

AMENDMENT OF SECTION 457 AND SECTION 459 OF THE INTERNAL REVENUE CODE

JUNE 26 (legislative day, JUNE 21), 1952.—Ordered to be printed

Mr. GEORGE, from the Committee on Finance, submitted the following

REPORT

[To accompany H. R. 8271]

The Senate Committee on Finance to whom was referred the bill (H. R. 8271) to amend section 457 of the Internal Revenue Code, having considered the same, report favorably thereon with amendments and recommend that the bill, as amended, do pass.

The amendments are as follows:

Amend the title so as to read:

An act to amend section 457 and section 459 of the Internal Revenue Code.

On page 2, after line 11, insert the following new sections:

SEC. 2. Section 459 of the Internal Revenue Code (miscellaneous provisions relating to the computation of average base period net income) is hereby amended by adding at the end thereof the following new subsection:

“(f) COMPANIES PRESERVING DEFENSE CAPACITY AND INCREASING CAPACITY FOR MANUFACTURING PEACETIME PRODUCTS FROM CERTAIN STRATEGIC AND CRITICAL METALS.—

“(1) ELIGIBILITY REQUIREMENTS.—In the case of a taxpayer which commenced business on or prior to January 1, 1936, and since such date has been primarily engaged in manufacturing, the taxpayer's average base period net income shall be determined under this subsection, if—

“(A) The percentage of the taxpayer's purchases of raw materials which were strategic and critical metals (as defined in paragraph (3)) was 80 per centum or more for each of the taxable years beginning with or within the taxpayer's base period;

“(B) The taxpayer's average monthly excess profits net income (computed in the manner provided in section 443 (e)) for the period comprising all taxable years ending with or within the first 24 months of its base period was 250 per centum or more of the average monthly excess profits net income (so computed) of the taxpayer for the period comprising all taxable years ending with or within the last 24 months of its base period;

“(C) The adjusted basis of the taxpayer's total facilities (as defined in section 444 (d)) as of the beginning of its base period (when added to the total facilities at such time of all corporations with which the taxpayer has the privilege under section 141 of filing a consolidated return for its first taxable year under this subchapter) did not exceed \$10,000,000; and

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“(D) The adjusted basis for determining gain of the taxpayer's total facilities (as defined in section 444 (d)) on the last day of its base period was 180 per centum or more of the adjusted basis for determining gain of its total facilities on the first day of its base period.

“(2) COMPUTATION.—The average base period net income determined under this subsection for a taxpayer entitled to the benefits of this subsection shall be the amount computed under section 435 (e) (2) (L) and (F) except that there shall be substituted for the aggregate of the excess profits net income for each of the six months in the period beginning July 1, 1949, and ending December 31, 1949, an amount computed by multiplying the aggregate of the excess profits net income for each of the six months in the period beginning July 1, 1946, and ending December 31, 1946, by the per centum determined by dividing the adjusted basis for determining gain of taxpayer's total facilities (as defined in section 444 (d)) on December 31, 1948, by the adjusted basis for determining gain of its total facilities on the first day of its base period. The average base period net income computed under the preceding sentence shall not exceed 80 per centum of the excess profits tax net income for the taxpayer's first taxable year under this subchapter.

“(3) DEFINITION OF STRATEGIC AND CRITICAL METALS.—As used in this subsection, the term 'strategic and critical metals' means copper and zinc which on January 1, 1945, had been determined by proper authority to be strategic and critical under the provisions of the Strategic and Critical Stock-Piling Act and shall include scrap containing such metals.

“Sec. 3. The amendment made by section 2 shall be applicable with respect to all taxable years ending after June 30, 1950.”

The bill provides for an adjustment in the base period earnings credit of companies which are required or permitted to make certain deposits of earnings under section 607 of the Merchant Marine Act, 1936. A provision with similar objectives was contained in the Senate version of the Excess Profits Tax Act of 1950, but was eliminated in conference in order that further study might be given to the proposal. The treatment of base period deposits of earnings has accordingly been given careful consideration. It is believed that base period deposits of earnings should be recognized, under the circumstances described in the bill, in order to reflect fully the taxpayer's actual base period earnings experience. Your committee understands that the Treasury Department has no objection to this provision.

