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2d Session }

VARIOUS REVENUE AND TARIFF BILLS

TESTIMONY TO BE RECEIVED TUESDAY, AUGUST 24, 1976, AND DEPARTMENTAL COMMENTS

COMMITTEE ON FINANCE
UNITED STATES SENATE
RUSSELL B. LONG, *Chairman*

AUGUST 24, 1976

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TESTIMONY OF SENATOR LEE METCALF
ON S. 2213
THE ELECTRIC UTILITY TAX EXEMPTION ACT
BEFORE THE SENATE FINANCE COMMITTEE
24 AUGUST, 1976

MR. CHAIRMAN, I AM TESTIFYING TODAY IN SUPPORT OF MY BILL, S. 2213 - THE ELECTRIC UTILITY TAX EXEMPTION ACT. BECAUSE OF ITS IMPORTANCE TO CONSUMERS OF ELECTRICITY AND THE DEVELOPMENT OF SOUND ENERGY REGULATION, I PROPOSED MY BILL AS AMENDMENT NUMBER 1849 TO THE TAX REFORM ACT OF 1976 - H. R. 10612.

I WITHDREW MY AMENDMENT AFTER RECEIVING ASSURANCE FROM SENATOR RIBICOFF, THE ACTING FLOOR MANAGER, THAT THIS COMMITTEE WOULD HOLD A HEARING ON S. 2213 PRIOR TO FINAL ADJOURNMENT OF THE NINETY-FOURTH CONGRESS. FROM OUR COLLOQUY AT THE TIME I WITHDREW MY AMENDMENT, I KNOW THAT SENATOR HASKELL IS CONCERNED ABOUT THE SERIOUS PROBLEMS FOR CONSUMERS WHICH HAVE EVOLVED FROM APPLICATION OF THE FEDERAL INCOME TAX LAWS TO ELECTRIC UTILITIES.

I BELIEVE THAT THE OTHER MEMBERS ON THIS COMMITTEE ARE ALSO CONCERNED OVER THE FINANCIAL HARDSHIPS WHICH WORKING FAMILIES AND THOSE LIVING ON FIXED INCOMES HAVE BEEN FORCED TO ENDURE DURING THE PAST FEW YEARS AS A RESULT OF SKYROCKETING ELECTRIC RATES.

APPLICATION OF THE FEDERAL INCOME TAX LAWS IN SETTING ELECTRIC RATES HAS UNNECESSARILY AGGRAVATED THE BURDEN OF RAPIDLY RISING ELECTRICITY PRICES FOR RESIDENTIAL CUSTOMERS AND BUSINESSMEN. CONGRESS MAY NOT BE ABLE TO CONTROL SOME OF THE FACTORS BEHIND THE INCREASED COST OF ELECTRICITY, BUT WE CAN ELIMINATE UNNECESSARY COST BURDENS RESULTING FROM THE FEDERAL INCOME TAX LAWS.

I INTRODUCED S. 2213 AS ONE PRACTICAL WAY FOR CONGRESS TO CORRECT THE RATE-MAKING ABUSES WHICH HAVE RESULTED FROM THE APPLICATION OF EXISTING FEDERAL INCOME TAX LAWS. THIS BILL WILL WORK BECAUSE ELECTRIC RATES WOULD NO LONGER BE SUBJECT TO THE UNFAIR AND CONTRADICTORY ACCOUNTING TECHNIQUES WHICH ARE USED TO CHARGE CUSTOMERS FOR FEDERAL INCOME TAXES THAT UTILITIES DO NOT PAY.

THE ELECTRIC UTILITY TAX EXEMPTION ACT PROVIDES SIMPLY THAT INVESTOR-OWNED ELECTRIC UTILITIES WOULD BE RELIEVED OF ALL OBLIGATIONS AND BENEFITS ARISING UNDER THE FEDERAL INCOME TAX LAWS. INFORMATION COMPILED BY THE FEDERAL POWER COMMISSION CONFIRMS THAT ENACTMENT OF S. 2213 WOULD HAVE A RELATIVELY LIMITED IMPACT ON TREASURY RECEIPTS WHEN COMPARED TO THE VAST AMOUNTS OF CUSTOMER OVERCHARGES WHICH WOULD BE PREVENTED.

DATA FROM 1974 - THE MOST RECENT AVAILABLE - SHOWS THAT THE ENTIRE ELECTRIC UTILITY INDUSTRY PAID ONLY FIVE HUNDRED AND TWENTY-EIGHT MILLION DOLLARS IN FEDERAL INCOME TAXES ON TOTAL ELECTRIC OPERATING REVENUES OF THIRTY-SEVEN AND TWO-TENTHS BILLION DOLLARS. THAT WAS ACTUALLY A FORTY-EIGHT PER CENT DECREASE IN ABSOLUTE DOLLARS FROM THE ONE BILLION DOLLARS PAID IN FEDERAL INCOME TAXES BY ELECTRIC UTILITIES IN 1955 - TWENTY YEARS AGO.

MORE THAN ONE-THIRD OF THE MAJOR ELECTRIC UTILITIES PAID NO FEDERAL INCOME TAXES AT ALL IN 1974. INSTEAD, THOSE UTILITIES ACCUMULATED OVER TWO HUNDRED AND EIGHTEEN MILLION DOLLARS OF TAX CREDITS.

ON A RELATIVE BASIS, THE AMOUNT OF FEDERAL INCOME TAXES PAID BY INVESTOR-OWNED ELECTRIC UTILITIES DECLINED FROM FOURTEEN AND SEVEN-TENTHS PER CENT OF REVENUES IN 1955 TO ONLY ONE AND FOUR-TENTHS PER CENT OF REVENUES IN 1974.

SINCE TAXES ARE BASED ON INCOME, IT SHOULD BE NOTED THAT THE ELECTRIC UTILITIES' PROFITABILITY, AS MEASURED BY THEIR RETURN ON COMMON STOCK EQUITY, WAS THE SAME IN 1955 AND 1974. IN BOTH YEARS, THEY AVERAGED A TEN AND EIGHT-TENTHS PER CENT RETURN ON EQUITY.

THE ABUSES PRESENT IN THE EXISTING TAX LAWS ARE BEST ILLUSTRATED BY COMPARING TOTAL FEDERAL INCOME TAXES PAID BY ELECTRIC UTILITIES IN 1974 WITH THE FEDERAL INCOME TAXES CHARGED TO CUSTOMERS ON JUST THE AMOUNT OF RATE INCREASES GRANTED IN A SINGLE YEAR.

BASED ON A RECENT SURVEY OF STATE REGULATORY COMMISSIONS, THE LIBRARY OF CONGRESS ESTIMATES THAT INVESTOR-OWNED ELECTRIC UTILITIES WERE GRANTED ADDITIONAL GENERAL RATE INCREASES TOTALING THREE AND THREE-TENTHS BILLION DOLLARS IN 1975 ALONE. APPROXIMATELY ONE HALF OF THAT AMOUNT - MORE THAN ONE AND SIX TENTHS BILLION DOLALRS- WAS EARMARKED FOR THE PAYMENT OF FEDERAL INCOME TAXES ON THE ADDITIONAL AMOUNT OF UTILITY REVENUES.

