabilities of taxpayers for tax and penalties, including the examination of claims for refund, credit or abatement, or for redemption of stamps. It also conducts field examinations of offers in compromise based on either doubt as to liability or inability to pay, and special field examinations as requested including joint examinations with special agents of the Intelligence Division where tax evasion may exist. The Branch processes informants' claims for reward making any necessary investigations and prepares reports on such claims, together with recommendations as to the amount of rewards.

(2) The Field Audit Branch holds informal conferences with taxpayers and their representatives, and prepares conference reports directing action to be taken by examining officers. It furnishes technical advice and assistance on pension trust plans, performs engineering and valuation work, prepares memoranda to accompany closing agreements and closing letters and releases in estate and gift tax cases, and recommends jeopardy assessments. The Branch furnishes information to the public on tax matters and assists taxpayers in preparing and filing tax returns and claims.

1118.42 *Office Audit Branch.*—(1) The Office Audit Branch conducts examinations through correspondence or interviews with taxpayers in offices of the Service relative to all types of taxes (except alcohol, tobacco and firearms) to determine correct liability of tax-

payers for tax and penalties, the allowableness of claims for refund, credit, or abatement, or for redemption of stamps, including claims for exemption from collecting admissions, transportation, and other excise taxes. It recommends jeopardy assessments.

(2) The Branch holds informal conferences with taxpayers and their representatives for the purpose of resolving disputed issues in unagreed cases. The Branch also furnishes information to the public on tax matters and assists taxpayers in preparing and filing tax returns and claims.

1118.43 *Review Staff.*—(1) The Review Staff reviews reports of examination of all types of tax returns to verify the determination of liability made by the examining officer. It directs the issuance of preliminary notices of deficiency to taxpayers, and prepares Form 7900 letters to taxpayers covering deficiencies in bankruptcy and receivership cases which serve as a basis for assessment and filing of proof of claim by the Collection Division. It reviews protests filed in response to notices of deficiency and Form 7900 letters for proper form, compliance with existing requirements and for new issues or facts. It also prepares statutory notices of deficiency.

(2) The Staff is responsible for the control, management and review of offers in compromise, informants' claims for reward and the special procedures applicable in cases involving renegotiation. It maintains and controls the preliminary notice file, the statutory notice file, the file on cases suspended pending court or other decision (Form 1254), power of attorney file, fee statement file, and worthless stock and taxability of dividend file, taking appropriate action as required. The Staff prepares the Management Information Reports for both agreed and unagreed cases.

(3) The Staff has primary responsibility within the district for maintaining quality standards in examinations and reports, and the technical accuracy of all matters subject to review. It issues correction memoranda in all cases or matters involving substantial error.

1118.44 *Service Branch.*—(1) The Service Branch performs clerical services for the Division necessary to the processing of returns, reports of examination, case files and correspondence. It maintains control of all returns and case files assigned to the Audit Division and of number assignments for Management Information Reports on audit cases. It types examining officers' reports, form letters, correspondence and other material as assigned and furnishes clerical, stenographic and typing assistance to all Division offices.

(2) The Service Branch also compiles detailed production statistics of the Audit Division.

1118.5 *Collection Division.*—(1) The Collection Division is responsible for the receipt and processing of tax returns and related documents filed with the district; the deposit of and accounting for tax remittances; making determinations with respect to tax refunds, credits, penalties, abatements or overassessments; maintaining prescribed accounting and ledger controls including control of the refund appropriation account; the performance of all collection activity as relates to the sale and accounting for revenue stamps; the collection

of delinquent accounts through distraint, seizure, levy and other means and the securing of delinquent returns.

(2) The organization of the Collection Division varies in its branches based on the size of the district. The basic or large district organization has four branches: Returns and Receipts, Revenue Accounting, Taxpayer Service, and Delinquent Accounts and Returns. The organization for medium districts has three branches: Returns and Receipts, Taxpayer Service and Accounts, and Delinquent Accounts and Returns. The organization for small districts has two branches: Office Branch, and the Delinquent Accounts and Returns Branch. The basic or large district organization is set forth below.

1118.51 *Returns and Receipts Branch.*—(1) The Returns and Receipts Branch is responsible for the receipt, categorical classification and internal routing of all tax returns, remittances, correspondence and other documents received by the District Office. It sorts, examines, verifies and reconciles tax returns, forms, schedules and other types of supporting tax and information documents for correctness; matches prepayment credits and associates supporting information documents with tax returns in preparation for audit: computes or verifies tax on all wage and excise tax returns, estate and gift and corporation income tax returns; makes certain penalty determinations; numbers all non-remittance returns; and prepares, transmits and controls shipment of returns and documents to and from the Service Center and the Social Security Administration.

(2) The Branch is responsible for the examination of all tax returns and documents received with remittance and for the determination of acceptability of remittances for deposit. It classifies returns and documents by prescribed classification and initially accounts for all remittances by class of tax; maintains required records and effects prescribed balancing of all recorded entries; takes required action to make daily deposits in designated depositary bank; and numbers all remittance returns. It coordinates cashier receipts and deposits activities with accounting and processing operations; initiates predeposit search on all remittances received without returns or identifying documents; and receives returned remittances from depositary bank and attempts to make collection from taxpayer; prepares necessary debit vouchers, posting vouchers and maintains pertinent records. The Branch is responsible for requisitioning, issuance and control of internal revenue stamps, Revenue Officers' receipt books, and other receipts for payment of internal revenue taxes. It handles and maintains collateral agreement records and related securities. The Branch has line responsibility for all teller activities in the same location as the Returns and Receipts Branch and functional responsibility for all other teller activities.

1118.52 *Revenue Accounting Branch.*—(1) The Revenue Accounting Branch performs all revenue accounting activities with respect to determining and recording of payments and adjustments to taxpayers' accounts and establishes and maintains all prescribed accounting control records, posting media and related accounting records. It is responsible for the mechanical listing (or scheduling) of all returns

filed, and for the posting of debits and credits to taxpayer accounts and balancing of ledgers to sectional controls. It classifies and records all tax payments received without appropriate identification and searches records to identify same; issues all tax bills, notices and taxpayer delinquent accounts; prepares required vouchers to effect adjustments involving payments, debits or credits to taxpayers' accounts and prepares abatement vouchers on duplicate assessments; maintains all account card files on a current posting basis; maintains all required sectional and general ledger controls in connection with revenue accounting operations; makes reconciliations of ledger controls with prescribed sectional controls and takes appropriate action to ascertain source of discrepancies and make necessary corrections in records; and prepares and submits all accounting and ledger reports as required.

(2) The Branch makes final determination of tentative carry-back adjustments; prepares necessary schedules and vouchers in connection with the refunding appropriation; computes general and restricted interest; maintains files of refund and credit schedules; prepares certificates of overassessment; prepares appropriate overassessment schedules for refund, credit or abatement; and computes or verifies tax on certain tax returns.

1118.53 *Taxpayer Service Branch.*—(1) The Taxpayer Service Branch is responsible for taxpayer contact by telephone, mail or personal call; adjustments on tax returns; preparation of replies to correspondence; informal conferences relative to tax adjustments; and taxpayer assistance except during filing periods.

(2) The Branch establishes and maintains all tax returns files and index card files and furnishes information from the files as requested. It maintains addressograph files and plates and performs all addressograph services; maintains and distributes adequate supplies of various types of income tax forms, returns, and all processing forms; addresses, stuffs and mails copies of blank tax forms, tax notice forms and other documents and forms, except those handled by Service Centers. Photostats all tax forms, returns and other documents, as required; assigns and controls all employers' identification numbers; receives, analyzes, classifies, controls, routes, performs research and makes reply to various routine types of correspondence on collection matters which can be serviced at a centralized point; prepares various documents for transmittal to the Federal Records Center, Service Center, Statistics Division and other (associate) Government agencies, as necessary; coordinates Collection activities with Administration, Audit, Intelligence, Appellate, Statistics, Federal Records Center and Service Centers relative to returns; disposition, classification, statistics and processing. The Branch is responsible for furnishing advice and testimony concerning filing, processing, coding and related markings on all returns and documents.

1118.54 *Delinquent Accounts and Returns Branch.*—(1) The Delinquent Accounts and Returns Branch makes collections of delinquent accounts and conducts a continuing program for the securing of delinquent returns.

(2) The Branch safeguards the Government's interests through the filing of notices of tax liens, and enforces collection by the serving of levies, and seizure and sale of real and personal property. It recommends jeopardy assessment when deemed necessary to protect revenue, civil actions to secure payment, suits to enforce penalty for failure to honor levies, and penalty assessments as a means of collection or as a method of obtaining compliance with existing laws and regulations. The Branch recommends the issuance of certificates of discharge of property from the effects of tax liens and conducts the investigations necessary to support such recommendations.

(3) The Branch receives, acts on, and processes information pertinent to bankruptcies, receiverships, assignments, reorganizations, probate proceedings, bulk sales, gifts and prizes, and dissolutions and initiates investigations for securing delinquent returns where necessary . It canvasses the district for delinquent returns and serves summonses on taxpayers to produce books, documents, returns or other information where necessary to secure compliance with the requirements for filing returns.

(4) The Branch maintains control of payments received in insolvency, bankruptcy, and decedent cases and of surety bonds and other collateral posted as security for tax liability. It also maintains files and control records of property seized under distraint authority and takes appropriate action with respect to seized property to assure that proper legal action may be timely taken.

(5) The Branch has line responsibility for all teller activities in a location different from that of the Returns and Receipts Branch.

1118.6 *Intelligence Division.*—(1) The Intelligence Division investigates alleged criminal violations of the tax statutes, including racketeer and wagering tax cases, but excluding alcohol, tobacco and firearms tax cases.

(2) The Division evaluates allegations and indications of tax law violations and determines investigations to be undertaken. It makes recommendations as to the disposition of cases investigated including recommendations of criminal prosecution, and the assertion of civil penalties. It provides assistance to U.S. Attorneys and the Regional Counsel in the trial of cases. The Intelligence Division consists of groups of special agents.

1118.7 *Administration Division.*—The Administration Division provides the personnel, training, budget and fiscal, procurement and supply, records, and communications services and other administrative services, within the limitations of the District Director's delegated authority, necessary to the effective operation and management of the district office. It coordinates the district office management improvement and incentive awards programs and other special projects. The Administration Division consists of three branches where size of the district office warrants such a breakdown: Facilities Management Branch, Personnel Branch, and Training Branch.

1118.71 *Facilities Management Branch.*—The Facilities Management Branch provides essential facilities and services necessary

to the efficient operation of the district office. The Branch carries out the space programs of the District Director and conducts periodic surveys to assure effective space utilization. It procures, requisitions, issues, and assures effective utilization of equipment, property and office supplies; maintains records on all equipment and property located within the district; and provides communications, duplicating, paperwork management, and internal management document distribution services. The Branch also furnishes data necessary for the preparation of that portion of the district office budget estimates and financial plans which is concerned with funds required for materials and facilities in the district. As required for district management control, it maintains blotter type records of fund commitments for materials and facilities (object classes 22, 23, 24, 25, 26, and 31 as defined in Bureau of the Budget Circular A–12). It administers document and property security, emergency planning for civil defense, and the safety programs in the district.

1118.72 *Personnel Branch.*—The Personnel Branch performs the recruitment and placement functions at the district level, and conducts the district's employee relations program and incentive awards program. It processes personnel action documents in accordance with prescribed procedure and maintains all district personnel records.

1118.73 *Training Branch.*—The Training Branch provides leadership and coordination to the district training program. It coordinates the district execution of training programs; gives advice on all training programs conducted in the district office, and assists in their development from the standpoint of training techniques. It participates in and coordinates the development of district training programs to meet local training needs that cut across organizational lines. In addition, it evaluates and reports on all district training programs.

1118.8 *Local Offices.*—(1) Local offices perform one or more of certain collection, audit and intelligence functions such as: The collection of delinquent accounts and the securing of delinquent returns; the receiving and deposit of monies tendered in payment of taxes; the examination of returns to determine correct liability of taxpayers for tax and penalties; the holding of informal conferences with taxpayers and their representatives regarding the determination of liability for tax and penalties; and the investigation of alleged criminal violation of the tax statutes.

(2) The administrative supervision of a local office is the responsibility of a representative designated by the District Director from among the personnel assigned to the local office. Technical supervision of the personnel at a local office is the responsibility of the group supervisor or group supervisors of whatever group or groups the employees are members.

Effective date: July 10, 1961.

[SEAL]

MORTIMER M. CAPLIN,
Commissioner of Internal Revenue.

