91st Congress 2d Session } SENATE { Report No. 91–1544

CERTAIN CUBAN EXPROPRIATION LOSSES

December 30 (legislative day, December 28), 1970.—Ordered to be printed

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

REPORT

[To accomapny H.R. 18693]

The Committee on Finance, to which was referred the bill (H.R. 18693) to amend section 165(i) of the Internal Revenue Code of 1954, having considered the same, reports favorably thereon with amendments and recommends that the bill (as amended) do pass.

I. SUMMARY

The bill as passed by the House amends the provisions of the tax laws relating to the deduction of Cuban expropriation losses of individuals to permit the carryback and carryover of losses of an individual resulting from the Cuban expropriation of investment property. Under present law, Cuban expropriation losses of an individual may generally be carried forward if they are attributable to property used in his trade or business, or carried back and forward if they are attributable to property held by him for personal use.

The bill as passed by the House also modifies the requirement under this provision of present law that the expropriated property must have been held by the taxpayer in Cuba on December 31, 1958. Under the modified requirement the property must have been held at some time during the period from December 31, 1958, through May 16, 1959. The modified requirement applies to personal-use property under present law, as well as to investment property under the bill. A trade or business expropriation loss, however, may be deducted when sustained without regard to these time limitations.

Claims for refund arising under the provisions of the bill may be filed between the date of enactment of the bill and July 1, 1971, even though they would otherwise be barred by the statute of limitations.

The committee accepted the House-passed provision without change. In addition, it added an amendment to the bill to increase the net operating loss carryover period for Cuban expropriation losses from 10 to 15 years.

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The Treasury Department has indicated that it does not oppose the enactment of this bill, as amended.

II. REASONS FOR BILL

Losses on investment property and time of loss

Under present law (sec. 172), net operating losses may be carried back 3 years and carried forward 5 years to offset income of the taxpayer. Net operating losses arising from expropriation by a foreign government may not be carried back, but they may be carried forward 10 years. However, in the case of individuals, these provisions are fully applicable, in effect, only to losses incurred in the taxpayer's trade or business.

A special rule (sec. 165 (i)) is provided for losses resulting from expropriation by the Cuban Government of property of an individual held for personal use, such as his residence. If the individual was a citizen or resident of the United States on December 31, 1958, any Cuban expropriation loss sustained before January 1, 1964, which was not a trade or business loss or an investment loss is treated as a casualty loss and therefore may be carried back 3 years and carried forward 5 years. (The special rule specifically provides that it may not be carried forward 10 years as a foreign expropriation loss.) If the property is tangible property, it must have been held by the taxpayer and located in Cuba on December 31, 1958.

An individual's losses on investment property (that is, property held for the production of income not in connection with a trade or business) may not be carried back or carried over under the regular net operating loss provision (sec. 172) except to the extent the individual has investment income. However, investment losses normally are capital losses, since they arise from the sale or exchange of capital assets, and as such they may be carried back or carried over under the capital loss carryback and carryover provisions (sec. 1212).

On the other hand, foreign expropriation losses of investment property are treated as ordinary losses and not as capital losses, since they are not considered as resulting from a sale or exchange. As a result there is no carryback or carryover of such losses except to the extent the taxpayer has investment income.

The committee agrees with the House that it is anomalous that unused Cuban expropriation losses of business property and personal-use property may be carried to other taxable years (under sec. 172) but unused Cuban expropriation losses of investment property cannot. There appears to be no reason why, if carrybacks and carryovers are to be allowed for expropriation losses of personal-use property, that they should not be allowed for expropriation losses of investment property, a class of property more closely related to business property, with respect to which losses have traditionally been accorded carryback and carryover treatment.

The committee is also concerned with the situation of a taxpayer who acquired property after December 31, 1958, but before the Cuban Government initiated its widespread policy of expropriation. This problem applies both to personal-use property under present law and investment property under the bill. (A trade or business expropriation loss already is eligible for the 10-year expropriation loss carryover even if the property was acquired after December 31, 1958).