The one and six-tenths billion dollars charged to customers for incremental Federal income taxes supposedly due on rate increases in 1975 was three times the amount of Federal income taxes actually paid by electric utilities on their <u>total</u> operating revenues in 1974. How is it that customers can be charged one billion dollars more for taxes in a single year of rate increases than the entire electric utility industry paid for Federal income taxes on total revenues the previous year?

The answer lies in the extensive array of complicated tax benefits which were available to electric utilities in 1974. Since 1974, Congress has provided more benefits by raising the investment tax credit for utilities from four to ten per cent, and removing the restrictions on its applicability.

The major problem with existing, complex provisions to aid electric utilities is that they do not also benefit consumers hard-pressed by vastly increased electricity rates. Many Members of Congress have mistakenly believed that voting for complicated accelerated depreciation and investment tax credit provisions would reduce rates for consumers.

THE PRESENT TAX BENEFITS FOR INVESTOR-OWNED ELECTRIC UTILITIES DO NOT GENERALLY PASS THROUGH TO CONSUMERS BECAUSE THE ELECTRIC UTILITIES CONTINUE TO CHARGE CUSTOMERS FOR FEDERAL INCOME TAXES AS IF THE TAX BENEFITS DID NOT EXIST. THE ELECTRIC UTILITIES ARE ABLE TO DO THIS WITH THE AID OF SOPHISTICATED ACCOUNTING TECHNIQUES WHICH PERMIT THEM TO KEEP TWO SETS OF BOOKS - ONE SHOWING LITTLE OR NO TAXES OWED FOR USE BY THE IRS, AND ONE SHOWING SUBSTANTIAL TAXES OWED FOR USE IN SETTING RATES.

THE DIFFERENCE CAN BE QUITE DRAMATIC. FOR EXAMPLE, A REGULATORY COMMISSION WHICH DETERMINES THAT A UTILITY NEEDS AN INCOME INCREASE OF TEN MILLION DOLLARS MAY ORDER A RATE INCREASE FOR CUSTOMERS OF ALMOST TWENTY MILLION DOLLARS. THE DOUBLING OF THE INCOME REQUIRED TO DETERMINE THE RATES CHARGED CUSTOMERS IS TO PERMIT THE ELECTRIC UTILITIES TO PAY FEDERAL INCOME TAXES AT THE THEORETICAL FORTY-EIGHT PER CENT ON THE AMOUNT OF RATE INCREASE, AND STILL HAVE TEN MILLION DOLLARS LEFT FOR INCOME.

OF COURSE, NEARLY ALL INVESTOR-OWNED ELECTRIC UTILITIES PAY LITTLE OR NO FEDERAL INCOME TAXES. INSTEAD, THEY KEEP THE EXTRA MONEY CHARGED FOR TAXES, AND CUSTOMERS ARE LEFT HOLDING THE BAG BECAUSE OF A FINE POINT OF ACCOUNTING THEORY.

THE PROCESS OF CHARGING CUSTOMERS FOR INCOME TAXES WHICH ARE NOT PAID TO THE FEDERAL GOVERNMENT HAS LED TO VAST OVERCHARGES THAT ARE NOT RELATED TO INCREASED COSTS OF SERVICE. AT THE END OF 1974, THE INVESTOR-OWNED ELECTRIC UTILITIES WERE HOLDING FIVE AND THREE-TENTHS BILLION DOLLARS WHICH HAD BEEN CHARGED TO CUSTOMERS FOR FEDERAL INCOME TAXES.

PAST EXPERIENCE INDICATES THAT CUSTOMER MONEY BEING KEPT BY UTILITIES FOR FEDERAL INCOME TAXES WILL NEVER BE PAID TO THE THE FEDERAL GOVERNMENT. NEW TAX DEFERRALS AND CREDITS ALWAYS EXCEED PAST TAX OBLIGATIONS COMING DUE, SO THE TOTAL AMOUNT OF KEPT TAXES IS CONSTANTLY INCREASING.

MY BILL EXTENDS THE FEDERAL INCOME TAX BENEFITS GIVEN ELECTRIC UTILITIES TO THEIR CUSTOMERS. BY EXEMPTING ELECTRIC UTILITIES FROM THE FEDERAL INCOME TAX LAWS, THEY WILL NO LONGER BE ABLE TO CLAIM A ONE HUNDRED PER CENT BONUS ON EVERY RATE INCREASE, BASED ON A CHARGE FOR FEDERAL INCOME TAXES THAT WILL NEVER BE PAID.

THE INVESTOR-OWNED ELECTRIC UTILITIES WILL BENEFIT FROM S. 2213 BECAUSE IT ASSURES THAT THEY WILL REMAIN FREE FROM THE BURDEN OF PAYING FEDERAL INCOME TAXES. THEIR CUSTOMERS WILL BENEFIT FROM S. 2213 BECAUSE ELECTRIC RATES WILL NOT INCLUDE ALLOWANCES FOR UNPAID FEDERAL INCOME TAXES.

A DECISION BY A REGULATORY COMMISSION THAT AN ELECTRIC UTILITY NEEDS INCREASED INCOME OF TEN MILLION DOLLARS WILL RESULT IN A RATE INCREASE FOR CUSTOMERS OF TEN MILLION DOLLARS, NOT TWENTY MILLION DOLLARS.

THE GOAL OF REGULATORY REFORM WILL ALSO BE ADVANCED SIGNIFICANTLY BY ENACTMENT OF S. 2213. THE CONFUSION AND EXPENSE RESULTING FROM TWO SETS OF BOOKS, SPECIAL TAX ACCOUNTS, COMPLEX ACCOUNTING PROCEDURES, AND VOLUMINOUS RECORD-KEEPING WOULD BE ELIMINATED FROM RATE PROCEEDINGS.

FEDERAL INTERFERENCE IN STATE REGULATORY PROCEEDINGS THROUGH TAX PROVISIONS WOULD BE STOPPED BY ENACTMENT OF MY BILL. FOR EXAMPLE, SECTION 46(E) OF THE INTERNAL REVENUE CODE REQUIRES THAT REGULATORY COMMISSIONS PERMIT ELECTRIC UTILITIES TO COLLECT A PROFIT FROM CUSTOMERS ON KEPT TAXES RELATING TO UNAMORTIZED INVESTMENT TAX CREDITS.

BEFORE SECTION 46(E) WAS ENACTED BY CONGRESS IN 1971, THE VAST MAJORITY OF STATE REGULATORY COMMISSIONS HAD DECIDED THAT IT WAS UNFAIR TO REQUIRE UTILITY CUSTOMERS TO PAY A PROFIT ON FUNDS THEY HAD PREVIOUSLY PAID TO THE UTILITY FOR FEDERAL INCOME TAXES.

SECTION 46(E) DENIES STATE REGULATORY COMMISSIONS THE ABILITY TO EXERCISE THEIR SOUND DISCRETION IN SETTING FAIR ELECTRIC RATES FOR THEIR CITIZENS. ENACTMENT OF S. 2213 WOULD RESTORE TO THE STATES COMPLETE AUTHORITY TO DETERMINE THE FAIRNESS OF ELECTRIC RATES.

EXEMPTING ELECTRIC UTILITIES FROM THE FEDERAL INCOME TAX LAWS MAY ACTUALLY INCREASE UNITED STATES TREASURY RECEIPTS. IN 1974, SHAREHOLDERS OF SOME ELECTRIC UTILITIES RECEIVED A TOTAL OF SIX HUNDRED AND FORTY-NINE MILLION DOLLARS IN DIVIDENDS WHICH WERE NOT SUBJECT TO PERSONAL FEDERAL INCOME TAXES.