The bill adds section 457 (c) to the Internal Revenue Code. This section provides that, for purposes of the excess profits tax, earnings deposited in reserve funds under section 607 of the Merchant Marine Act, 1936, shall be taken into account to a limited extent in computing the base period earnings credit. The deposited earnings are added to the excess profits net income for any base period year only to the extent that the deposits made or accrued in such base period year exceed the amount of such deposits for the taxable year for which an excess profits tax credit is being computed. The amount of deposits in the base period or excess profits tax period is subject to adjustment, under regulations prescribed by the Secretary of the Treasury, to exclude therefrom any amount which is payable to the Maritime Administration for such year as reimbursement of operating differential subsidy.

The deposited earnings referred to in the bill are the type referred to as "tax-deferred" under the provisions of closing agreements executed by the subsidized lines and the Bureau of Internal Revenue. Tax-deferred deposits do not include depreciation computed according to tax basis, but do include any depreciation in excess of tax depreciation which is deposited in the reserve funds. The term "earnings" does not include amounts which would be treated as capital gains under the Internal Revenue Code.

Your committee's amendment would provide excess profits tax relief for certain manufacturers using strategic and critical metals as their raw materials where the combination of rising raw material prices and failure of increased manufacturing facilities to be reflected in base period income has prevented their base period incomes from providing a fair base for excess profits tax credits. Strategic and critical metals are defined as copper and zinc, which were determined to be strategic and critical under the Strategic and Critical Stock Piling Act, and scrap containing such metals. A provision with similar objectives was contained in an amendment to the Revenue Act of 1951 which was offered on the floor of the Senate, but was withdrawn in order to permit further study with the understanding that it would then receive reconsideration. Eligibility under the amendment would be limited to corporations meeting the following tests:

1. The corporation must have commenced business on or before January 1, 1936, and engaged primarily in manufacturing since the beginning of 1936.

2. At least 80 percent of the corporation's purchases of raw materials during each of its base period years must have been strategic and critical metals.

3. The corporation's excess profits net income during the first half of its base period must have been at least 250 percent of its excess profits net income during the second half of its base period.

4. The adjusted basis of the corporation's total facilities at the beginning of its base period (plus the total facilities of all other corporations with which the taxpayer could file a consolidated return for its first excess profits tax year) did not exceed \$10 million.

5. The adjusted basis of the corporation's total facilities increased at least 80 percent during the base period.

Taxpayers qualifying under these eligibility tests may determine their average base period net income under section 435 (e) (2) (E) and (F) (the growth alternative). For purposes of this computation eligible taxpayers may use a substitute excess profits net income figure for the 6 months beginning July 1, 1949, and ending December 31, 1949. This substitute figure is obtained by multiplying income for the last 6 months of 1946 by the percent the taxpayer's total facilities on December 31, 1948, are of its total facilities at the beginning of its base period. In order to conform this amendment with the basic principles of the present growth alternative under the excess profits tax, the average base period net income figure determined under the amendment cannot exceed 80 percent of the taxpayer's excess profits tax net income (determined under section 433 (b)) for its first excess profits tax year.

Your committee's amendment is effective with respect to taxable years ending after June 30, 1950, so that the relief will cover the period for which the present excess profit tax has been in effect.

CHANGES IN EXISTING LAW

In compliance with subsection 4 of rule XXIX of the Standing Rules of the Senate, changes in existing law made by the bill are shown as follows (existing law proposed to be omitted is enclosed in black brackets; new matter is printed in italics; existing law in which no change is proposed is shown in roman):

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SECTION 457 OF THE INTERNAL REVENUE CODE

SEC. 457. CORPORATIONS COMPLETING CONTRACTS OR MAKING DEPOSITS UNDER MERCHANT MARINE ACT.