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APPENDIX A [1]

INTERNAL REVENUE REGIONAL OFFICES

Atlanta, Ga., Federal Office Building, 275 Peachtree Street, Northeast.
Boston, Mass., Houghton-Dutton Building, 55 Tremont Street.
Chicago, Ill., State-Madison Building, 22 West Madison Street.
Cincinnati, Ohio, Swift Building, 230 East Ninth Street.
Dallas, Tex., 1114 Commerce Building, 1114 Commerce Street.
New York, N.Y., Federal Office Building, 90 Church Street.
Omaha, Nebr., U.S. Post Office and Court House, 215 North Seventeenth Street.
Philadelphia, Pa., 2 Penn Center Plaza Building, 2 Penn Center Plaza.
San Francisco, Calif., Flood Building, 870 Market Street.

INTERNAL REVENUE DISTRICT OFFICES

Birmingham, Ala., Birmingham Post Building, 1531 Third Avenue, North.
Anchorage, Alaska, M. & S. Enterprises, Inc., 428 Fifth Avenue.
Phoenix, Ariz., U.S. Government Building, 140 West Monroe Street.
Little Rock, Ark., Post Office and Court House Building, 600 West Capitol Avenue.
Los Angeles, Calif., Post Office and Court House Building, 312 North Spring Street.
San Francisco, Calif., 100 McAllister Building, 100 McAllister Street.
Denver, Colo., New Custom House Building, 19th and California.
Hartford, Conn., 460–470 Capitol Avenue.
Wilmington, Del., Post Office Building, 11th and Market Streets.
Jacksonville, Fla., 400 Building, 400 West Ashley Street.
Atlanta, Ga., Federal Office Building, 275 Peachtree Street, Northeast.
Honolulu, Hawaii, Post Office, Court and Custom House, Mililani, King and Richards Streets.
Boise, Idaho, Broadway Holding Company Building, 914 Jefferson Street.
Chicago, Ill., State-Madison Building, 22 West Madison Street.
Springfield, Ill., Staley Building, 621 East Adams Street.
Indianapolis, Ind., Post Office Building, Ohio, between Meridian and Pennsylvania.
Des Moines, Iowa, Court House Building, East First and Walnut Streets.
Wichita, Kans., Internal Revenue Service Building, 412 South Main Street.
Louisville, Ky., Federal Building, Sixth and Broadway.
New Orleans, La., Federal Office Building, 600 South Street.
Augusta, Maine, Internal Revenue Service Building, 221 State Street.
Baltimore, Md., The 707 Building, 707 North Calvert Street.
Boston, Mass., 174 Ipswich Street.
Detroit, Mich., New Federal Building, 231 West Lafayette Avenue.
St. Paul, Minn., Post Office and Custom House Building, 180 East Kellogg Boulevard.
Jackson, Miss., Post Office and Court House Building, Capitol and West Streets.
Kansas City, Mo., Court House Building, 811 Grand Avenue.
St. Louis, Mo., New Federal Building, 1114 Market Street.
Helena, Mont., Federal Office Building, North Park Avenue.
Omaha, Nebr., Federal Office Building, 15th and Dodge Streets.
Reno, Nev., Post Office Building, P.O. Box 891.
Portsmouth, N.H., 600 State Street.
Camden, N.J., Service Building, 808 Market Street.
Newark, N.J., Industrial Office Building, 1060 Broad Street.
Albuquerque, N. Mex., Federal Office Building, 517 Gold Avenue SW.
Albany, N.Y., 161 Washington Avenue.
Brooklyn, N.Y., Ludwig Bauman Building, 210 Livingston Street.
Buffalo, N.Y., Edwards Building, 266–270 272–294 Pearl Street.
New York, N.Y., Grand Central Palace Building, 484 Lexington Avenue.
Syracuse, N.Y., Chimes Building, 109 West Onondaga Street.
Greensboro, N.C., Federal Office Building, 320 South Ashe Street.
Fargo, N. Dak., Pioneer Mutual Life Insurance Building, 203 North 10th Street.
Cincinnati, Ohio, 700 Walnut Building, 700 Walnut Street.
Cleveland, Ohio, Huron-Sixth Building, 626 Huron Road.

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[1] 26 F.R. 11219.

Oklahoma City, Okla., Sooner Building, 7 South Harvey Street.
Portland, Oreg., 830 Building, 830 Northeast Holladay Street.
Philadelphia, Pa., Court House Building, Ninth and Chestnut Streets.
Pittsburgh, Pa., New Federal Building, Seventh Avenue and Grant Street.
Scranton, Pa., Post Office Building, Corner Linden Street and North Washington Avenue.
Providence, R.I., Co-Op Building, 544 Elmwood Avenue.
Columbia, S.C., Federal Office Building, North West Corner College and Sumter Streets.
Aberdeen, S. Dak., Post Office and Court House Building, Fourth Avenue and Lincoln Street.
Nashville, Tenn., Federal Office Building, Eighth Avenue and Broad Street.
Austin, Tex., Lowich Building, 314 West 11th Street.
Dallas, Tex., Lynch Building, 2101 Pacific Avenue.
Salt Lake City, Utah, Federal Office Building, 350 South Main Street.
Burlington, Vt., Federal Office Building, 11 Elmwood Avenue.
Richmond, Va., Richmond Dry Goods Building, 11 South Seventh Street.
Seattle, Wash., Exchange Building, 109 Marion Street.
Parkersburg, W. Va., DILS Building, 211 Sixth Street.
Milwaukee, Wis., Federal Office Building, 517 East Wisconsin Avenue.
Cheyenne, Wyo., Federal Office Building, 21st and Carey Avenue.

APPENDIX B

Alcohol and Tobacco Tax Branch Offices

Birmingham, Ala., Seventeen Ten Building, 1710 First Avenue, North.
Little Rock, Ark., 555 Building.
Los Angeles, Calif., Subway Terminal Building, 417 South Hill Street.
San Francisco, Calif., 333 Fell Street.
Denver, Colo., New Customhouse Building, Room 188, 19th and California.
Hartford, Conn., American Industrial Building, 983 Main Street.
Jacksonville, Fla., Post Office and Courthouse Building, Suite 325–333, 311 West Monroe Street.
Atlanta, Ga., Federal Office Building, 275 Peachtree Street, Northeast.
Honolulu, Hawaii, Alexander Young Building, 1015 Bishop Street.
Chicago, Ill., State-Madison Building, 22 West Madison Street.
Louisville, Ky., Federal Office Building, 6th and Broadway.
Baltimore, Md., The 707 Building, 707 North Calvert Street.
Boston, Mass., Houghton-Dutton Building, 55 Tremont Street.
Detroit, Mich., Post Office and Courthouse Building, 231 West Lafayette Street.
St. Paul, Minn., Main Post Office Building and Customhouse, Room 1033, 180 East Kellogg Boulevard.
Jackson, Miss., Milner Building, Lamar and Pearl Streets.
Kansas City, Mo., Federal Office Building, Room 2509–10, 911 Walnut Street.
St. Louis, Mo., Court House and Customhouse Building, Room 738.
Omaha, Nebr., 704 Federal Office Building, 15th and Dodge Streets.
Newark, N.J., Industrial Office Building, 1060 Broad Street.
Buffalo, N.Y., Court House Building.
New York, N.Y., Greenwich Village Post Office Station, 641 Washington Street.
Charlotte, N.C., Post Office Building, Room 228, Corner West Trade and Mint Streets.
Cincinnati, Ohio, 474 Alms and Doepke Building, 222 East Central Parkway.
Oklahoma City, Okla., Sooner Building, 7 South Harvey Street.
Philadelphia, Pa., Room 500, U.S. Custom House, Second and Chestnut Streets.
Pittsburgh, Pa., Vistory Building, 212 Ninth Street.
San Juan, P.R., Post Office and Courthouse Building, Box 1601.
Columbia, S.C., Federal Office Building, Northwest Corner College and Sumter Streets.
Nashville, Tenn., Court House Building, 801 Broadway.
Dallas, Tex., Wholesale Merchants Building, 912 Commerce Street.
Richmond, Va., Parcel Post Building, 1100 East Main Street.
Seattle, Wash., Courthouse Building, Fifth and Madison.
Charleston, W. Va., Morrison Building, 815 Quarrier Street.
Milwaukee, Wis., Federal Office Building, 517 East Wisconsin Avenue.

APPENDIX C

APPELLATE BRANCH OFFICES

Birmingham, Ala., 6th Floor, The American Life Building, 2308 Fourth Avenue, North.
Los Angeles, Calif., Room 1250, Subway Terminal Building, 417 South Hill Street.
San Francisco, Calif., Room 1010, Flood Building, 870 Market Street.
Denver, Colo., 809 Central Bank Building, 1108 Fifteenth Street.
New Haven, Conn., 1221 Chapel Street.
Washington, D.C., Room 2547, Internal Revenue Service Building, 12th and Constitution Avenue NW.
Jacksonville, Fla., 405 P.O. and Court House Building.
Miami, Fla., 1005 Metropolitan Bank Building, 117 Northeast First Avenue.
Atlanta, Ga., Federal Office Building, 275 Peachtree Street Northeast.
Chicago, Ill., 17 North Dearborn Street.
Springfield, Ill., Modern Age Building, 405 East Washington Street.
Indianapolis, Ind., 510 Guaranty Building,
Wichita, Kans., Room 305, Insurance Building, 212 North Market Street.
Louisville, Ky., 410 Federal Building.
New Orleans, La., 444 Federal Office Building, 600 South Street.
Baltimore, Md., Room 626, 707 North Calvert Street.
Boston, Mass., 114 Federal Street.
Detroit, Mich., Room 900, Cadillac Tower,
St. Paul, Minn., W–981, First National Bank Building, 332 Minnesota Street.
Kansas City Mo., Room 1006, Federal Office Building, 911 Walnut Street.
St. Louis, Mo., 751 New Federal Building, 1114 Market Street.
Omaha, Nebr., U.S. Post Office and Court House, 215 North 17th Street.
Newark, N.J., Room 624, 1060 Broad Street.
Buffalo, N.Y., 330 U.S. Court House, Niagara Square.
New York, N.Y., 807 Federal Office Building, 90 Church Street.
Greensboro, N.C., Fifth Floor, 320 South Ashe Street.
Cincinnati, Ohio, 818 Enquier Building, 617 Vine Street.
Cleveland, Ohio, 410 Federal Reserve Bank Building.
Oklahoma City, Okla., 614 Sooner Building, 7 South Harvey Street.
Portland, Oreg., 425 Pittock Block, 921 Southwest Washington Street.
Philadelphia, Pa., 4th Floor, 2 Penn Center Plaza.
Pittsburgh, Pa., 2304 Clark Building, 7th and Liberty Avenue.
Nashville, Tenn., 654 New U.S. Court House Building, 801 Broadway.
Dallas, Tex., Room 1504, 1114 Commerce Street.
Houston, Tex., 10th Floor, State National Building, 412 Main Street.
Salt Lake City, Utah, Room 400, Tribune Building, 143 South Main Street.
Richmond, Va., 421 Post Office Building.
Seattle, Wash., 123 U.S. Court House Building.
Huntington, W. Va., Post Office Building, Ninth Street and Fifth Avenue.
Milwaukee, Wis., 530 Federal Building, 517 East Wisconsin Avenue.

(Filed by the Division of the Federal Register on July 14, 1961, 8:53 a.m., and published in the issue of the Federal Register for July 15, 1961, 26 F.R. 6372; appendixes A, B, and C filed by the Division of the Federal Register on November 27, 1961, 8:46 a.m., and published in the issue of the Federal Register for November 28, 1961, 26 F.R. 11219)

TREASURY DEPARTMENT ORDER 150–56

Internal Revenue Service—Change in office designation and establishment of new office.

1. *Establishment of new office.*—There is hereby established in the National Office of the Internal Revenue Service the office of Assistant Commissioner (Data Processing).

2. *Change in designation of office.*—The office designated as Assistant Commissioner (Operations) by Treasury Department Order No.

150–5, July 29, 1952, is hereby designated Assistant Commissioner (Compliance).

Dated September 15, 1961.

[SEAL] DOUGLAS DILLON,
Secretary of the Treasury.

(Filed by the Division of the Federal Register on September 21, 1961, 8:49 a.m., and published in the issue of the Federal Register for September 22, 1961, 26 F.R. 8953)

Commissioner of Customs—Collection of tobacco taxes; delegation of authority.