THIS WAS AN UNINTENDED BENEFIT WHICH CONGRESS HAS UNSUCCESSFULLY TRIED TO CORRECT. ENACTMENT OF S. 2213 WILL ENSURE THAT ELECTRIC UTILITY DIVIDENDS ARE FAIRLY TAXED BY THE FEDERAL GOVERNMENT.

S. 2213 WOULD REFORM TAX-RELATED ABUSES IN SETTING ELECTRIC RATES BY SIMPLY EXEMPTING ELECTRIC UTILITIES FROM THE PROVISIONS OF THE INTERNAL REVENUE CODE. ANOTHER APPROACH WOULD BE TO REFORM ACCOUNTING PROCEDURES WHICH HAVE BEEN DEVELOPED TO PROVIDE LEGITIMACY FOR THESE ABUSES OF THE REGULATORY SYSTEM.

THE REPORTS, ACCOUNTING AND MANAGEMENT SUBCOMMITTEE, OF WHICH I AM CHAIRMAN, HAS BEEN STUDYING THE DEVELOPMENT AND APPLICATION OF ACCOUNTING PROCEDURES THAT HAVE RESULTED IN MISLEADING AND INCONSISTENT INFORMATION BEING REPORTED TO THE PUBLIC. ONE OF THE MAJOR PROBLEM AREAS IN ACCOUNTING IS THE USE OF MORE THAN ONE SET OF BOOKS TO REPORT DIFFERENT FINANCIAL RESULTS TO DIFFERENT PARTIES.

Common sense often gives way to absurd, but expedient accounting theories when corporations are required to report on the results of their activities to governmental authorities or the public. Unfortunately, accounting for Federal income taxes in setting electric rates has been one of the most fruitful areas of resourceful creativity in developing misleading accounting procedures.

I received the Treasury Department's comments on S. 2213 only last Thursday, but its objections to my bill demonstrate some of the problems I have described.

Treasury points out that five hundred and twenty-eight million dollars is too much revenue for the Treasury to lose. Treasury does not mention the five and three-tenths billion dollars of unpaid Federal income taxes which electric utilities were keeping at the end of 1974.

If utility customers were not overcharged that amount, that money would undoubtedly be spent in other sectors of our economy, including such depressed areas as automobiles and housing. Those expenditures would probably yield more tax revenues for the Federal government than would be lost by enactment of S. 2213.

The Treasury Department also states that the losses and meager income shown by electric utilities for Federal income tax purposes is a more realistic indication of their true earnings than publicly reported utility earnings. Even the investor-owned electric utilities and their high-priced tax lawyers and accountants have not tried to push that nonsense.

Our studies clearly indicate that accounting procedures used by utilities in reporting to the public are developed with a primary concern for promoting the utilities' interests.

Finally, the Treasury Department believes that S. 2213 conflicts with the "goal of achieving increased energy independence" by wastefully encouraging energy consumption. We know that it is a major policy of the present Administration to raise the cost of basic and necessary energy supplies for consumers.

Congress has not accepted that policy, and I believe such a policy disregards the magnitude and effects of cost increases which have already occurred.

The electric utilities have not supported S. 2213 because, unlike their customers, they have successfully turned the concept of Federal income taxation into a cost-free source of ready cash. They call it 'cash flow', and speak of the benefits existing Federal tax policies bring to customers.

I CALL IT TAX-KEEPING, AND SAY THAT IT IS UNFAIR TO REQUIRE HARD-PRESSED RESIDENTIAL CUSTOMERS AND BUSINESSMEN TO PAY "PHANTOM" FEDERAL INCOME TAXES. I HAVE NOT YET MET A CUSTOMER WHO BELIEVES THAT HE SHOULD PAY FOR PROPERTY USED BY MONOPOLIES TO PROVIDE BASIC AND NECESSARY ELECTRIC SERVICE AT A HEALTHY PROFIT.

HOWEVER, I HAVE HEARD FROM ANGRY CUSTOMERS WHO ARE OUTRAGED AT BEING CHARGED FOR FEDERAL INCOME TAXES WHICH ARE NOT BEING PAID BY THEIR ELECTRIC UTILITIES.

MILLIONS OF CUSTOMERS CAN NO LONGER AFFORD THE UNNECESSARY AND EXTRAVAGANT "CASH-FLOW" PROVISIONS FOR ELECTRIC UTILITIES WHICH ARE EMBEDDED IN THE PRESENT FEDERAL TAX LAWS.

I URGE THAT THIS COMMITTEE GIVE SERIOUS CONSIDERATION TO S. 2217 AND THE REFORM IT WOULD BRING TO THE PROCESS OF SETTING ELECTRIC RATES. I ALSO URGE THAT THE FINANCE COMMITTEE STAFF WORK WITH THE STAFF OF MY SUBCOMMITTEE IN FURTHER EXPLORING THE WAYS IN WHICH ACCOUNTING PROCEDURES BRING CONFUSION AND INEQUITY INTO THE COMPUTATION OF FEDERAL INCOME TAXES.

I BELIEVE THAT A JOINT EFFORT WOULD BE VERY HELPFUL TO CONGRESS IN REFORMING OUR TAX LAWS, AND UNDERSTANDING THE IMPORTANCE OF PROPER ACCOUNTING PROCEDURES.

Mr. Chairman, I would like to submit for the record a list of my remarks in the Congressional Record concerning Federal income taxes paid by electric utilities. Those remarks contain much detail which I have omitted from my testimony today. I also include for the record a copy of my amendment 1840 to H.R. 10612, with correction of two typographical errors in the printing of that amendment.

I also submit for the hearing record an article from the 13 September, 1975 Philadelphia Inquirer. It shows how utility consumers are overcharged for phantom Federal taxes.

In this instance Philadelphia Electric based a 1974 rate increase request, in part, on a projected Federal tax payment of one hundred and two million dollars that year.

The state utility commission, which eventually granted most of the rate-increase request, contended that the company would have to pay only ninety-one million dollars in Federal taxes.

But, as it turned out, the company did not pay a cent of Federal income taxes in 1974, despite earnings of one hundred and twenty-nine million dollars.

Instead, the company accumulated tax credits of more than eleven million dollars.

THAT IS THE COSTLY EFFECT OF THE PRESENT LAW ON THE CONSUMERS OF JUST ONE UTILITY IN ONE STATE.

BUT, MR. CHAIRMAN, THE MOST OUTRAGEOUS PART OF THE UTILITY TAX RIP-OFF IS YET TO COME, IF THE UTILITIES GET THEIR WAY.

THEY WANT TO SELL THEIR UNUSED TAX CREDITS!

THE BOARD CHAIRMAN OF PACIFIC POWER AND LIGHT, DON C. FRISBEE, TESTIFIED ON THAT POINT BEFORE THE WAYS AND MEANS COMMITTEE LAST YEAR.

HE RECOMMENDED THAT UTILITIES BE ALLOWED TO SELL UNUSED INVESTMENT TAX CREDITS. I WONDER HOW MUCH THAT WOULD COST THE TREASURY, WHICH DID NOT EVEN MENTION, IN ITS COMMENTS ON MY AMENDMENT, THE MORE THAN FIVE BILLION DOLLARS THE UTILITIES WERE KEEPING AT THE END OF 1974.