(a) If the Federal Maritime Board certifies to the Secretary that the taxpayer has completed within the taxable year any contracts or subcontracts which are subject to the provisions of section 505 (b) of the Merchant Marine Act of 1936, as amended, then the tax imposed by this subchapter for such taxable year shall be, in lieu of a tax computed under section 430, a tax computed under subsection (b) of this section, if, and only if, the tax computed under subsection (b) is less than the tax computed under section 430.

(b) The tax computed under this subsection shall be the excess of—

(1) A tentative tax computed under section 430 with the normal-tax net income increased by the amount of any payments made, or to be made, to the Federal Maritime Board with respect to such contracts or subcontracts; over

(2) The amount of such payments.

(c) *BASE PERIOD EARNINGS CREDIT FOR DEPOSITS UNDER MERCHANT MARINE ACT, 1936.*—The excess profits net income computed under section 433 (b) for any base period year shall be increased by the amount, if any, by which (1) the taxpayer's tax-deferred deposits of earnings, made in or accrued to reserve funds under section 607 of the Merchant Marine Act, 1936, in respect of such base period year, exceeds (2) the amount of such deposits of earnings for the taxable year. The Secretary shall provide, by regulation, for proper adjustment of the deposits made in or accrued to the reserve funds for any taxable year so as to exclude therefrom any amount payable for such year as reimbursement of operating-differential subsidy.

SECTION 459 OF THE INTERNAL REVENUE CODE

SEC. 459. MISCELLANEOUS PROVISIONS.

(f) *COMPANIES PRESERVING DEFENSE CAPACITY AND INCREASING CAPACITY FOR MANUFACTURING PEACETIME PRODUCTS FROM CERTAIN STRATEGIC AND CRITICAL METALS.*—

(1) *ELIGIBILITY REQUIREMENTS.*—In the case of a taxpayer which commenced business on or prior to January 1, 1936, and since such date has been primarily engaged in manufacturing, the taxpayer's average base period net income shall be determined under this subsection, if—

(A) The percentage of the taxpayer's purchases of raw materials which were strategic and critical metals (as defined in paragraph (3)) was 80 per centum or more for each of the taxable years beginning with or within the taxpayer's base period;

(B) The taxpayer's average monthly excess profits net income (computed in the manner provided in section 443 (c)) for the period comprising all taxable years ending with or within the first 24 months of its base period was 250 per centum or more of the average monthly excess profits net income (so computed) of the taxpayer for the period comprising all taxable years ending with or within the last 24 months of its base period;

(C) The adjusted basis of the taxpayer's total facilities (as defined in section 444 (d)) as of the beginning of its base period (when added to the total facilities at such time of all corporations with which the taxpayer has the privilege under section 141 of filing a consolidated return for its first taxable year under this subchapter) did not exceed \$10,000,000; and

(D) The adjusted basis for determining gain of the taxpayer's total facilities (as defined in section 444 (d)) on the last day of its base period was 180 per centum or more of the adjusted basis for determining gain of its total facilities on the first day of its base period.

(2) *COMPUTATION.*—The average base period net income determined under this subsection for a taxpayer entitled to the benefits of this subsection shall be the amount computed under section 435 (e) (2) (E) and (F) except that there shall be substituted for the aggregate of the excess profits net income for each of the six months in the period beginning July 1, 1949, and ending December 31, 1949, an amount computed by multiplying the aggregate of the excess profits net income for each of the six months in the period beginning July 1, 1946, and ending December 31, 1946, by the per centum

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determined by dividing the adjusted basis for determining gain of taxpayer's total facilities (as defined in section 444 (d)) on December 31, 1948, by the adjusted basis for determining gain of its total facilities on the first day of its base period. The average base period net income computed under the preceding sentence shall not exceed 80 per centum of the excess profits tax net income for the taxpayer's first taxable year under this subchapter.

(3) DEFINITION OF STRATEGIC AND CRITICAL METALS.—As used in this subsection the term "strategic and critical metals" means copper and zinc which on January 1, 1945, had been determined by proper authority to be strategic and critical under the provisions of the Strategic and Critical Stock-Piling Act and shall include scrap containing such metals.