TREASURY DEPARTMENT ORDER 165–12

By virtue of the authority vested in the Secretary of the Treasury by Reorganization Plan No. 26 of 1950 (3 CFR, 1950 Supp., Ch. III), and pursuant to authorization given to me by Treasury Department Order No. 190 (26 F.R. 7019), there are transferred from the Commissioner of Internal Revenue and delegated to the Commissioner of Customs the functions of collecting the taxes imposed on tobacco materials, tobacco products, and cigarette papers and tubes imported or brought into the United States on which internal-revenue taxes under section 5701 and section 7652 of the Internal Revenue Code, as amended, are due and payable at the time of release from customs custody in accordance with the method prescribed by regulations of the Internal Revenue Service.

It is hereby ordered that the provisions of Treasury Department Order No. 165–2 (18 F.R. 7177) and Amendment 1 thereof (24 F.R. 1991) C.B. 1959–1, 767, are applicable to refunds of such collections.

The functions herein delegated to the Commissioner of Customs may be delegated by him to subordinates in such manner as he shall direct.

This order shall be effective October 1, 1961.

[SEAL] HENRY H. FOWLER,
Under Secretary of the Treasury.

(Filed by the Division of the Federal Register on September 5, 1961, 8:48 a.m., and published in the issue of the Federal Register for September 6, 1961, 26 F.R. 8400)

DELEGATION ORDER NO. 83
(Effective October 16, 1961)

Delegation of authority to permit inspection of returns and related documents.

Pursuant to authority vested in me by Treasury Decision 6543, approved by the President January 17, 1961, [C.B. 1961–1, 671]. District Directors, the Director of International Operations, and the Director of the Collection Division are authorized:

1. To permit inspection of returns in their custody by any applicant eligible therefor in accordance with paragraph (c) of section 301.6103(a)–1 of Treasury Decision 6543, including any applicant with respect to whom inspection is made discretionary with the

Secretary or the Commissioner or the delegate of either, provided such applicant meets the requirements embodied by such paragraph. The authority delegated in this paragraph of this order is limited to returns as filed by or on behalf of the taxpayer, including any schedules, lists and other written statements which have been filed with the Internal Revenue Service by or on behalf of the taxpayer or which have previously been furnished by the Service to the taxpayer.

2. To permit inspection of returns in their custody by United States attorneys and attorneys of the Department of Justice in accordance with paragraph (g) of section 301.6103(a)-1 of Treasury Decision 6543, and to furnish returns, or copies, thereof, to such attorneys in accordance with paragraph (h) of such section. The authority delegated in this paragraph of this order is limited to returns as filed by or on behalf of the taxpayer, including any schedules, lists and other written statements which have been filed with the Internal Revenue Service by or on behalf of the taxpayer or which have previously been furnished by the Service to the taxpayer, except that other records or reports containing information included or required by statute to be included in the return may be furnished (a) when the return or copy thereof is requested for official use in the prosecution of claims and demands by, and offenses against, the United States, or the defense of claims and demands against the United States or officers and employees thereof, in cases arising under the internal revenue laws or related statutes which were referred by the Department of the Treasury to the Department of Justice for such prosecution or defense, or (b) in cases not so referred when so authorized by the Assistant Commissioner (Compliance).

The authority delegated herein may not be redelegated.

WILLIAM H. LOEB,
Acting Commissioner.

(Filed by the Division of the Federal Register on October 31, 1961, 8:52 a.m., and published in the issue of the Federal Register for November 1, 1961, 26 F.R. 10241)

TITLE 26—INTERNAL REVENUE.—CHAPTER I, SUBCHAPTER H, PART 601.—STATEMENT OF PROCEDURAL RULES[1]

This part as filed with the Federal Register on June 29, 1955 [C.B. 1955-1, 921], and as last amended on December 28, 1960 [C.B. 1961-1, 866], is further amended by revising paragraph (b)(1)(ii) of § 601.702 to read as follows:

§ 601.702 PUBLICATION AND PUBLIC INSPECTION.

* * * * * * *

(b) *Final opinions and orders.*— * * *

(1) *Accepted offers in compromise.*— * * *

(ii) *Liquors.*—For each offer in compromise submitted and accepted on or after August 1, 1961, pursuant to section 7122 of the Code in any case arising under chapter 51 of the Code, or pursuant to section 7 of the Federal Alcohol Administration Act in any case arising under that Act, a copy of the abstract and statement relating to the offer shall be available for public inspection for a period of one year from the date of acceptance. Copies of abstracts and statements covering offers accepted pursuant to the Code may be inspected in the

[1] 26 F.R. 6813.

office of the assistant regional commissioner (alcohol and tobacco tax) who received the offer or in the office of the district director for the internal revenue district in which the offer was submitted. Copies of abstracts and statements covering offers accepted pursuant to the Federal Alcohol Administration Act may be inspected in the office of the assistant regional commissioner (alcohol and tobacco tax) who received the offer. Information, however, is not disclosed concerning any trade secrets, processes, operations, style of work, or apparatus, or confidential data, amount or source of income, profits, losses, or expenditures, or any other matter within the prohibition of section 1905 of Title 18 of the United States Code. (R.S. 161; 5 U.S.C. 22.)

JOHN W. S. LITTLETON,
Acting Commissioner of Internal Revenue.

(Filed by the Division of the Federal Register on July 28, 1961, 8:53 a.m., and published in the issue of the Federal Register for July 29, 1961, 26 F.R. 6813)

(Also Part I, Section 819; 26 CFR 1.819–2.) T. D. 6567[1]

TITLE 26—INTERNAL REVENUE.—CHAPTER I, SUBCHAPTER A, PART 1.—INCOME TAX; TAXABLE YEARS BEGINNING AFTER DECEMBER 31, 1953

Percentage to be used by foreign life insurance companies in determining the "minimum figure" under section 819(b) of the Internal Revenue Code of 1954, for purposes of computing declaration of estimated income tax for the taxable year 1961.

DEPARTMENT OF THE TREASURY,
Washington 25, D.C.

To Officers and Employees of the Treasury Department and Others Concerned:

Section 819(b) of the Internal Revenue Code of 1954, as added by the Life Insurance Company Income Tax Act of 1959 (73 Stat. 136) [P.L. 86–69, C.B. 1959–2, 654], provides for the determination of a percentage to be used in determining a "minimum figure" for each foreign life insurance company described in section 819(a). Where this minimum figure exceeds the foreign life insurance company's surplus held in the United States, the amount of the "policy and other contract liability requirements" (determined under section 805 without regard to section 819(b)), and the amount of the "required interest" (determined under section 809(a) without regard to section 819(b)), must each be reduced by an amount determined by multiplying such excess by the "current earnings rate" (as defined in section 805(b)(2)). In view of the extensions granted to many domestic life insurance companies to file their 1960 returns, it will not be possible to compute the percentage required by section 819(b) prior to the expiration of the date for the filing of the declaration of estimated income tax for the taxable year 1961. Accordingly, it is hereby determined that for purposes of the declaration of estimated 1961 income tax and payments of installments thereof by foreign life insurance companies, a percentage of 14.3 (the percentage applicable for 1960) shall be used in determining the minimum figure under section 819(b). No additions to tax shall be made because of any underpayment of tax which results solely from the use of this percentage.

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[1] 26 F.R. 7263.

Because the public cannot effectively participate in the determination of the percentage announced in this Treasury Decision, 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 such Act.

STANLEY S. SURREY,
Assistant Secretary of the Treasury.

August 8, 1961.

(Filed by the Division of the Federal Register on August 10, 1961, 8:53 a.m., and published in the issue of the Federal Register for August 11, 1961, 26 F.R. 7263)

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26 CFR 601.301: Imposition of taxes, qualification requirements, and regulations.
(Also Part III–A, Sections 5204, 5207, 5212; 201.269, 201.368, 201.628.)

Rev. Proc. 61–16

Procedures are prescribed for proprietors of distilled spirits plants respecting the gauge of packages of spirits found to have sustained a loss for which a claim for remission is or may be required, and the recording of such loss in the warehouse records and reports.

Revenue Procedure 61–9, C.B. 1961–1, 894, superseded.

SECTION 1. PURPOSE.

The purpose of this Revenue Procedure is to set forth warehouse recordkeeping procedures when a claim for remission of tax on spirits lost from packages is required and the packages are to remain in bonded storage.

SEC. 2. BACKGROUND.

Under the provisions of sections 201.309 and 201.311 of the Distilled Spirits Plant Regulations, the Assistant Regional Commissioner, Alcohol and Tobacco Tax, may require the proprietor of bonded warehouse facilities of a distilled spirits plant to file claim for relief from the tax on spirits lost or destroyed in bond, whether by theft or otherwise, and such tax on the quantity of spirits lost may be remitted or paid.

SEC. 3. PROCEDURE.

Where a package of spirits in bond is found to have sustained a loss for which a claim for remission of tax is or may be required the procedure set forth below shall be followed:

.01 The proprietor shall prepare Form 2630, Package Gauge Report, reporting the gauge made to determine the quantity of spirits lost. A copy of the report shall be furnished the assigned officer for his information and files.

.02 When the tax on such loss is remitted or paid, the proprietor shall note in the right-hand column of the appropriate deposit record required by section 201.628 of the regulations the gross weight, tare (if determined), and proof, ascertained at the time of the gauge to determine the loss, and the date of such gauge.

.03 No adjustment for such a loss shall be made in the summary of deposits and withdrawals, Form 1621, required by section 201.629 of the regulations. However, any taxpaid losses shall be recorded at line 26 only of Form 2731, Monthly Report of Bonded Storage Operations, for the month in which the taxpayment is made. Footnote three on Form 2731 will be appropriately amended when the form is next reprinted.

.04 In the event such a package is transferred in bond, the provisions of section 201.368(b) of the regulations shall be followed. Accordingly, the gross weight and the tare ascertained at the time of the gauge to determine the loss shall be reported in columns (c) and (f), respectively, of the Form 2630 covering the transfer. If such package is weighed at the time of shipment, the shipping weight shall be recorded in column (k) and no entry shall be made in column (c) unless the package has been filled for withdrawal on the original gauge as provided in section 201.269. In addition, the date of the loss gauge and the proof ascertained shall be recorded in column (o) where a reduction in proof was a factor in the loss determination or where the package is not weighed at the time of shipment.

SEC. 4. EFFECT ON OTHER DOCUMENTS.

Revenue Procedure 61–9, C.B. 1961–1, 894, is hereby superseded.

SEC. 5. INQUIRIES.

Inquiries regarding this Revenue Procedure should refer to its number and be addressed to the appropriate office of the Assistant Regional Commissioner, Alcohol and Tobacco Tax.

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26 CFR 601.301: Imposition of taxes, qualification requirements, and regulations. (Also Part III–A, Sections 5006, 5025, 5201, 5234; 201.270, 201.297, 201.301, 201.303, 201.307.)

Rev. Proc. 61–17

The latest date of original packaging of spirits mingled or blended under the Distilled Spirits Plants Regulations shall be entered on deposit and withdrawal forms covering such spirits in lieu of, or in addition to, the date of original entry into bond of the youngest spirits.

SECTION 1. PURPOSE.

The purpose of this Revenue Procedure is to outline the procedure to be followed in determining and recording on deposit and withdrawal forms the date from which age statements may be established when spirits are mingled under section 201.297 of the Distilled Spirits Plants Regulations and mingled to consolidate packages under section 201.301, or blended under section 201.307 of the regulations.

SEC. 2. BACKGROUND.

.01 Section 201.270 of the regulations permits a proprietor of a distilled spirits plant to enter spirits into bonded storage for subsequent packaging in wooden packages.

.02 Section 201.303 of the regulations provides, in part, that when packages of spirits are mingled as provided in section 201.297, or blended as provided in section 201.307 of the regulations, the date

of original entry of the oldest spirits mingled shall be the date of original entry for the entire lot; the appropriate deposit and withdrawal forms, however, shall show the date of original entry of the oldest and the youngest spirits in the lot. Section 201.303 of the regulations also provides that when spirits are mingled under section 201.301, the date of original entry for the entire lot shall be the date of original entry of the youngest spirits mingled.

SEC. 3. PROCEDURE.

.01 Whenever spirits are entered into bond under section 201.270 of the regulations and subsequently packaged in wooden packages, then later mingled under section 201.297 or blended under section 201.307 of the regulations, the deposit and withdrawal forms covering the mingled spirits shall, for force-out purposes, show the earliest date of original entry into bond of any of the spirits mingled. If the date of original packaging of any of the spirits is later than the latest date of original entry into bond of any of the spirits mingled, the latest date of original filling of any of the spirits into wooden packages (regardless of the dates of original entry into bond) shall be entered on the deposit and withdrawal forms; in such instances this date shall be entered in lieu of the date of original entry into bond of the youngest spirits.