SO THE UTILITIES DON'T WANT TO SETTLE FOR JUST BEING TAX-KEEPERS, RATHER THAN TAXPAYERS. THEY WANT THEIR CAKE, THEIR FROSTING, AND THE PAN.

I URGE THIS COMMITTEE TO BRING AN END TO THIS NONSENSE BY ADOPTION OF MY PROPOSAL.

Calendar No. 891

94TH CONGRESS
2D SESSION

H. R. 10612

IN THE SENATE OF THE UNITED STATES

JUNE 14, 1976

Ordered to lie on the table and to be printed

AMENDMENT

Intended to be proposed by Mr. METCALF to H.R. 10612, an Act to reform the tax laws of the United States, viz: At the appropriate place insert the following:

SEC. . EXEMPTION OF ELECTRICAL UTILITIES FROM INCOME TAX.

(a) IN GENERAL.—Section 501 (c) (3) (relating to list of exempt organizations) is amended by adding at the end thereof the following new paragraph:

"(20) A corporation engaged predominantly in the sale of electrical energy, if the rates for such sale have been established or approved by a State or political subdivision thereof, by an agency or instrumentality of the United States, or by a public utility or public service commission or other similar body in the District of Columbia or of any State or political subdivision thereof.".

Amdt. No. 1840

(b) TECHNICAL AND CONFORMING AMENDMENTS.—

(1) Section 46(e)(3) (relating to public utility property) is amended by striking out "electrical energy," in subparagraph (B)(i),

(2) Section 167 (l) (3) (relating to definition of public utility property) is amended by striking out "electrical energy," in subparagraph (A)(i).

(3) Section 247(b)(1) (relating to definition of public utility) is amended to read as follows:

"(1) PUBLIC UTILITY.—The term 'public utility' means a corporation engaged in the furnishing of telephone service or in the sale of gas or water if the rates for such furnishing or sale, as the case may be, have been established or approved by a State or political subdivision thereof or by an agency or instrumentality of the United States, or by a public utility or public service commission or other similar body of the District of Columbia, or of any State or political subdivision thereof.".

(4) Section 7701(a)(33) (relating to definition of regulated public utility) is amended by striking out "electric energy," in subparagraph (A)(i).

(c) EFFECTIVE DATE.—The amendments made by this section apply to taxable years beginning October 1, 1977.

Statements by Senator Lee Metcalf in the Congressional Record Regarding Federal Income Taxation of Investor-Owned Electric Utilities.

11 September, 1974; p. S16345 - Utility Consumers Simonized

29 July, 1975; p. S14090 - Introduction of S. 2213

10 September, 1975; p. S15679 - Competition Keen Among Utilities For Taxkeeper of the Year Award

15 September, 1975; p. S15930 Competition Keen Among Utilities for Tax Keeper of the Year Award - Corrections of Typographical Errors in Tables

4 March, 1976; p. S2901 - The $649 Million Tax-Free Bonanza for Utility Investors

23 March, 1976; p. S3997 - More Tax-Free Dividends for Utilities

14 June, 1976; p. S9136 - Introductory Remarks to Amendment No. 1840 to H.R. 10612 - The Tax Reform Act of 1976

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H.R. 3052 (Mr. Rostenkowski)

TUESDAY, AUGUST 24, 1976

UNITED STATES SENATE, COMMITTEE ON FINANCE

TESTIMONY OF WALLACE D. BARLOW, EXECUTIVE DIRECTOR, STOCK OPTION WRITER'S ASSOCIATION, 6210 MASSACHUSETTS AVENUE, BETHESDA, MARYLAND.

I am Wallace Barlow of Bethesda, Maryland. I have been trading in stock options for the last 48 years. I appear today on behalf of the independent stock option writers, whose existence has been threatened by H.R. 3052; (also by H.R. 12224 (Mikva), which has now been added to the so-called "tax reform" bill.

This bill would transfer income from the pockets of the independent writers to the pockets of the tax exempt organizations. Our option lapse income would be taxed at ordinary income rates; theirs would no longer be considered "unrelated business income" and would NOT be taxed.

How important is option lapse income to the writer, (or seller), of stock options? My own experience is typical. In the last ten years, an average of 66% of our options lapsed. In 1973, 79% lapsed and in the first half of 1976, 40% lapsed. In 1975, our option lapse income was 80% of the total; dividends were 20%; capital gains were zero.

H.R. 3052 is, in effect, a private bill for the relief of the Chicago Board Options Exchange, (CBOE); also the ASE and the PBW exchanges, in that it would enlarge their markets. In this new market, the exempt organizations would have an unfair advantage over the independent writers.

Already, since the advent of "listed" options, in 1973, most of the independent writers are bankrupt. The few remaining writers of conventional, (or non-listed), options have suffered, in that premiums on the listed options are much lower than on the non-listed options. In 1976, to date, our annualized premiums as a percentage of the amount at risk, amounted to 44.9% on the non-listed calls and 21.6% on the listed calls.

We need 45% per year to survive, since our investment may be ten times as large as that of the buyer. Also, we need a cushion to protect us against the accumulation of "rejects". For example, when Canadian Javelin fell from $21 to $2, and was de-listed, we gained some option lapse income. However, we stand to lose far more than this on the ultimate sale, or charge off, of 2200 shares.

We regard H.R. 3052 as rank and offensive discrimination and we ask the Committee to protect our people against the ruinous competition of tax exempt organizations.

Thank you for the privilege of testifying.

W. Barlow

Wallace D. Barlow

Summary of Statement

of

Leon Pomerance

on Behalf of

the Chicago Board Options Exchange

Before the

Senate Committee on Finance

August 24, 1976

The Chicago Board Options Exchange ("CBOE") strongly supports H.R. 3052 which removes a barrier to the participation in the options markets on the part of exempt organizations. Present law unnecessarily discourages exempt organizations from writing options to buy or sell securities by inconsistently applying the unrelated business income tax to certain income which exempt organizations receive from writing options.

Most exempt organizations are acutely aware of their need for additional funds. One effective method to increase the yield from their securities portfolio is an investment strategy known as "covered option writing." In covered option writing, an investor who owns a stock writes a "call" (an option to buy that stock at a specified price within a specified period of time). The option writer foregoes the possible appreciation in the value of the stock during the option period in return for the premium he receives when he writes the option. This premium income is similar to other passive income, such as dividends, which an exempt organization derives from investment activity and which is not subject to the unrelated business income tax.

The "unrelated business income tax" is imposed on the net income derived from any unrelated trade or business of certain exempt organizations. However, the unrelated business income tax is not applicable to investment income such as dividends, interest, annuities, royalties, and capital gains from the sale of investment assets. Under present law there is an anomaly in the application of the unrelated business income tax to exempt organizations. If an exempt organization writes an option which is later exercised, the gain or loss realized upon the exercise is treated as capital gain or loss, and is thus exempt from the unrelated business income tax. In contrast, if the option lapses or the organization terminates its obligation under the option by entering into a closing transaction, the gain or loss is treated as ordinary income or loss and is subject to the unrelated business income tax.

H.R. 3052 amends Internal Revenue Code §512(b)(5) to exclude from the term "unrelated business taxable income" all gains on the lapse or termination of options to buy or sell securities, if the options have been written in connection with an exempt organization's investment activities. Thus, H.R. 3052 removes the anomaly in present law: the change would bring the tax treatment of lapse and closing transaction income into line with other passive income derived by an exempt organization from its investment activities.