15-year loss carryover for trade or business losses

In 1964, Congress permitted taxpayers to substitute, on an elective basis, a 10-year carryover period for the usual 3-year carryback and 5-year carryover period. This was done because it was recognized that foreign expropriations, particularly the then recent Cuban expropriations, often represent larger than normal losses for which the usual 8-year carryback carryover period was inadequate. It has come to the attention of the committee that because of the magnitude of the losses sustained as a result of Cuban expropriations, some taxpayers—particularly small businesses not generating large annual incomes—have been unable to offset their expropriation losses against their income in the 10-year carryover period. Because of this the committee believes that it is appropriate to extend the carryover period further in the case of Cuban expropriation losses.

III. EXPLANATION OF BILL

Loss on investment property and time of loss

The bill generally provides that Cuban expropriation losses of individuals with respect to investment property are to be treated in the same way as Cuban expropriation losses of individuals with respect to personal use property under present law—that is, as casualty losses which may be carried back and carried over under the net operating loss provisions.

As in the case of expropriations of personal-use property, an investment property loss is to be treated as having been sustained on October 14, 1960, unless it is established that it was sustained on some other day, and the normal 3-year carryback and 5-year carryover rule is to apply (rather than the 10-year carryover rule applicable to foreign expropriation losses incurred in a trade or business).

The bill provides that for purposes of determining whether investment property qualifies for casualty loss treatment, the property must have been held by the taxpayer in Cuba on one or more days during the period beginning on December 31, 1958, and ending on May 16, 1959. The bill also changes the provision of present law, which requires personal-use property to be held by the taxpayer in Cuba on December 31, 1958, in order to qualify for casualty loss treatment. The amendment permits personal use property to qualify if it was held on one or more days during the period beginning on December 31, 1958, and ending on May 16, 1959. For example, if a taxpayer acquired a residence in Cuba in February 1959, he could qualify for casualty loss treatment with respect to a later expropriation of the residence.

For purposes of determining fair market value of personal-use property or investment property which receives casualty loss treatment, the bill provides that the fair market value is to be determined on the first day in the period beginning on December 31, 1958, and ending on May 16, 1959, on which the property was held by the taxpayer.

The bill also provides that, notwithstanding any law or rule of law, refund or credit of any overpayment attributable to the amendments made by the bill, may be made or allowed if a claim for refund or credit is filed after the date of enactment of the bill and before January 1, 1971. This provision permits a taxpayer to file a claim for refund or credit for otherwise closed years (1) with respect to expropriated investment property, and (2) with respect to personal-use property acquired and held in Cuba after December 31, 1958, and on or before May 16, 1959, since casualty loss treatment is not available for expropriations of such property under present law. No interest is to be allowed on these refunds or credits for any period before January 1, 1972.

15-year carryover for trade or business losses

Under an amendment added by the committee, the net operating loss carryover period for Cuban expropriation losses is increased from 10 to 15 years. The carryover period for expropriation losses other than those incurred in Cuba remains at 10 years. Both the 10-year period for expropriations generally and the new 15-year Cuban expropriation loss carryover are available only for losses incurred in a trade or business.

For purposes of the provision added by the committee a net operating loss for a taxable year is considered to be attributable first to any Cuban expropriation losses for the taxable year up to the amount of these losses, then to other foreign expropriation losses up to the amount of these losses. In other words, income for a year is first offset by ordinary losses and deductions, then by non-Cuban expropriation losses, and finally by Cuban expropriation losses. A similar result is achieved when a net operating loss is carried over and partially absorbed in a taxable year. In this case, the amount of the carryover attributable to ordinary net operating losses is considered to be absorbed first, the amount attributable to foreign expropriation losses other than Cuban expropriation losses is considered to be absorbed next, and the amount attributable to Cuban expropriation losses is considered to be absorbed last. These rules have the effect of preserving as carryovers those losses to which the longest carryover period applies.

The amendments made by provision of the bill are to apply with respect to foreign expropriation losses sustained in taxable years ending after December 31, 1958.

IV. CHANGES IN EXISTING LAW

In the opinion of the committee, it is necessary, in order to expedite the business of the Senate, to dispense with the requirements of subsection 4 of rule XXIX of the Standing Rules of the Senate (relating to the showing of changes in existing law made bv the bill, as reported).

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