.02 Whenever spirits are entered into bond under section 201.270 of the regulations and subsequently packaged in wooden packages, then later mingled to consolidate packages under section 201.301 of the regulations, the deposit and withdrawal forms covering the mingled spirits shall, for force-out purposes, show the latest date of original entry into bond of any of the spirits mingled. If the date of original packaging of any of the spirits is later than the latest date of original entry into bond of any of the spirits mingled, the latest date of packaging, from which age statements may be established, shall also be shown.

SEC. 4. INQUIRIES.

Inquiries concerning this Revenue Procedure should refer to its number and be addressed to the office of the appropriate Assistant Regional Commissioner, Alcohol and Tobacco Tax.

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26 CFR 601.103: Summary of general tax procedure. Rev. Proc. 61–18

(Also Part I, Section 6212; 301.6212-2.)

In general, it will be the Internal Revenue Service practice to regard the address of the taxpayer's duly authorized representative as constituting the last known address of the taxpayer within the meaning of section 6212(b) of the Internal Revenue Code of 1954 in cases where, subsequent to the date on which he files a return for the taxable year, or concurrently with such filing, the taxpayer files a power of attorney with the Internal Revenue Service which authorizes the designated attorney to represent him and requests that *all* communications concerning his tax matters with regard thereto, or concerning a proposed deficiency in tax for that taxable year, be mailed to his attorney at his attorney's address. See *Mary Jo Williams, Administrator*, v. *United States*, 264 Fed. (2d) 227 (1959)

certiorari denied, 361 U.S. 862, and *Marjorie F. Birnie* v. *Commissioner*, 16 T.C. 861 (1951).

Under different facts and circumstances, a determination as to what is the taxpayer's last known address will still be made on the basis of the particular facts involved, the requirements of section 6212(b) of the Code and the applicable case law. For example, in cases in which the power of attorney directs that "a copy of all communications" addressed to the taxpayer be sent the named attorney. The Tax Court of the United States has held that a notice sent directly to the taxpayer by registered mail at his last known address will give the Tax Court jurisdiction upon the filing of a timely petition. *Draper Allen et ux.* v. *Commissioner*, 29 T.C. 113 (1957). Compare *Clement Brzezinski et al.* v. *Commissioner*, 23 T.C. 192 (1954).

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26 CFR 601.401: Employment taxes. (Also Part I, Sections 1402, 3121; 31.3121(b)(8)–2.)

Rev. Proc. 61–19

Procedures to be followed so that remuneration received by certain lay missionaries or other individuals, on which amounts have been erroneously paid as tax under the Self-Employment Contributions Act of 1954, may be deemed to constitute net earnings from self-employment.

SECTION 1. PURPOSE.

The purpose of this Revenue Procedure is to set forth conditions and procedures under which remuneration received by certain lay missionaries or other individuals on which amounts have been erroneously paid as tax under section 1401 of the Self-Employment Contributions Act of 1954 (chapter 2, subtitle A, Internal Revenue Code of 1954) may be deemed to constitute net earnings from self-employment.

SEC. 2. BACKGROUND.

Section 1402(g) of the Self-Employment Contributions Act of 1954, as added by the Social Security Amendments of 1960, Public Law 86–778, C.B. 1960–2, 693, provides that, under certain circumstances, remuneration will be deemed to constitute net earnings from self-employment if (1) the remuneration was or is received by an individual for services performed as an employee of a nonprofit educational, charitable, religious, etc., organization exempt from income tax as an organization described in section 501(c)(3) of the Code (other than service performed as a duly ordained, commissioned, or licensed minister of a church in the exercise of his ministry or as a member of a religious order in the exercise of duties required by such order), and (2) the remuneration was or is erroneously reported by the individual as self-employment income on a return for any taxable year ending after 1954 and before 1962.

SEC. 3. PREREQUISITES TO VALIDATION.

The remuneration described above will be "validated" as net earnings from self-employment if the following conditions are met:

(1) A statement requesting such validation is filed after September 13, 1960, and on or before April 16, 1962, (1) by the

individual or by a fiduciary acting for him or (2) if he is deceased, by a fiduciary acting for his estate, or by his spouse, former wife divorced, child or parent, who survives him;

(2) The nonprofit organization, which paid the remuneration erroneously reported as self-employment income, has filed Form SS–15, Certificate Waiving Exemption From Taxes Under The Federal Insurance Contributions Act, on or before the date the request is filed;

(3) The remuneration for any taxable year for which validation is requested has been reported as self-employment income on a return filed on or before the due date prescribed for filing such return, including any extension thereof, and the tax thereon has been paid;

(4) No credit or refund of any portion of the amount erroneously paid for such taxable year as self-employment tax under section 1401 of the Self-Employment Contributions Act (other than a credit or refund which would be allowable if such tax were applicable with respect to such remuneration) has been obtained before the date on which such request is filed or, if obtained, the amount credited or refunded (including any interest under section 6611 of the Code) has been repaid on or before such date; and

(5) No tax (other than an amount erroneously paid as tax) has been paid under the Federal Insurance Contributions Act (chapter 21, subtitle C, of the Code) with respect to such remuneration.

SEC. 4. REQUEST FOR VALIDATION.

(1) No particular form is prescribed for making a request under section 1402(g) of the Self-Employment Contributions Act. In general, the statement requesting validation should be made and filed as provided herein.

(2) The statement requesting validation should be in writing, should be signed and dated by the person making the request, and should include the following:

a. The name, address, and social security account number of the individual with respect to whose remuneration the request is made;

b. A request that, pursuant to section 1402(g) of the Act, such remuneration for one or more specified years (ending after 1954 and before 1962) be deemed to constitute net earnings from self-employment and not remuneration for employment;

c. A statement that the remuneration was erroneously reported as self-employment income on the individual's return for each year specified and that the return was filed on or before the due date (including any extension thereof);

d. Identification of the office of the District Director of Internal Revenue where each return was filed;

e. A statement that no portion of the amount erroneously paid by the individual as self-employment tax with respect to the remuneration has been credited or refunded (other than a credit or refund which would be allowable if the tax were applicable with respect to the remuneration); or, if a credit or refund of any

portion of such amount has been obtained, a statement identifying the refund or credit and showing how and when the amount credited or refunded, together with any interest received in connection therewith, was repaid by the taxpayer to the Government;

f. The name and address of the organization which paid the remuneration to the individual;

g. The date on which the organization filed a waiver certificate on Form SS–15, and identification of the District Director's office where it was filed; and

h. The date on which the certificate became effective with respect to services performed by the individual.

(3) If the request is made by any person other than the individual to whom the remuneration was paid (for example, by a fiduciary or a survivor), the request should show the name and address of that person and should be accompanied by evidence, or an explanation in writing, of such person's authority to make the request.

(4) The request should be filed with the District Director of Internal Revenue with whom the latest of the returns, referred to in paragraph (2)c of this section, was filed.

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26 CFR 601.602: Forms and instructions. (Also Part I, Sections 3201, 3211, 3221; 31.3201–1, 31.3211–1, 31.3221–1.) Rev. Proc. 61–20

Computation of employer tax, employee tax, and employee representative tax imposed under the Railroad Retirement Tax Act, with respect to compensation paid for services rendered after 1936 and before June 1, 1959.

Revenue Procedure 58–3, C.B. 1958–1, 685, superseded, with respect to compensation paid after 1961.

SECTION 1. PURPOSE.

The purpose of this Revenue Procedure is to provide instructions for the computation of employer tax and employee tax to be reported on Form CT–1, Employer's Quarterly Railroad Retirement Tax Return, and employee representative's tax to be reported on Form CT–2, Employee Representative's Quarterly Railroad Retirement Tax Return, under the Railroad Retirement Tax Act (chapter 22, subtitle C, Internal Revenue Code of 1954), with respect to compensation paid after 1961 for services rendered after 1936 and before June 1, 1959.

SEC. 2. BACKGROUND.

The January 1962 revision of Form CT–1 and Form CT–2 will provide entry spaces and rates for computing tax with respect to compensation for services performed after May 31, 1959. Because of the infrequency of payments of compensation for services rendered before June 1, 1959, the forms will not provide a schedule for computation of tax with respect to such compensation. Instead, a single entry line will be provided for the reporting of such tax, which may be computed by reference to this Revenue Procedure. See section 10 of this Procedure, however, relating to the reporting of employee representative tax with respect to compensation earned before 1947.

SEC. 3. COMPUTATION OF EMPLOYER TAX AND EMPLOYEE TAX.

The schedule shown below is provided as a guide for computing the employer tax and employee tax applicable to compensation paid for services rendered after 1936 and before June 1, 1959.

1. Computation of employee tax on compensation for services rendered before June 1, 1959:

Period in which compensation, paid during quarter, was earned (a)	Compensation paid during quarter for such services, subject to employee tax (b)	Rate of employee tax on such compensation (c)	Amount of employee tax (col. (b)×col. (c)) (d)
January 1, 1947 through May 31, 1959	$	6¼ percent	$
Calendar year 1946	$	3½ percent	$
Calendar years 1943, 1944, and 1945	$	3¼ percent	$
Calendar years 1940, 1941, and 1942	$	3 percent	$
Calendar years 1937, 1938, and 1939	$	2¾ percent	$
Totals	$	x x x x x x	$

2. Compensation, subject to employer tax paid during quarter for services rendered after 1936 and before June 1, 1959	$	
3. Employer tax (6¼ percent of line 2)		$
4. Employee tax (total of column (d), above)	$	
5. Total taxes (line 3 plus line 4) (Enter on Form CT–1 and attach explanation, in duplicate)		$

(NOTE.—If the total of column (b) differs from the amount in line 2, include in the explanation a statement of the computations which cause the amounts to be different. See sections 6 and 7, below.)

SEC. 4. EMPLOYEE TAX AND EMPLOYER TAX WITH RESPECT TO COMPENSATION EARNED AFTER JUNE 30, 1954, AND BEFORE JUNE 1, 1959.

The employee tax and employer tax apply to compensation not in excess of $350 for services rendered in any calendar month beginning after June 30, 1954, and ending before June 1, 1959. If an employee is paid total compensation of more than $350 by two or more employers for services rendered in any such month, the amount of compensation subject to tax should be computed in accordance with the rules stated in paragraph G of the instructions relating to Form CT–1 (except that the tax does not apply to compensation in excess of $350 for such services).

SEC. 5. EMPLOYEE TAX AND EMPLOYER TAX WITH RESPECT TO COMPENSATION EARNED AFTER 1946 AND BEFORE JULY 1, 1954.

The employee tax and employer tax apply to compensation not in excess of $300 for services rendered in any calendar month beginning after 1946 and ending before July 1, 1954. If an employee is paid compensation of more than $300 by two or more employers for services rendered in any such month, the amount of compensation sub-

ject to tax should be computed in accordance with the rules stated in paragraph G of the instructions relating to Form CT–1 (except that the tax does not apply to compensation in excess of $300 for such services).

SEC. 6. EMPLOYEE TAX WITH RESPECT TO COMPENSATION EARNED BEFORE 1957.

The employee tax imposed by section 2(a) of the Carriers Taxing Act of 1937, 45 U.S.C. 261, and by section 1500 of the Internal Revenue Code of 1939 prior to its amendment by the Act of July 31, 1946, Public Law 572, 79th Cong., C.B. 1946–2, 269, applies to compensation, not in excess of $300, earned by an employee from one or more employers in a calendar month before 1947. If an employee earned compensation of more than $300 in a calendar month before 1947, only $300 thereof is subject to the employee tax irrespective of the year or years in which such compensation is paid to the employee. If an employee earned compensation from two or more employers in a calendar month before 1947, and if the aggregate compensation paid (at any time) to such employee by all employers is more than $300 for such calendar month, each employer must report and pay employee tax with respect to that proportion of $300 which such employer's payment to the employee bears to the aggregate compensation paid (at any time) to such employee by all of his employers for that calendar month.

SEC. 7. EMPLOYER TAX WITH RESPECT TO COMPENSATION EARNED BEFORE 1947.

The employer tax applies to compensation, not in excess of $300, paid to an employee after 1946 by one or more employers for services rendered in any calendar month before 1947. The amount of such compensation which is subject to employer tax must be computed without regard to any payment made to the employee before 1947 by such employer or by any other employer. If an employee is paid total compensation of more than $300 after 1946 by two or more employers for services rendered in a calendar month before 1947, the amount of such compensation which is subject to employer tax should be computed by each employer in accordance with the rules stated in paragraph G of the instructions relating to Form CT–1 (except that the employer tax does not apply to compensation in excess of $300 for such services).