Sound tax policy dictates that H.R. 3052 should be adopted. First, for more than four years the Congress has attempted to make this change and has recognized that all passive investment income derived from an exempt organization's investment activities should be treated consistently: not subject to the unrelated business income tax. Income from lapses or terminated options is such passive investment income.

Second, the inconsistent treatment of income from options should be corrected, since such treatment discourages exempt organizations from writing options in their overall investment strategy. When an exempt organization writes a call option, it cannot know whether that option will be terminated through exercise, lapse, or closing transaction. The possibility that the unrelated business income tax will apply to the income derived from writing options deters some exempt organizations from writing options. We do not feel that the Congress intends to discourage option writing on the part of exempt organizations in this manner.

Finally, the purpose of the unrelated business income tax -- to prevent tax exempt businesses from unfairly competing with taxable businesses -- is not furthered by applying the tax to income derived from the lapse of, or closing transaction in, options written by exempt organizations in connection with investment activities. Production of investment income, such as capital gains, by exempt organizations simply does not involve competition with taxable businesses.

H.R. 3052 is closely related to an amendment to H.R. 10612 (the Tax Reform Act of 1976), and H.R. 12224 which passed the House on July 20, 1976. The amendment to H.R. 10612 and H.R. 12224 are substantiallly the same and relate to the tax treatment of income derived from writing options. These provisions correct another example of inconsistent treatment of transactions in options, and amend Internal Revenue Code §1234 to provide that gain on the lapse of, and gain or loss from any closing transaction in, options shall be treated as short-term capital gain or loss.

The CBOE supports the principles of consistency and neutrality in the tax treatment of options and believes that those principles underlie the amendment to H.R. 10612 and H.R. 12224. We therefore supported H.R. 12224 in testimony before the Ways and Means Committee and suggested changes which were ultimately adopted in that bill. We wish to point out that the amendment to H.R. 10612 and H.R. 12224 will be disruptive to transactions on our exchange and other options exchanges if they were to contain an effective date which is significantly prior to the date on which the bill is enacted into law. Since these provisions change the character of gain on the lapse of, and gain or loss from any closing transaction in, options from ordinary income to short-term capital gain, investors will be uncertain about the tax treatment of their transactions in options between the effective date of the bill and the date of enactment. Such uncertainty will deter many transactions. We believe that both the House and the Senate recognized and appreciated the severity of this problem and wrote into H.R. 12224 and the amendment to H.R. 10612 an effective date which is their estimates of when the bill would likely be enacted into law. We trust that the Conference Committee will establish an effective date which is not prior to the date of the provision's enactment.

STATEMENT OF

LEON POMERANCE

ON BEHALF OF

THE CHICAGO BOARD OPTIONS EXCHANGE

BEFORE THE

SENATE COMMITTEE ON FINANCE

AUGUST 24, 1976

I am Leon Pomerance, Chairman of the Board of Directors of the Chicago Board Options Exchange. With me are Daniel B. Skelton, Vice President of the Exchange, and Ernest S. Christian, Jr., special tax counsel.

The Chicago Board Options Exchange ("CBOE") is a national securities exchange registered under the Securities Exchange Act of 1934. It was the first exchange in the United States to provide a central marketplace for trading option contracts for the purchase and sale of stock, popularly known as "puts" and "calls". The CBOE has overcome the deficiencies of the over-the-counter market by providing an efficient and continuous options market in which a position previously taken can be liquidated at any time. At the present time, trading exists in call options on stocks which are listed on the New York and American Stock Exchange. The CBOE expects that trading in puts will begin soon, and that the number of listed stocks in which options are traded will be increased.

CBOE's Position on H.R. 3052

The CBOE strongly supports H.R. 3052 which removes a barrier to the participation in the options market on the part of exempt organizations. H.R. 3052 modifies the provisions of present law which unnecessarily discourage exempt organizations from writing options by applying the unrelated business income tax to certain income which exempt organizations receive from writing options to buy or sell securities.

The Importance of Option Writing to Exempt Organizations

The options exchanges provide exempt organizations with an important new source of income from their investment activities. The options markets, as sources of additional funds, are important to most exempt organizations, particularly colleges and universities, since they cannot attract sufficient funds from contributions or grants, and therefore must look to their investments for additional income.

An investment technique, known as "covered option writing," is a low-risk investment strategy and should not be discouraged by the tax law. On the contrary, the covered writer risks only the possible appreciation in the value of the stock during the option period. The writer foregoes this potential growth in return for the premium he receives when he writes the option. This premium income is similar to other passive income, such as dividends, which an exempt organization derives from investment activity and which is not subject to the "unrelated business income tax."

Covered option writing may be illustrated by an example. Assume that a university has stock in its portfolio with a value of $10,000 on January 1, 1976, and that it intends to hold the stock as a long-term investment. The stock will undoubtedly fluctuate in value; and at the end of the year, the university will have an unrealized gain or loss on the stock. However, except to the extent that the university has received a dividend on the stock during the year, it will not have realized any income from its investment.

Instead, suppose that the university writes a call option with a $10,000 strike price on January 1, and receives a premium of $1,000 for doing so. If the stock declines in value or even remains the same during the option period, the option will become worthless and will not be exercised. The university will realize $1,000 of income when the option lapses, and will also retain the stock which will then have a value of $10,000 or less. Alternatively, if the stock increases in value during the option period, the option will probably be exercised. The university will realize the same $1,000 premium from writing the option, but rather than having the stock with a value in excess of $10,000, it will receive $10,000 in cash for reinvestment.

Present Tax Treatment of Option Writing by Exempt Organizations

The "unrelated business income tax" is imposed on the net income derived from any unrelated trade or business of certain exempt organizations. However, the unrelated business income tax is not applicable to investment income such as dividends, interest, annuities, royalties, and capital gains from the sale of investment assets.

Under present law, there is an anomaly in the application of the unrelated business income tax to exempt organizations. The tax treatment of income which an exempt organization derives from writing puts and calls depends on whether the option is exercised, lapses, or is terminated in a closing transaction. If an exempt organization writes a call in connection with its investment activities and the call is exercised, the underlying stock is sold by the exempt organization. The premium previously received for writing the option is treated as part of the capital gain or loss from the sale of the underlying stock. If a gain has occurred, the entire gain on the sale, including part or all of the premium, is not taxed since present Internal Revenue Code § 512(b)(5) provides that "unrelated business taxable income" excludes all gains or losses from the sale, exchange, or other disposition of capital assets.

On the other hand, the anomaly arises if an option written by an exempt organization is not exercised, and the option lapses or the writer terminates his obligation under the option by entering into a closing transaction. In the case of both a lapse and a closing transaction, any gain or loss realized is classified as ordinary income or loss rather than capital gain or loss. The Internal Revenue Service has ruled that income realized by an exempt organization from call options which lapse is income subject to the unrelated business income tax. Rev. Rul. 66-47, 1966-1 C.B. 149.

The Change in Present Law Effected by H.R. 3052

H.R. 3052 amends Code § 512(b)(5) to exclude from the term "unrelated business taxable income" all gains on the lapse or termination of options to buy or sell securities, if the options have been written in connection with the exempt organization's investment activities. Thus, H.R. 3052, which has Treasury Department support, removes the anomaly in present law: the change would bring the tax treatment of lapse and closing transaction income into line with other passive income derived by an exempt organization from its portfolio securities.

Reasons for the Change Made by H.R. 3052

More than four years ago, in reporting H.R. 11196 (a bill similar to H.R. 3052), the Committee on Ways and Means recognized that income from lapse or termination of an option should not be treated differently from income upon the exercise of an option, when the options have been written in connection with investment activities of the organization. The Committee concluded that in such circumstances both types of income should be exempt from the unrelated business income tax because both types constitute investment income traditionally exempted from that tax. H.R. 3052

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again recognizes that the taxation of income from options which are written by exempt organizations and which lapse or are terminated is inconsistent with the generally tax-free treatment accorded to exempt organization's income from investment activites.

The inconsistent treatment of income from option transactions by exempt organizations should be corrected, since such treatment discourages exempt organizations from using options in their overall investment strategy. When the university in the above example writes a call option, it cannot know whether that option will be terminated through exercise, lapse, or closing transaction. As explained, the covered writer foregoes part of the possible appreciation in the value of the stock during the option period in reutrn for the premium it receives when it writes the option. To the extent that under some circumstances (i.e., lapse or closing transaction) the premium may be taxed as unrelated business taxable income, this potential tax will deter some exempt organizations from writing options. We do not feel that the Congress intends to discourage option writing -- a basically conservative investment strategy -- on the part of exempt organizations.

Finally, the purpose of the unrelated business income tax -- to prevent tax-exempt businesses from unfairly competing with taxable businesses -- is not furthered by applying the tax to income derived from the lapse of, or closing transaction in, options written by exempt organizations in connection with investment activities. The production of investment income, such as capital gains, by exempt organizations simply does not involve competition with taxable businesses. All of this passive investment income, including gains from the lapse or closing transactions in options, should therefore be exempt from the unrelated business income tax.

H.R. 3052 and the Percy Amendment No. 325 to H.R. 10612 (Tax Reform Act of 1976)

In addition to our testimony in support of H.R. 3052, the CBOE believes that it would be remiss if it did not point out to the Committee the closely related provisions of Amendment No. 325 to H.R. 10612 (Tax Reform Act of 1976) which amendment was offered by Senator Percy and agreed to on August 6, 1976, and H.R. 12224 which is substantially the same as the Percy amendment and was passed by the House on July 20, 1976. The Percy amendment and H.R. 12224 deal with another example of inconsistent treatment of transactions in options, and amend Internal Revenue Code §1234 to provide that gain on the lapse of, and gain or loss from any closing transaction in, options shall be treated as short-term capital gain or loss. Investors who buy and sell stocks and securities receive capital treatment for gains and losses derived from their investment activities. Similarly, investors who buy and then resell options receive capital treatment on their gains and losses. The inconsistency in present law occurs in the tax treatment of option writers whose options lapse or are terminated through a closing transaction. Under rulings from the Internal Revenue

Service, gain or loss derived by an option writer from the lapse of, or closing transaction in, options is ordinary income or loss to the option writer. The Percy amendment and H.R. 12224 remove the inconsistency in present law by providing that a writer's gain on the lapse of, and gain or loss from any closing transaction in, options is treated as short-term capital gain or loss.

Removal of this inconsistency was the subject of extensive public hearing in the Committee on Ways and Means, is supported by the Treasury and results in a revenue gain of about $10 million.

Options traded on the CBOE should be taxed no more and no less favorably than other similar securities and transactions. We support the principles of consistency and neutrality in the tax treatment of options and believe that those same principles underlie the Percy amendment and H.R. 12224. We therefore support those provisions.

We wish to point out that the Percy amendment and H.R. 12224 will be disruptive to transactions on the CBOE and other options exchanges if they were to contain an effective date which is significantly prior to the date on which the bill is enacted into law. H.R. 12224 changes the character of gain on the lapse of, and gain or losss from any closing transaction in, options from ordinary income to short-term capital gain. Thus, it can readily be appreciated that between the effective date of the bill and the date of enactment investors will be uncertain about the tax treatment of their transactions in options and will therefore be deterred from making commitments which they otherwise would have made.

We believe that the Committee on Ways and Means recognized and appreciated the severity of this problem and wrote into H.R. 12224 an effective date which reflected its judgment concerning when the provision would likely be enacted into law. Similarly, in adopting the Percy amendment to H.R. 10612, the Senate provided for an effective date of September 1, 1976, which is its estimate of when the provision would likely be enacted into law. We trust that the Conference Committee will establish an effective date which is not prior to the date of the provision's enactment, and thus will avoid retroactive treatment of investors.

In conclusion, Mr. Chairman, we thank you for your attention and consideration of our views concerning these two important provisions relating to the tax treatment of options.

STATEMENT OF THE DISTILLED SPIRITS COUNCIL OF THE U.S., INC.

Before the Committee on Finance, U.S. Senate, in Support of HR 3055

The Distilled Spirits Council of the U.S., Inc. (DISCUS), the national trade association of the domestic distilling industry, whose members produce approximately 95% of all distilled spirits produced in the United States, supports the provisions of HR 3055 for the reasons set forth in attachment A to this statement (attachment A sets forth the purposes of each section, the revenue impact, if any, and the reasons in support of enactment). Attachment B is a section by section explanation of HR 3055.

The bill would simplify and encourage the exportation of distilled spirits. In addition, the bill would liberalize the removal of samples for research, development, or testing and would relax existing requirements for the mingling and blending of distilled spirits in bond. Production of gin with greater uniformity and without loss in quality would be permitted. Finally, the bill would extend to bulk spirits brought into the United States from Puerto Rico or the Virgin Islands the same loss provisions presently applicable to imported and domestic spirits thereby curing an inequity in the present law.

There would be no loss of revenue as a result of the amendments contained in the bill; there would be a short-term lag in revenue of an undetermined, but not major, amount resulting from Section 3 of the bill.

In keeping with our need and desire to improve our export position in all fields, DISCUS urges adoption of these amendments. We appreciate this opportunity to present our views on pending legislation and request favorable consideration.

SUMMARY OF PRINCIPAL POINTS
Included in the Statement of Distilled Spirits Council of the U.S., Inc.
Before the Committee on Finance, U.S. Senate, in Support of HR 3055

A. Benefits of Bill:

1. Simplification of export procedures

2. Liberalization and simplification of plant procedures

3. Equalization of loss provision applicable to all distilled spirits

B. Revenue Effect:

1. No loss of revenue

2. Short term lag in revenue in minor amounts

ATTACHMENT A

Summary of Provisions of H. R. 3055
94th Congress, First Session

A. Sets forth the purpose of the Section

B. The revenue impact, if any

C. The reasons in support of enactment

Section 1

a) Would eliminate the requirement of showing on the label of gin and vodka bottled in bond for export the name of the distiller.

b) Revenue effect - none.

c) Would simplify the labeling of gin and vodka for export and thereby facilitate export sales.

Section 2

a) Would extend to bulk imported goods which are bottled in the United States for export the same tax benefits presently permitted for domestically produced goods bottled for export.

b) Revenue effect - none.

c) Would broaden market for goods to be exported from the United States.

Section 3

a) Would create an export facility on distilled spirits plant premises.

b) Revenue effect - no loss of revenue but a short-term lag in revenue of undetermined, but not major, amount.

c) Would simplify export procedures and encourage further development of export markets.