It should be noted that the amount of compensation, if any, subject to employee tax (column (b) in section 3, above) generally will be less than the amount of compensation subject to employer tax (line 2 in section 3, above) for the reason that the latter amount must be computed without regard to compensation paid to the employee before 1947.

SEC. 8. AMOUNT OF COMPENSATION, FOR SERVICES RENDERED BEFORE JUNE 1, 1959, WITH RESPECT TO WHICH EMPLOYEE REPRESENTATIVE TAX IS IMPOSED.

The employee representative tax applies to the amount of compensation for services rendered as an employee representative which does not exceed the monthly maximum of $350 earned in any calendar month after June 30, 1954, and before June 1, 1959, and $300 earned

in any calendar month after 1936 and before July 1, 1954. If in any calendar month an individual renders services as an employee representative and as an employee and if the total compensation paid to him for such services exceeds the monthly maximum ($350 or $300, as the case may be), the measure of the employee representative tax is the monthly maximum minus the compensation paid to him for services rendered during the month as an employee.

SEC. 9. EMPLOYEE REPRESENTATIVE TAX WITH RESPECT TO COMPENSATION EARNED AFTER 1946 AND BEFORE JUNE 1, 1959.

Employee representative tax is imposed at the rate of 12½ percent with respect to compensation paid for services rendered as an employee representative after 1946 and before June 1, 1959. See section 8 of this Procedure. The amount of such tax should be reported on the employee representative's return on Form CT–2 for the calendar quarter in which the compensation is paid.

SEC. 10. EMPLOYEE REPRESENTATIVE TAX WITH RESPECT TO COMPENSATION EARNED BEFORE 1947.

Employee representative tax with respect to compensation paid for services rendered as an employee representative in any calendar quarter beginning after 1936 and ending before 1947 should be reported on a return on Form CT–2 for such calendar quarter and not on the Form CT–2 for the quarter in which the compensation is paid. See section 8 of this Procedure. If a return on Form CT–2 was filed for the calendar quarter in which the compensation was earned, any subsequent payment of compensation earned in such quarter should be reported on a return on Form CT–2 which is marked "Amended" and which is altered to show the applicable rate of tax. The rates of employee representative tax applicable with respect to compensation paid for services rendered before 1947 as an employee representative are as follows:

Calendar year or years in which compensation was earned	*Rate of employee representative tax*
1946	7 percent
1943, 1944, and 1945	6½ percent
1940, 1941, and 1942	6 percent
1937, 1938, and 1939	5½ percent

SEC. 11. EFFECT ON OTHER DOCUMENTS.

Revenue Procedure 58–3, C. B. 1958–1, 685, which contains instructions for the computation of employer tax and employee tax to be reported on Form CT–1, Employer's Railroad Retirement Tax Return, with respect to compensation paid for services rendered after 1936 and before 1947, is hereby superseded, with respect to compensation paid after 1961.

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26 CFR 601.301: Imposition of taxes, qualification requirements, and regulations.
(Also Part III–A, Sections 5207, 5555; 201.6333.)

Rev. Proc. 61–21

Pending revision of Form 2730 (7–60), Monthly Report of Production Operations, imported spirits received at production facilities of distilled spirits plants, for redistillation, shall be specifically identified and separately reported commencing with the report on Form 2730 for July 1961.

SECTION 1. PURPOSE.

The purpose of this Revenue Procedure is to advise proprietors of distilled spirits plants that, pending revision of Form 2730 (7–60), Monthly Report of Production Operations, imported spirits received at their production facility, for redistillation, shall be specifically identified and separately reported on Form 2730, commencing with the report for July 1961.

SEC. 2. BACKGROUND.

Instructions of Form 2730 do not require that imported spirits received for redistillation be identified as such and separately reported. Separate reporting of such information on Form 2730 is necessary for statistical purposes.

SEC. 3. PROCEDURE.

.01 Imported spirits received at the production facility of a distilled spirits plant, for redistillation, shall be specifically identified and separately reported at line 16, section I, of Form 2730, and any such spirits on hand at the end of the month shall likewise be reported by interlining at line 17(a), section I, of Form 2730.

.02 The quantities of imported spirits used for redistillation shall be specifically identified and separately reported in sections II and IV of Form 2730.

SEC. 4 INQUIRIES.

Inquiries in regard to this Revenue Procedure should refer to its number and be addressed to the office of the appropriate Assistant Regional Commissioner, Alcohol and Tobacco Tax.

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26 CFR 601.301: Imposition of taxes, qualification requirements, and regulations.
(Also Part III–B, Section 5(e); 27 CFR 4.45.)

Rev. Proc. 61–22

Portuguese Moscatel De Setubal and port wine shipped from the Republic of Portugal to the United States on and after July 15, 1961, must be accompanied by appropriate certificates of origin and identity issued under the authority of the Portuguese Government. In addition, Vintage Port must be accompanied by a certificate of authenticity of vintage date.

SECTION 1. PURPOSE.

The purpose of this Revenue Procedure is to inform importers of Portuguese Moscatel De Setubal and port wine that such wines shipped from foreign ports, on and after July 15, 1961, must be accompanied by appropriate certificates of origin and identity. In addition, in the case of Vintage Port, a certificate of authenticity of vintage date issued under the authority of the Portuguese Government must accompany the goods.

SEC. 2. BACKGROUND.

Section 4.45 of the Federal Labeling and Advertising of Wine Regulations, under the Federal Alcohol Administration Act, provides in part that imported wines shall not be released from Customs cus-

tody for consumption unless the invoice is accompanied by a certificate of origin issued by a duly authorized official of the appropriate foreign government, if the issuance of such certificates with respect to such wines has been authorized by the foreign government concerned. Revenue Procedure 59–9, C.B. 1959–1, 818, informed importers of wine of the provisions of the regulations regarding certificates of origin and identity and certificates of authenticity of vintage dates for bottled imported wines. Revenue Procedure 59–32, C.B. 1959–2, 951, described the type and form of certificate required of wines bottled in countries other than the country of origin.

SEC. 3. CONCLUSION.

.01 Under Portuguese law the "Institute Do Vinho Do Porto" and the "Uniao Vinicola Da Regiao Do 'Moscatel De Setubal'" are authorized to issue the "Certificado de origem de Vinho Do Porto" and the "Certificado de origem de Vinho 'Moscatel De Setubal'" to cover the respective wines exported from Portugal. In addition to a verification of origin and identity, the Certificado de origem de Vinho Do Porto will attest to the accuracy of any vintage date which may appear on the labels for port wine.

.02 If these wines are shipped in bulk to other countries for bottling prior to shipment to the United States, they must be covered by appropriate certification before such wines may be released from Customs custody. For example, if port wine is shipped from Portugal, in bulk, to England for bottling, the bottled wine, if exported to the United States, must be covered by an appropriate certificate issued by the office of British Customs and Excise which will be accepted by United States Customs officers in place of the original Portuguese certificates described above.

.03 In order to avoid detention of merchandise at the ports of entry, all importers of port wine and Moscatel De Setubal should advise their principals abroad of these provisions.

SEC. 4. INQUIRIES.

Correspondence in regard to this Revenue Procedure should refer to its number and be addressed to the Director, Alcohol and Tobacco Tax, Internal Revenue Service, Washington, D.C., attention O:AT:B.

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26 CFR 601.301: Imposition of taxes, qualification requirements, and regulations.
(Also Part III–A, Sections 5207; 201.629)

Rev. Proc. 61–23

Recording and reporting warehouse transactions respecting spirits entered into bonded storage at a proof of 190 degrees or more and subsequently reduced in bonded storage below 190 degrees or spirits having a proof of less than 190 degrees and increased through mingling in bonded storage to 190 degrees or more.

Revenue Procedure 61–2, C.B. 1961–1, 887, modified.

SECTION 1. PURPOSE.

This Revenue Procedure outlines procedures to be followed by proprietors of distilled spirits plants (a) in recording and reporting

warehouse transactions respecting spirits of 190 degrees or more of proof which are reduced below 190 degrees, and spirits of less than 190 degrees of proof which are increased to 190 degrees or more through mingling in bonded storage, and (b) in making adjusting entries necessitated by the provisions of Revenue Ruling 61–166, page 267, this Bulletin, in warehouse records and reports.

SEC. 2. BACKGROUND.

.01 Revenue Ruling 60–381, C.B. 1960–2, 509, held that the bonding period limitation in section 5006(a)(2) of the Internal Revenue Code of 1954 did not apply to spirits entered into bonded storage at 190 degrees or more of proof even though such spirits were subsequently reduced below 190 degrees of proof. The Internal Revenue Service has found this ruling untenable in light of the specific language of section 5006(a)(2) of the Code. Accordingly, the Service revoked Revenue Ruling 60–381 by issuing Revenue Ruling 61–166 which holds that the exemption in section 5006(a)(2)(B)(i) of the Code from the bonding period limitation applies only to spirits which are, in fact, "of 190 degrees or more of proof." See page 267 of this Bulletin. Therefore, if spirits entered into storage at 190 degrees or more of proof are reduced, in bonded storage, below 190 degrees of proof, they immediately become subject to the bonding period limitation.

.02 On the basis of the revoked ruling, spirits entered into bonded storage at a proof of 190 degrees or more and subsequently reduced below 190 degrees were recorded in the summary accounts on Form 1621, Summary of Deposits and Withdrawals at Bonded Warehouses, as though they were 190 degrees or more of proof and exempt from the bonding period limitations. Now, on the basis of Revenue Ruling 61–166, all spirits which are, in fact, of less than 190 degrees of proof must be recorded as such in the summary accounts according to producer, and year and season of production. See section 201.629 of the Distilled Spirits Plants Regulations.

SEC. 3. RECORD REQUIREMENTS.

.01 When spirits having a proof of 190 degrees or more are reduced in bonded storage below 190 degrees, or spirits having a proof of less than 190 degrees are increased through mingling in bonded storage to 190 degrees or more, the proprietor shall make appropriate entries in his summary accounts on Form 1621 to reflect such transactions. Where spirits not subject to the bonding period limitation become subject thereto through reduction in proof, the proprietor shall, as provided in Revenue Ruling 61–166, consider the date of reduction as the date of original entry.

.02 If any spirits of less than 190 degrees of proof are currently carried in the proprietor's summary records as though they are 190 degrees or more of proof and not subject to the bonding period limitation, the proprietor shall transfer such spirits from the account in which they are now erroneously carried to the appropriate producer's and season's accounts required by section 201.629 of the regulations. The proprietor shall notify the assigned officer, in writing, of the quantities of spirits transferred between accounts as provided in this subsection.

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SEC. 4. REPORT REQUIREMENT.

.01 The proprietor shall continue to report in column (g) of Form 2731, Monthly Report of Bonded Storage Operations, transactions in alcohol and spirits which are, in fact, of 190 degrees or more of proof. Transactions in alcohol and spirits which are, in fact, of less than 190 degrees of proof shall be reported in column (h) of the form.

.02 Whenever any adjusting entries prescribed by subsection 3.01 above are required in the summary accounts, the proprietor shall also make appropriate credit and debit entries at lines 5 and 19 in columns (g) and (h) of Form 2731, with descriptive entries in column (a).

.03 Similarly, appropriate credit and debit entries shall be made on Form 2731 to record the transfer of spirits of less than 190 degrees of proof to the proper account as provided in subsection 3.02 above.

SEC. 5. EFFECT ON OTHER DOCUMENTS.

Revenue Procedure 61–2, C.B. 1961–1, 887, is hereby modified to remove therefrom those procedures which relate to Form 2731.

SEC. 6. INQUIRIES.

Inquiries regarding this Revenue Procedure should refer to its number and be addressed to the office of the appropriate Assistant Regional Commissioner, Alcohol and Tobacco Tax.

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26 CFR 601.301: Imposition of taxes, qualification requirements, and regulations. (Also Part III–A, Sections 5053, 5062, 5214, 5362; 245.170, 252.23, 240.670.)

Rev. Proc. 61–24 [1]

Pakistan and Venezuela have been added to the list of countries to which has been extended the privilege of withdrawing alcohol, distilled spirits, beer, and wine free of tax or with benefit of drawback for use as supplies on aircraft.

Revenue Procedure 61–13, C.B. 1961–1, 900, superseded.

SECTION 1. PURPOSE.

The purpose of this Revenue Procedure is to announce the addition of Pakistan and Venezuela to the list of foreign countries to which the reciprocal privileges provided by section 309 of the Tariff Act of 1930, as amended, 46 Stat. 690, as amended, 19 U.S.C. 1309, may be extended.

SEC. 2. BACKGROUND.

Under the provisions of section 309 of the Tariff Act of 1930, as amended, and sections 5053, 5055, 5062(b), 5214(a)(7) and 5362(c)(3) of the Internal Revenue Code of 1954, and applicable regulations of the Internal Revenue Service, alcohol, distilled spirits, beer, and wine may be withdrawn free of tax or with benefit of drawback for use as supplies on aircraft registered in foreign countries and actually engaged in foreign trade or trade between the United States and its possessions, or between Hawaii and any other part of the United States or between Alaska and any other part of the United

[1] Superseded by Rev. Proc. 61–34, page 573, this Bulletin.

States where trade by foreign aircraft is permitted. Such privilege is extended in respect of aircraft registered in a foreign country only if the Secretary of Commerce has found that such foreign country allows, or will allow, substantially reciprocal privileges in respect of aircraft registered in the United States.

SEC. 3. PAKISTAN AND VENEZUELA.

In addition to those countries listed in Revenue Procedure 61–13, C.B. 1961–1, 900, the Department of Commerce has found and has advised the Secretary of the Treasury that the countries of Pakistan and Venezuela extend to aircraft registered in the United States and engaged in foreign trade, privileges substantially reciprocal to those given aircraft registered in Pakistan and Venezuela and engaged in foreign trade.

SEC. 4. COMPLETE LIST OF FOREIGN COUNTRIES.

The complete list of foreign countries to which reciprocal privileges may be extended is as follows:

Argentina	El Salvador	Nicaragua
Australia	France	Norway
Bahama Islands	Germany, Federal Republic of	Pakistan
Belgium	Greece	Peru
Bermuda	India	Spain
Brazil	Israel	Sweden
Canada	Italy	Switzerland
Costa Rica	Japan	United Kingdom
Denmark	Lebanon	Venezuela
Dominican Republic	Mexico	
Ecuador	Netherlands	
Eire		

SEC. 5. EFFECT ON OTHER DOCUMENTS.

This Revenue Procedure supersedes Revenue Procedure 61–13, C.B. 1961–1, 900.

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26 CFR 601.301: Imposition of taxes, qualification requirements, and regulations. (Also Part III–A, Section 5006; 201.634.) — Rev. Proc. 61–25

Gin of 190 degrees or more of proof shall be reported in column (d) of Form 332, Statement by Kinds, Seasons, and Years of Production of Spirits in Bonded Warehouses, rather than in item 6 of the form.

SECTION 1. PURPOSE.

The purpose of this Revenue Procedure is to set forth the procedures to be followed in reporting gin of 190 degrees or more of proof on Form 332, Statement by Kinds, Seasons, and Years of Production of Spirits in Bonded Warehouses.

SEC. 2. BACKGROUND.

Section 5006(a)(2)(B) of the Internal Revenue Code of 1954 provides that the bonding period limitation for distilled spirits in bonded storage shall not apply to distilled spirits of 190 degrees or more of proof.

SEC. 3. PROCEDURE.

All gin shall be entered in column (d) in Form 332. Gin of less than 190 degrees of proof shall be entered according to its season and year of production. Gin of 190 degrees or more of proof shall be entered separately in column (d) on an unused line and shall be identified as being of 190 degrees or more of proof. The entry at item 6, therefore, shall include only neutral spirits and alcohol of 190 degrees or more of proof.

SEC. 4. INQUIRIES.

Inquiries regarding this Revenue Procedure should refer to its number and be addressed to the office of the appropriate Assistant Regional Commissioner, Alcohol and Tobacco Tax.

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26 CFR 601.301: Imposition of taxes, qualification requirements, and regulations. (Also Part III–B, Section 5; 27 CFR 5.21.) Rev. Proc. 61–26

All French grape brandies, other than Cognac and Armagnac, shipped from foreign ports to the United States after June 1, 1961, must be accompanied by certificates of identification and analysis issued by the French Ministry of Agriculture.

SECTION 1. PURPOSE.

The purpose of this Revenue Procedure is to advise importers of French brandies that all such brandies (other than Cognac and Armagnac) shipped from foreign ports to the United States must, in addition to the required age and origin certificates, be accompanied by certificates of identification and analysis.

SEC. 2. BACKGROUND.

In order to assure that French brandy exported to the United States meets the standard of identity for "brandy" under section 5.21(d), class 4, of the Labeling and Advertising of Distilled Spirits Regulations, under the Federal Alcohol Administration Act, a method of control by analysis has been adopted by France through the French Ministry of Agriculture.

SEC. 3. CONCLUSION.

.01 The Internal Revenue Service has been advised by the French Government that all French grape brandies, other than Cognac and Armagnac, shipped to the United States after June 1, 1961, will be covered by an analysis certificate issued by the French Ministry of Agriculture. Two laboratories have been designated by the French Government to make the analysis and issue certificates pursuant thereto. A certificate issued by either the "Laboratoire Central De Recherches Et D'Analyses" or the "Station Agronomique Et Oenologique De Bordeaux" will be acceptable to effect release of the brandies covered thereby from Customs custody.

.02 Where French brandies are exported after June 1, 1961, to another country prior to shipment to the United States, such brandies may not be released from Customs custody in the United States unless accompanied by a certificate issued by a duly authorized officer of such other country certifying that the brandy was received from

France, accompanied by French certificates of age and origin and certificates of analysis issued by (*name of Laboratory*), and while in such other country was not blended or otherwise treated prior to shipment to the United States.

SEC. 4. INQUIRIES.

Correspondence regarding this Revenue Procedure should refer to its number and be addressed to the Director, Alcohol and Tobacco Tax Division (O:AT:B), Washington 25, D.C.

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25 CFR 601.106: Appellate functions. Rev. Proc. 61-27

Procedures to be followed with respect to protests before a regional Appellate Division in unagreed 100-percent penalty cases arising in District Collection Divisions.
Revenue Procedure 57-26, C.B. 1957-2, 1093, amplified.

SECTION 1. PURPOSE.

The purpose of this Revenue Procedure is to set forth procedures for protests and conferences before a Regional Appellate Division in unagreed cases arising in District Collection Divisions involving section 6672 of the Internal Revenue Code of 1954 or corresponding provisions of the Internal Revenue Code of 1939.

SEC. 2. BACKGROUND.

.01 Section 6672 of the Code imposes a penalty (hereinafter referred to as the 100-percent penalty) against any person who, being required to collect, truthfully account for, and pay over any tax imposed by the Code, wilfully fails to collect such tax, or truthfully account for and pay over such tax, or wilfully attempts in any manner to evade or defeat any such tax or the payment thereof.

.02 The terms "person" and "taxpayer," as used herein, include an officer or employee of a corporation, or a member or employee of a partnership who as such officer, employee, or member is under a duty to perform the act in respect of which the violation occurs.

.03 Revenue Procedure 57-26, C.B.1957-2, 1093, extended jurisdiction of the Appellate Division, prior to assessment, to all unagreed cases arising in District Audit Divisions which involve excise taxes imposed under Chapters 31, 32, 33, 34, 36, 37, Subchapter F of Chapter 38, and Subchapters B, C, D, E, and F of Chapter 39, and employment taxes under Chapters 21, 22, 23, and 24 of the Internal Revenue Code of 1954 and corresponding provisions of the Internal Revenue Code of 1939, except where collection of the amount involved is in jeopardy. This Procedure explains the right of taxpayers to Appellate Division consideration, prior to assessment, in unagreed and protested 100 percent penalty cases arising in District Collection Divisions.

SEC. 3. SCOPE.

The procedures set forth herein are applicable to all unagreed 100-percent penalty cases arising in District Collection Divisions which relate to employment and excise taxes imposed under Chapters 21, 22, 24, and 33 of the 1954 Code and corresponding provisions of the 1939 Code, except where collection is in jeopardy.

SEC. 4. PROCEDURE IN DISTRICT COLLECTION DIVISIONS.

.01 When, at the conclusion of an investigation to determine whether liability for the 100-percent penalty has been incurred, assessment of the penalty is proposed, the taxpayer will be so informed by letter from the District Collection Division and will be afforded an opportunity to execute an agreement form. If the taxpayer does not agree to the proposed assessment, he will be afforded an opportunity to present objections thereto at an informal conference. If the taxpayer does not request an informal conference or if an agreement is not reached at an informal conference, a formal notice of the proposed assessment will be issued to the taxpayer granting him 30 days in which to file a protest and request a conference before the Regional Appellate Division. A copy of the revenue officer's report of investigation or report of the conference will accompany the 30-day notice.

.02 If a signed agreement form is received from the taxpayer, whether prior or subsequent to issuance of the 30-day notice referred to in paragraph .01 of this section, or if the taxpayer does not file a protest within the specified 30-day period, the penalty will be assessed. If the taxpayer submits a timely protest in response to the 30-day notice and requests that his case be referred to the Regional Appellate Division, the case will be reviewed in the District Director's office to determine whether new facts are presented in the taxpayer's formal protest which require verification or which may constitute a basis for possible revision of the position previously taken by the District Director's office. If additional facts are presented which require verification or which indicate that it may be possible to reach agreement on the liability issue, necessary action will be taken to accomplish such verification and, if appropriate, an informal conference with the taxpayer will be arranged. If no additional facts are presented in the taxpayer's protest or if consideration of such additional facts as may be presented does not produce a basis for closing the case in the District Collection Division, the case will be forwarded to the Regional Appellate Division for necessary action.

SEC. 5. PROCEDURE IN DISTRICT DIRECTORS' OFFICES IN DISPOSING OF CLAIMS.

If the 100-percent penalty has been assessed (1) by reason of the failure of the taxpayer to respond to a 30-day notice within the 30-day period or (2) on the basis of the decision of the Regional Appellate Division, the taxpayer ordinarily will be required to pay the assessment and file a claim for refund prior to any further consideration of the case on its merits by the District Director or the Regional Appellate Division. After assessment of the penalty under either of the conditions specified above, the Internal Revenue Service will not recognize any claim for abatement which may be filed, unless the taxpayer establishes a meritorious reason warranting consideration of such a claim, such as failure to receive a 30-day notice. If the District Director concludes that no consideration is to be given to an abatement claim that has been filed, the taxpayer will be notified to that effect. A claim for refund, or a claim for abatement of an assessment made under conditions other than conditions (1) and (2) described above, will be considered on its merits and will be referred to

the Regional Appellate Division if the taxpayer protests the District Director's conclusions and requests Appellate Division consideration.

SEC. 6. PROCEDURE IN REGIONAL APPELLATE DIVISIONS.

The procedure before a Regional Appellate Division in unagreed 100-percent penalty cases is similar to the procedure for the handling of cases prescribed in section 601.106(b) of the Statement of Procedural Rules, as amended, C.B. 1955–2, 921; C.B. 1958–1, 664; and C.B. 1959–1, 770.

SEC. 7. EFFECT ON OTHER DOCUMENTS.

Revenue Procedure 57–26, C.B. 1959–2, 1093, is hereby amplified to include the provisions stated herein.

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26 CFR 601.301: Imposition of tax, qualification requirements, and regulations. (Also Part III–A, Section 5212; 201.368.)

Rev. Proc. 61–28

On and after October 1, 1961, proprietors of distilled spirits plants shall prepare an additional copy of Form 2630, Package Gauge Report, when spirits in packages are to be transferred in bond.

SECTION 1. PURPOSE.

The purpose of this Revenue Procedure is to provide instructions for the number of copies of Form 2630, Package Gauge Report, to be prepared when packages of spirits are transferred in bond.

SEC. 2. BACKGROUND.

0.1 Section 201.368 of the Distilled Spirits Plants Regulations provides that when packaged spirits are to be transferred in bond, the consignor shall, in addition to preparing Form 236, Transfer of Spirits or Denatured Spirits in Bond, prepare Form 2630, Package Gauge Report, describing the packages.

0.2 The instructions on Form 236 which cover the preparation and distribution of Form 2630 do not provide a copy of Form 2630 for the Assistant Regional Commissioner, Alcohol and Tobacco Tax, of the consignor's region. Such a copy has been found necessary to complete the records of the Internal Revenue Service covering packages of spirits in bond.

SEC. 3. PROCEDURE.

0.1 On and after October 1, 1961, proprietors of distilled spirits plants shall prepare Form 2630 in quadruplicate, instead of in triplicate as prescribed by instructions on Form 236, when packaged spirits are to be transferred in bond. The additional copy shall be furnished to the Government officer assigned to the shipping plant for forwarding, with a copy of the Form 236 covering the shipment, to his Assistant Regional Commissioner.

0.2 The instructions on Form 236 covering the preparation and distribution of Form 2630 will be revised to conform with this procedure when Form 236 is reprinted.