Section 4

a) Would liberalize export procedures by permitting transfer to any Customs-bonded warehouse for export.

Section 8

a) Would extend to bulk spirits brought into the United States from Puerto Rico or the Virgin Islands the same loss provisions made applicable to imported and domestic spirits.

b) Revenue effect - none.

c) Would correct an oversight in prior law whereby loss allowances applicable to domestic and imported spirits were not made applicable to products from Puerto Rico and the Virgin Islands.

Section 9

Provides only for effective date.

ATTACHMENT B

H.R. 3055

94th Congress - First Session

EXPLANATION OF THE BILL

This bill makes a series of amendments to the distilled spirits plant provisions of the Internal Revenue Code which in general are designed to remove restrictions which are not necessary for effective enforcement of the revenue and regulatory aspects of these provisions and which would facilitate and encourage exportations. These amendments will have no adverse effect on the revenue. They can be summarized as follows:

SECTION 1. NAME OF DISTILLER ON LABEL OF GIN AND VODKA BOTTLED IN BOND FOR EXPORT.

Section 1 of the bill would eliminate the requirement of showing, on the label of gin and vodka bottled in bond for export, the name of the distiller. Such information serves no useful purpose, and since gin and vodka are produced from neutral spirits, compliance with the statute means showing the distiller of the neutral spirits which may be a person different from the producer of the gin or vodka; the showing of such distiller on the label could even be deceptive to the consumer.

SECTION 2. DRAWBACK FOR BULK IMPORTED GOODS BOTTLED IN UNITED STATES.

Section 2 of the bill would authorize allowance of drawback of tax on bulk imported goods which are bottled in the United States and exported therefrom. Because of the limitation to goods "manufactured or produced in the United States" in existing law, imported distilled spirits are not subject to drawback under section 5062(b). However, by virtue of section 5523, IRC, reduction in proof and bottling or packaging are deemed to constitute manufacturing under section 311 of the Tariff Act of 1930. (19 U.S.C. 1311) This amendment would make the export standards of Sec. 5062(b) consistent with those in Section 311.

SECTION 3. DISTILLED SPIRITS RETURNED TO BONDED PREMISES.

Section 3 of the bill would permit the bottler or packager to return to an export storage facility on bonded premises distilled spirits which would be eligible for drawback under Section 5062(b). The return of the spirits must be solely for the purpose of storage pending withdrawal for export, or other withdrawal without payment of tax authorized under Section 5214(a), or free of tax under Section 7510.

This section also permits the bottler to return to appropriate storage facilities on the bonded premises distilled spirits which he had bottled in bond after tax determination. Such spirits may be withdrawn for any purpose for which distilled spirits bottled in bond before tax determination may be withdrawn from bonded premises.

Appropriate amendments are made to provide for the remission, abatement, credit, or refund of tax on spirits returned to bonded premises under this section.

The amendments made by this section are designed to simplify and encourage export transactions.

SECTION 4. WITHDRAWALS TO CUSTOMS BONDED WAREHOUSES.

Section 4 of the bill would authorize withdrawal of distilled spirits from bonded premises without payment of tax for transfer to any customs bonded warehouse. This provision applies to spirits bottled in bond for export and to spirits returned to bonded premises under section 5215(b). The amendment is designed to simplify and encourage export transactions.

SECTION 5. REMOVAL OF SAMPLES FOR RESEARCH, DEVELOPMENT, OR TESTING.

Section 5 of the bill would make a reasonable extension of the purposes for which samples may be removed without payment of tax to include plant research in addition to laboratory analysis. This amendment is similar to the recent amendment to Section 5053 relating to beer.

SECTION 6. MINGLING AND BLENDING OF DISTILLED SPIRITS.

Section 6 of the bill would permit distilled spirits plant proprietors to commingle distilled spirits within 20 years of the date of original entry rather than the existing 8 years. The section also eliminates the requirements of existing law that the mingled spirits be placed in the same barrels and that the mingling must be for further storage in bond. Proper administration of the distilled spirits tax and regulatory provisions does not require the limitations on commingling to 8 years or the return of the distilled spirits to bonded storage. From a practical standpoint, the use of the same package is an unnecessary restriction.

SECTION 7. USE OF JUNIPER OILS IN PRODUCTION OF GIN.

Section 7 of the bill would authorize the use of the extracted oils of juniper berries and other aromatics in the production of gin without incurrence of the rectification tax in addition to the present system of redistillation of a pure spirit over juniper berries and other aromatics. This amendment will permit production of gin with greater uniformity and without loss in quality.

SECTION 8. LOSS PROVISIONS FOR SPIRITS BROUGHT IN FROM PUERTO RICO AND THE VIRGIN ISLANDS.

Section 8 would extend to bulk spirits brought into the United States from Puerto Rico or the Virgin Islands the same loss provisions now applicable to imported and domestic spirits.

Due to an oversight when the law was amended to permit entry of such spirits into bond the provisions applicable to imported and domestic spirits were not extended to spirits brought in from Puerto Rico or the Virgin Islands. Enactment of this section would cure inequities in the present law.

SECTION 9. EFFECTIVE DATE.

The act would become effective on the first day of the first calendar month which begins more than 90 days after enactment. This will give the Treasury Department and the distilling industry sufficient time to modify procedures under the statutes amended.

STATEMENT OF

THE ASSOCIATION OF AMERICAN PUBLISHERS

In Support of Extending H. R. 5161

To Mass Market Paperback Books

Submitted to

The Committee on Finance

United States Senate

August 24, 1976

Summary of Principal Points

1. Proposed Amendment to H. R. 5161 Would Avoid Unjust Discrimination. H. R. 5161 ameliorates a hardship in the magazine distributing business by adopting a tax accounting rule which is more consistent with the generally accepted accounting principle of matching income and expenses. It provides that distributions made primarily for display purposes (and which are returned within 2 1/2 months after the taxable year) are not includible in taxable income. The bill, however, is limited to magazines, and failure to accord display distributions of mass market paperback books the same treatment would result in unjust discrimination between similarly situated taxpayers.

2. Mass Market Paperbacks Meet the Substantive Tests of H. R. 5161. The House bill would prescribe two requirements for determining whether publications have been distributed for display purposes. Mass market paperback publishers and distributors, like magazine publishers and distributors, meet these requirements. In both businesses --

a. Excess quantities of publications, intended for retail display, are distributed with no expectation that they will be sold.

b. Publishers and distributors are legally bound to accept returns of the excess distributions.

3. Mass Market Paperbacks and Magazines Have Other Significant Characteristics in Common. Apart from meeting the substantive requirements of H. R. 5161, mass market paperback books have other characteristics in common with magazines which strongly militate against disparate treatment of the two types of publications. In both businesses --

a. The display distributions are substantial in amount (about 35% for paperbacks). Therefore, treatment of such distributions as completed sales may have a significant distorting effect on taxable income, particularly during periods of inflation.

b. The publications have very short retail shelf-lives.

c. Unsold distributions have little or no economic value and are almost never resold. Display distributions are generally returned in the form of covers which have been stripped from the books.

d. The publications are generally distributed by the same wholesalers, and often to the same retail outlets with the same potential customers.

4. Summary. For the foregoing reasons, the improved accounting method which H. R. 5161 would provide for magazine publishers and distributors should be extended as well to publishers and distributors of mass market paperback books.