SEC. 4. INQUIRIES.

Inquiries concerning this Revenue Procedure should refer to its number and be addressed to the office of the appropriate Assistant Regional Commissioner, Alcohol and Tobacco Tax.

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26 CFR 601.602: Forms and instructions. Rev. Proc. 61–29
(Also Part I, Section 6051, 31.6051–1.)

Substitutes for Form W–2, Withholding Tax Statement–1962, may be privately printed with slight variations in format and used without specific approval of the Internal Revenue Service, provided that they meet specified conditions with respect to physical characteristics, use of additional copies, and additional information, if any, to state and local taxing authorities.

SECTION 1. PURPOSE.

The purpose of this Revenue Procedure is to state the requirements of the Internal Revenue Service relating to the preparation of acceptable substitutes for Form W–2, Withholding Tax Statement–1962, for filing purposes in lieu of the official form printed by the Government Printing Office.

SEC. 2. SPECIFICATIONS.

.01 *Substitutes.*—Substitutes for Form W–2 may be privately printed with slight variations in format and used without requesting approval of the Internal Revenue Service if the conditions enumerated in section 3 are met. For proposed substitutes which do not meet such conditions, specific approval must be requested as provided by section 5, below. In any rearrangement of the information, care should be taken to prevent disclosure of wage and tax information if a window envelope is used for mailing.

.02 *Design for mailing.*—The official form is designed for mailing in a standard window envelope. This feature will be found desirable in most of the privately printed substitutes.

.03 *Copy D.*—Copy D is included in the official assembly for the convenience of the employer. Although there is no requirement that privately printed substitute forms include Copy D, employers may find it desirable to make and retain such copy.

SEC. 3. CONDITIONS.

.01 *Color and quality of ink and paper.*—The substitute forms, except for authorized punch card substitutes, must be printed in brown ink on white paper, both of quality as good as that used by the Government. The paper must be of substantially the same weight and texture as that used in the official form, which is printed on substance 32-pound white-writing—basis 1,000 sheets 17 x 22.

.02 *Typography.*—Type may not be smaller than the corresponding type on the official form and as nearly as possible of the same font.

.03 *Format.*—The substitute forms must provide the same spaces as the official form for showing wages paid and tax withheld. In any rearrangement of such spaces, the block headed "INCOME TAX INFORMATION" is to be placed in a prominent position on the Form, preferably in the right-center position, the spaces for showing

social security information to be either to the left or above such block.

.04 *Dimensions.*—The official form is eight inches wide by three and one-half inches deep, exclusive of a half inch snap-stub on the left side of the form. The substitute forms may vary in width from seven inches to eight inches and in depth from three and one-sixth inches to three and two-thirds inches. The snap feature is not required on substitutes.

.05 *Carbonized forms or "spot carbons."*—Carbonized forms and "spot carbons" are not permissible. Interleaved carbon, if used, must be of good quality to preclude smudging and, preferably, black.

.06 *Special identification.*—Copy B must show the full-face dots, arranged vertically on the upper right side.

.07 *The Government Printing Office symbols.*—The Government Printing Office symbols must be omitted.

SEC. 4. ADDITIONAL INSTRUCTIONS.

.01 *Arrangement of assembly.*—Except as provided in paragraph .02 below, the parts of the assembly shall be arranged, from top to bottom, as follows: Copy A, "For District Director;" Copy B, "To be filed with Employee's Tax Return;" Copy C, "For Employee's Records;" Copy D, "For Employer." All references to the various parts shall be to "Copy A," "Copy B," "Copy C," or "Copy D."

.02 *Additional copies.*—Additional copies may be prepared for the use of employers in connection with taxes or deductions other than Federal income tax and Federal Insurance Contributions Act taxes. Such additional copies may not be placed ahead of Copy C in the assembly except that if a copy or copies for a state or local taxing authority are prepared only one such copy may be placed ahead of Copy C in the assembly, for better legibility. Forms for delivery to state or local taxing authorities should be clearly labeled to indicate the purpose for which they are intended and should not bear any part of the designation, "Form W-2—U.S. Treasury Department, Internal Revenue Service."

.03 *Excludable sick pay.*—If desired, a block may be shown on Form W-2 for excludable sick pay. However, if such a block is provided and no amount is entered, the word "None" or "O" should be shown.

.04 *Statement to support excludable sick pay.*—A statement from the employer to support sick pay excludable from gross income may be made a part of the assembly, provided it is not placed ahead of Copies A and B in the assembly and is printed on paper of distinctive color. Such statement should substantially conform with the statement set forth in Revenue Procedure 57-1, C.B. 1957-1, 721. It should be clearly indicated on such statement that it is to be attached to page 2 of the taxpayer's Federal income tax return, Form 1040.

.05 *Instructions.*—No deviation from the instructions on either the front or back of Copies A, B, or C will be permitted.

.06 *State or local taxing authorities.*—Additional wage or tax information for state or local taxing authorities may be shown on Copy C, but not on Copies A and B.

.07 *Other information.*—Payroll deductions other than those required to be reported on Form W-2 may not be shown on Copies A and B, except as provided in paragraph .08 below.

.08 *State agencies.*—The amounts of wages paid and employee contributions withheld under a State-Federal agreement, entered into pursuant to section 218 of the Social Security Act, may be shown in the spaces on Form W–2 for Federal Insurance Contributions Act wages and employee tax, provided appropriate distinguishing captions are used to identify such amounts. The identification number assigned by the Social Security Administration to the state (prefix 69) should be shown in addition to the employer identification number assigned by the Internal Revenue Service for income tax withholding purposes.

SEC. 5. SUBSTITUTES NOT MEETING ABOVE CONDITIONS.

Proposed substitute forms which do not meet the conditions stated above and requests for submission of punched card Forms W–2 should be forwarded by letter to the Commissioner of Internal Revenue, Attention: D: S: P, Washington 25, D.C., for approval.

SEC. 6. REPRODUCTION PROOFS.

Reproduction proofs of the official Form W–2 are available upon the request of any employer who desires to use reproductions of such form. Requests for reproduction proofs should be addressed to the Commissioner of Internal Revenue, Attention: A: FM: P, Washington 25, D.C.

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26 CFR 1.9100–1: Extension of time for making certain elections.
(Also Part I, Section 1372; 1.1372–3.)

Rev. Proc. 61–30 [1]

The Internal Revenue Service will consider, upon request, the granting of extensions of time for the filing of consents by certain shareholders who failed to file timely consents to elections by small business corporations under section 1372 of the Internal Revenue Code of 1954.

The shareholders involved are either new share holders of the corporation or a husband or wife who has failed to file a timely consent. In the case of a husband or wife, the stock owned must have been community property (or the income from which is community income) or the stock must have been held as joint tenants, tenants by the entirety, or tenants in common.

Consideration will be given to requests for extensions of time for the filing of such consents only where the following conditions are met:

(1) A timely election under section 1372 must have been filed by the corporation or must be in effect for the corporation and its shareholders for the year for which the extension is requested.

(2) Since the request for extension of time will be considered under section 1.9100–1 of the Income Tax Regulations, good cause must be shown for the granting of the extension and it must be shown that the interests of the Government are not jeopardized.

(3) A request for an extension of time will be granted only if the other shareholders of the corporation who previously filed

[1] Based on Technical Information Release 336, dated September 18, 1961.

timely and proper consents (or who are affected by such a consent) execute new consents.

Ordinarily, if good cause exists for the granting of a new election under section 1372(f), it will be regarded as good cause for the granting of an extension of time for filing consents.

Requests for an extension of time should be addressed to the Commissioner of Internal Revenue, 12th and Constitution Avenue, N.W., Washington 25, D.C., Attention: Tax Rulings Division.

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26 CFR 601.602: Forms and instructions. (Also Part I, Sections 6001, 6011, 6018, 6019; 1.6001–1, 1.6011–1, 20.6018–1, 25.6019–1.) Rev. Proc. 61–31

Reproduced copies of certain Federal tax return forms and schedules may be used for filing purposes in lieu of the applicable official forms, subject, however, to prescribed conditions.

Revenue Procedure 60–27, C.B. 1960–2, 1003, superseded.

SECTION 1. PURPOSE.

The purpose of this Revenue Procedure is to restate the requirements of the Internal Revenue Service relating to the preparation of acceptable reproductions of Federal tax return forms and schedules for filing purposes in lieu of the official forms and schedules.

SEC. 2. SPECIFICATIONS.

Subject to the conditions enumerated in section 3 below, the Service will accept, for filing purposes, reproduced copies of any of the following tax return forms and schedules:

Employee's Withholding Exemption Certificate, Form W–4
U.S. Estate Tax Return, Form 706
U.S. Gift Tax Return, Form 709
Life Insurance Statement, Form 712
Claim, Form 843
U.S. Exempt Cooperative Association Income Tax Return, Form 990–C
U.S. Return of Employees' Trust Described in Section 401(a) and Exempt Under Section 501(a) of the Internal Revenue Code of 1954, Form 990–P
U.S. Individual Income Tax Return, Form 1040
Supplemental Schedule of Income and Credits, Schedule B (Form 1040)
Profit (or Loss) From Business or Profession, Schedule C (Form 1040)
Gains and Losses from Sales or Exchanges of Property, Schedule D (Form 1040)
U.S. Departing Alien Income Tax Return, Form 1040C
Declaration of Estimated Tax, Form 1040–ES
Schedule of Farm Income and Expenses, Schedule F (Form 1040)
U.S. Fiduciary Income Tax Return, Form 1041
Allocation of Accumulation Distribution, Schedule J (Form 1041)
U.S. Partnership Return of Income, Form 1065

Gains and Losses from Sales or Exchanges of Property, Schedule D (Form 1065)
Statement in Support of Credit Claimed by Domestic Corporation for Taxes Paid or Accrued to a Foreign Country or a Possession of the United States, Form 1118
U.S. Corporation Income Tax Return, Form 1120
Schedule of Gains and Losses From Sales or Exchanges of Property, Schedule D (Form 1120)
U.S. Small Business Corporation Return of Income, Form 1120–S
Gains and Losses from Sales or Exchanges of Property, Schedule D (Form 1120–S)
Return of Information and Authorization and Consent of Subsidiary Corporation Included in a United States Consolidated Income Tax Reurn, Form 1122
Statement for the Purpose of Extending Time for Payment of Taxes by Corporations Expecting Carrybacks, Form 1138
Application for Tentative Carryback Adjustment, Form 1139

SEC. 3. CONDITIONS.

.01 Reproductions must be facsimiles of the official form, produced by photo-offset, photoengraving, photocopying, or other similar reproduction process.

.02 Reproductions must be on paper of substantially the same weight and texture and of a quality at least as good as that used in the official form.

.03 Reproductions must substantially duplicate the colors of the paper and/or ink of the official form in order to be acceptable.

.04 Reproductions must have a high standard of legibility, both as to original form and as to filled-in matter. The Internal Revenue Service reserves the right to reject any reproductions with poor legibility, to withdraw the benefits of this Revenue Procedure from any firm or individual, and to reject any process which fails to meet these standards.

.05 Reproductions of Schedule C–3 and Schedule F–1, Form 1040, which contain Schedule SE, U.S. Report of Self-Employment Income, must be on properly perforated paper of substantially the same weight and texture as that used in the official form.

.06 Reproductions can be the same size as that of the official form. However, the standard commercial size of 8½ x 11 (as noted in columns 2 and 3 of table in section 5 below) will be accepted, but no tolerances will be permitted in the image size of printed material.

SEC. 4. ADDITIONAL INSTRUCTIONS.

.01 The Service ordinarily does not undertake to approve or disapprove the specific equipment or process used in reproducing official forms, but requires only that the reproduced forms and schedules satisfy the stated conditions.

.02 While it is preferred that both sides of the paper be used in making reproductions, resulting in the same page arrangement as that of the official form, the Service will not object if only one side of the paper is used or if the reproduction has a different fold than that provided on the official form.

.03 Reproductions of forms may be made after insertion of the tax computations and other required information. However, all signatures on forms to be filed with the Service must be original signatures, affixed subsequent to the reproduction process.

.04 Reproductions of forms and schedules meeting the above conditions may be used without the prior approval of the Service. However, if specific approval of a reproduction of any such form or schedule is desired, or if the use of a reproduction of any form or schedule not listed herein or otherwise specifically authorized is desired, a sample of the proposed reproduction should be forwarded, by letter, to the Commissioner of Internal Revenue, Attention: D:S:P, Washington 25, D.C., for consideration.

SEC. 5. PHYSICAL ASPECTS.

The conditions with respect to size, number of printed pages, and color of both paper and ink are as follows:

Form No.	Official IRS trim size [1]	Tolerances permitted in size [2]	Number of printed pages	Color of—	
				Paper	Ink
(1)	(2)	(3)	(4)	(5)	(6)
W-4	7⅞ x 3⅞16	8 x 3½	2	White	Black.
706	8⅜ x 11	8½ x 11	40	White	Black.
709	8½ x 11		2	Buff	Black.
712	8 x 10½	8½ x 11	1	White	Black.
843	8 x 10½	8½ x 11	2	White	Black.
990-C	8½ x 13⅜	8½ x 14	4	White	Black.
990-P	8 x 10½	8½ x 11	3	White	Black.
1040	8 x 11	8½ x 11	2	White	Black.
Schedule B, 1040	8 x 11	8½ x 11	2	White	Black.
Schedule C, 1040	7⅞ x 11	8½ x 11	4	White	Black.
Schedule D, 1040	8 x 11	8½ x 11	2	White	Black.
1040C	7⅞ x 11	8½ x 11	4	White	Black.
1962 1040-ES	8 x 10½	8½ x 11	2	White	Black.
Schedule F, 1040	7⅞ x 11	8½ x 11	4	White	Black.
1041	7⅞ x 11	8½ x 11	4	Pink	Black.
Schedule J, 1041	7⅞ x 11	8½ x 11	2	Pink	Black.
1065	8 x 11	8½ x 11	4	Yellow	Black.
Schedule D, 1065	8 x 11	8½ x 11	2	Yellow	Black.
1118	11 x 8½		2	White	Black.
1120	8 x 11	8½ x 11	4	Blue	Black.
Schedule D, 1120	8 x 11	8½ x 11	4	Blue	Black.
1120S	8½ x 11		4	Green	Black.
Schedule D, 1120S	8½ x 11		2	Green	Black.
1122	8 x 10½	8½ x 11	1	Blue	Black.
1138	8½ x 10½	8½ x 11	2	White	Black.
1139	8½ x 11		3	White	Black.

[1] Sizes shown are for single forms furnished by Internal Revenue Service offices; forms supplied in Income Tax Packages are 8¾" x 11"

[2] Forms cannot exceed sizes shown, nor be less than size of official forms.

SEC. 6. BLACK AND WHITE PROOFS.

The Service, upon application, will furnish one set of black and white proofs to be used as the reproducible media in the printing of forms. These proofs, for which separate requests must be received annually, will be supplied free of charge to all concerns in the forms

reproduction business. Reproduction proofs are available only for the following forms:

W–4	1065
1040	Schedule D (1065)
Schedule B (1040)	1096
Schedule C (1040)	1099
Schedule D (1040)	1099L
1040–ES	1120
Schedule F (1040)	Schedule D (1120)
1041	1120S
Schedule J (1041)	Schedule D (1120S)

Requests for reproduction proofs should be addressed to the Commissioner of Internal Revenue, Attention: A:FM:P, Washington 25, D.C.

SEC. 7. EFFECT ON OTHER DOCUMENTS.

This Revenue Procedure supersedes Revenue Procedure 60–27, C.B.1960–2, 1003.

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26 CFR 601.105: Examination of returns and claims for refund, credit or abatement; determination of correct tax liability. (Also Part I, Section 162; 1.162–15.) — Rev. Proc. 61–32

Revenue Procedure 61–10, C.B. 1961–1, 895, described the informal conference and appeals procedure established by the Internal Revenue Service in cases where an organization, such as a labor union or trade association, is examined solely to determine the deductibility under section 1.162–15(c)(2) of the Income Tax Regulations of dues and other payments made by contributors to such organization. However, it did not include a provision for notifying such an exempt organization regarding the conclusions of the Service after review of the agreement or findings in the organization's case.

A new section containing such a provision as section 3.07 is added to Revenue Procedure 61–10 as follows:

.07 After the Service's review of an agreement or finding in an exempt organization case, the organization will be appropriately notified in the matter. This notice will be issued either before or at the time District Directors in affected districts are notified regarding the deductibility of the dues or other payments made by members or contributors to the organization.

Revenue Procedure 61–10 is hereby amplified.

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26 CFR 601.301: Imposition of taxes, qualification requirements, and regulations. (Also Part III–B, Section 5(e); 27 CFR 4.45.) — Rev. Proc. 61–33

Spanish sherry wine shipped from foreign ports to the United States, on and after August 31, 1961, must be accompanied by appropriate certificates of origin and identity.

SECTION 1. PURPOSE.

The purpose of this Revenue Procedure is to inform importers of Spanish sherry wine that such wine shipped from foreign ports, on and after August 31, 1961, must be accompanied by an appropriate certificate of origin and identity.

SEC. 2. BACKGROUND.

Section 4.45 of the Federal Labeling and Advertising of Wine Regulations under the Federal Alcohol Administration Act, provides in part that imported wines shall not be released from Customs custody for consumption unless the invoice is accompanied by a certificate of origin issued by a duly authorized official of the appropriate foreign government, if the issuance of such certificate with respect to such wines has been authorized by the foreign government concerned. Revenue Procedure 59–9, C.B.1959–1, 818, informed importers of wine of the provisions of the regulations regarding certificates of origin and identity and certificates of authenticity of vintage dates for bottled imported wines. Revenue Procedure 59–32, C.B.1959–2, 951, described the type and form of certificate required of wines bottled in countries other than the country of origin.

SEC. 3. CONCLUSION.

.01 Under Spanish law the Consejo Regulador De La Denominacian De Origen "Jerez-Xeres-Sherry" is authorized to issue certificates of origin to cover sherry wines exported from Spain.

.02 If sherry wine is shipped to other countries for bottling prior to shipment to the United States, it must be covered by appropriate certification before it may be released from Customs custody. For example, if sherry wine is shipped from Spain, in bulk, to England for bottling, the bottled wine, if exported to the United States, must be covered by an appropriate certificate issued by the office of British Customs and Excise which will be accepted by the United States Customs officers in place of the original Spanish certificate described above.

.03 In order to avoid detention of merchandise at the ports of entry, all importers of sherry wine should advise their principals abroad of these provisions.

SEC. 4. INQUIRIES.

Correspondence in regard to this Revenue Procedure should refer to its number and be addressed to the Director, Alcohol and Tobacco Tax (CP:AT:B), Washington 25, D.C.

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26 CFR 601.301: Imposition of taxes, qualification requirements, and regulations.
(Also Part III–A, Sections 5053, 5062, 5214, 5362; 245.170, 252.23, 240.670.)

Rev. Proc. 61–34

The Republic of Panama has been added to the list of countries to which has been extended the privilege of withdrawing alcohol, distilled spirits, beer, and wine free of tax or with benefit of drawback for use as supplies on aircraft.

Revenue Procedure 61–24, page 560, this Bulletin, superseded.

SECTION 1. PURPOSE.

The purpose of this Revenue Procedure is to announce the addition of Panama to the list of foreign countries to which the reciprocal privileges provided by section 309 of the Tariff Act of 1930, 19 U.S.C. 1309, as amended may be extended.

SEC. 2. BACKGROUND.

Under the provisions of section 309 of the Tariff Act of 1930, as amended, and sections 5053, 5055, 5062(b), 5214(a)(7) and 5362(c)(3) of the Internal Revenue Code of 1954, and applicable regulations of the Internal Revenue Service, alcohol, distilled spirits, beer, and wine may be withdrawn free of tax or with benefit of drawback for use as supplies on aircraft registered in foreign countries and actually engaged in foreign trade or trade between the United States and its possessions, or between Hawaii and any other part of the United States, or between Alaska and any other part of the United States where trade by foreign aircraft is permitted. Such privilege is extended in respect of aircraft registered in a foreign country only if the Secretary of Commerce has found that such foreign country allows, or will allow, substantially reciprocal privileges in respect of aircraft registered in the United States.

SEC. 3. PANAMA.

In addition to those countries listed in Revenue Procedure 61–24, page 560, this Bulletin, the Department of Commerce has found and has advised the Secretary of the Treasury that the country of Panama extends to aircraft registered in the United States and engaged in foreign trade, privileges substantially reciprocal to those given aircraft registered in Panama and engaged in foreign trade.

SEC. 4. COMPLETE LIST OF FOREIGN COUNTRIES.

The complete list of foreign countries to which reciprocal privileges may be extended is as follows:

Argentina
Australia
Bahama Islands
Belgium
Bermuda
Brazil
Canada
Costa Rica
Denmark
Dominican Republic
Ecuador
Eire
El Salvador
France
Germany, Federal Republic of
Greece
India
Israel
Italy
Japan
Lebanon
Mexico
Netherlands
Nicaragua
Norway
Pakistan
Panama
Peru
Spain
Sweden
Switzerland
United Kingdom
Venezuela

SEC. 5. EFFECT ON OTHER DOCUMENTS.

This Revenue Procedure supersedes Revenue Procedure 61–24, page 560, this Bulletin.

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26 CFR 601.401: Employment taxes. (Also Part I, Section 1402.) Rev. Proc. 61–35

The Social Security Amendments of 1961, Public Law 87–64, approved June 30, 1961, page 315, this Bulletin, added a new paragraph (6) to section 1402(e) of the Self-Employment Contributions Act of 1954 (chapter 2, subtitle A, Internal Revenue Code of 1954).

This new paragraph relates to the filing of a Form 2031, Waiver Certificate to Elect Social Security Coverage for Use by Ministers, Certain Members of Religious Orders, and Christian Science Practitioners. In any case in which the minister, member of the religious order, or Christian Science practitioner dies after September 12, 1960,

and before April 16, 1962, without having filed a certificate on Form 2031, his survivor (as defined in section 205(c)(1)(C) of the Social Security Act, as amended) or the fiduciary of his estate may file the waiver certificate after June 30, 1961, and before April 16, 1962. The waiver certificate will be effective as if filed by the decedent on the day of his death.

Each waiver certificate filed pursuant to this new paragraph should be accompanied by a statement in writing, signed by the person filing the waiver certificate, setting forth such person's name and address, an explanation of such person's authority to file the waiver certificate, and the date of the decedent's death. If the waiver certificate is filed by a fiduciary, the statement should be accompanied by evidence of authority to file the waiver certificate.

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26 CFR 601.106: Appellate functions. Rev. Proc. 61–36 [1]

The procedure for bringing certain tax cases before the Appellate Division has been changed. The written protests which taxpayers are required to file with the District Director to bring unagreed tax cases before the Appellate Division may now be certified as true under the penalties of perjury. Formerly such written protests had to be filed under oath.

This relaxing of the requirements is effective immediately and applies to written protests on unagreed income, excess profits, estate and gift tax cases which are not docketed in The Tax Court of the United States and to unagreed employment and certain excise tax cases.

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26 CFR 601.301: Imposition of tax, qualification requirements, and regulations.
(Also Part III–A, Section 5212; 201.368, 201.369.) Rev. Proc. 61–37 [2]

Form 236, Transfer of Spirits or Denatured Spirits in Bond, and accompanying forms, if any, shall accompany the shipment when spirits are transferred in bond by truck.

SECTION 1. PURPOSE.

The purpose of this Revenue Procedure is to outline the procedures to be followed by Government officers in forwarding Form 236, Transfer of Spirits or Denatured Spirits in Bond, and accompanying forms, if any, when spirits are transferred in bond by truck.

SEC. 2. BACKGROUND.

.01 Instructions on Form 236 require that, when shipment of spirits is made by truck, the consignee's copies of Form 236 and any accompanying Form 1620, Filled Case Report, or Form 2630, Package Gauge Report, shall be forwarded to the assigned officer at the consignee plant via the driver of the truck.

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[1] Based on Technical Information Release 343, dated October 31, 1961.
[2] Based on Industry Circular No. 61–44, dated October 31, 1961.

.02 In certain circumstances this procedure has been found impracticable. Consequently, the instructions on Form 236 will be revised at the first suitable opportunity to provide merely that the consignee's copies of the transfer forms shall "accompany the shipment" if the shipment is made by truck.

SEC. 3. PROCEDURE.

When spirits are transferred in bond by truck, the Government officer assigned to the consignor premises shall enclose the consignee's copy of Form 236 and accompanying Form 1620 or 2630, if any, in a sealed envelope and deliver it to the driver of the truck or, if this is impracticable, the forms shall be placed with the shipment in such manner that they will be protected en route and will be readily available when the shipment is received.

SEC. 4. INQUIRIES.

Inquiries concerning this Revenue Procedure should refer to its number and be addressed to the office of the appropriate Assistant Regional Commissioner, Alcohol and Tobacco Tax.

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