STATEMENT OF
THE ASSOCIATION OF AMERICAN PUBLISHERS
IN SUPPORT OF

EXTENSION OF H. R. 5161 TO MASS MARKET PAPERBACK PUBLICATIONS

I. SUMMARY

A. Problem Addressed by H.R. 5161

H. R. 5161, approved by the House of Representatives on August 2, 1976, would go a long way toward eliminating a disparity which exists between the book and income tax accounting of accrual basis taxpayers in the magazine publishing industry.

The disparity arises because, under Internal Revenue Service interpretation, current law does not permit magazine publishers and distributors to deduct from gross income amounts which they place in reserve, in accordance with generally accepted accounting principles, to provide for refunds payable with respect to magazines distributed in a taxable year and returned to them after the close of that year. Such reserves are considered nondeductible for tax purposes even though the publisher or distributor intentionally oversells periodicals to wholesalers to assure adequate display at the retail level and is legally obligated to accept for refund all returns of the excess distributions.

In the periodicals industry, the law as so interpreted may result in significant distortions of taxable income. Excess distributions of periodicals which the parties never expect to be sold are nonetheless included in income. When this occurs in the latter part of the tax year, most returns of the excess distributions are not taken into account until early in the succeeding year. The result is that taxable income may be overstated during periods of rising sales, and understated during periods of declining sales.

Without affecting existing law relating to the nondeductibility of estimated expenses, H. R. 5161 would ameliorate the income-distorting effect on publishers and distributors of periodicals. The House-passed bill, which the Treasury Department has stated it does not oppose, would accord those taxpayers an elective right not to include in income distributions of periodicals made for display purposes (as defined) where the taxpayer can establish, within two and one-half months after the close of the year of distribution, that the periodicals have not been and will not be sold.

B. Position of Association of American Publishers

As described in detail below, accrual basis publishers and distributors of mass market paperback books are in the same tax position as periodicals publishers and distributors.

In both industries

-- large quantities of publications are distributed for display purposes with no expectation that the excess distributions will be sold.

-- the substantial excess distributions which are put on display are in fact a method of advertising for retail sales.

-- publishers and distributors are legally bound to accept all returns of the excess distributions for full refund or credit, and the returns are normally in the form of covers which have been stripped from the books.

-- the two types of publications have very short retail shelf-lives. Publishers release hundreds of new paperbacks on a monthly basis and, because of the scarcity of retail shelf space, many older titles are withdrawn each month.

-- most returns early in a particular tax year are attributable to the prior year's excess distributions, and the returns are almost never resold.

-- the publications are often distributed by the same wholesalers.

-- the two types of publications are often displayed at the same retail outlets with the same potential customers.

Under these circumstances, mass market paperback publishers and distributors have as strong a case as do periodicals publishers and distributors for the relief which H. R. 5161 would provide. Limitation of its provisions to periodicals would create an inequity between similarly situated taxpayers and it is strongly urged that H. R. 5161 be modified to avoid this inequity.

II. EXPLANATION OF H. R. 5161

H. R. 5161 would add a new subsection (e) to section 451 of the Internal Revenue Code. The new provisions would apply to sales of magazines or other periodicals "for display purposes." Such sales are defined in paragraph (2) of H. R. 5161 as those made "in order to permit an adequate display of the magazine or other periodical . . . if at the time of sale the taxpayer has a legal obligation to accept returns of such magazine or other periodical." For transactions meeting this definition, paragraph (1) authorizes accrual basis taxpayers to elect not to include in gross income of the taxable year receipts from sales which are returned by the 15th day of the third month of the next year[1/], or with respect to which the taxpayer otherwise establishes that sales have not occurred and will not occur (in accordance with regulations to be prescribed by the Secretary or his delegate). An election under these provisions would be binding for subsequent years and would otherwise be treated as a method of accounting.

In effect, H. R. 5161 would authorize a tax treatment for excess distributions of magazines which is more consistent with economic realities than is the present treatment. Periodicals publishers and distributors would no longer be required to report artificially created income attributable to shipments in the latter part of the year of excess quantities of periodicals which the parties know will not be sold, provided the taxpayer also eliminates equally artificial off-setting deductions now taken for returns made in the following taxable year. Excess distributions returned within the statutory period would be ignored for purposes of taxation.

1/ The two-and-one-half month cutoff coincides with the date on which corporate tax returns are normally due.

III. REASONS FOR EXTENDING H. R. 5161 TO MASS MARKET PAPERBACK PUBLICATIONS

In its Report on H. R. 5161, the Committee on Ways and Means stated:

> Your committee believes that when periodicals are shipped to retailers for display purposes with no expectation on the part of the parties that these periodicals will be sold, it is not appropriate to treat the shipment as income to the publisher or distributor.

Since mass market paperback books are distributed under substantially the same arrangement, H. R. 5161 should cover these publications as well as magazines and other periodicals.

A. Nature and Size of Mass Market Paperback Business

Mass market paperback books, like periodicals, represent a distinct segment of the publications industry. They are nontechnical paperbacks of standard "rack-size" (approximately 7" by 4-1/2" or smaller) intended for general consumption and characteristically having lower prices and shorter shelf-lives than special interest books or "trade" paperbacks (e.g., those educational publications, reprints of classics, and religious and scientific books which have a limited appeal). For both internal and industry-wide reporting purposes, these characteristics distinguish mass market from other paperback publications. The annual Industry Sales Statistics survey of the Association of American Publishers indicates that mass market paperbacks accounted for approximately $319 million in net sales in 1975.[2/]

2/ Total net sales of all books (hard cover and paperback) by U.S. publishers in 1975 amounted to approximately $3.81 billion.

Distribution of mass market paperback books is highly competitive. It is estimated that the average retail outlet contains fewer than 120 "pockets" for displaying rack-size paperbacks. However, in recent years mass market paperback new releases alone have exceeded 5,000 separate titles annually. Considering the large number of releases of mass market paperback publications, the relatively infrequent use of media advertising and the scarcity of retail display space, it becomes obvious that steps to assure adequate retail display are central to the sales strategies of mass market paperback publishers.

To reach the maximum number of retail outlets, mass market paperbacks, like periodicals, are distributed direct to retailers and through a system of independent wholesalers and jobbers. Indeed, in most cases periodicals and mass market paperbacks are distributed by the same wholesalers. As a result, as described below, the methods of marketing the two types of publications are substantially the same.

B. Distributions for Display by Publishers of Mass Market Paperback Books

Distributions -- technically in the form of sales -- for purposes of display within the meaning of H. R. 5161 are as prevalent in the mass market paperback business as in the periodicals business. Mass market paperback publishers and distributors regularly and deliberately make excess distributions of their publications for the same reason as do periodicals publishers: experience has shown that net sales will suffer unless sufficient quantities of books are shipped to assure adequate display at retail outlets. In a very real sense, for mass market paperbacks, perhaps even more so than for periodicals, the books themselves are their own advertisements. 3/

The Association of American Publishers believes all U. S. mass market paperback publishers employ the sale-for-display marketing technique. As in the periodicals industry, mass market paperback publishers and their customers have no expectation that the excess distributions will in fact be sold. Under agreements with their wholesalers and jobbers, mass market paperback publishers and distributors have a legal obligation to accept for full refund or credit all returns of books not sold at the retail level. The proportion of shipments which are in fact returned is clearly substantial. AAP surveys indicate that 35 to 37 percent of the mass market paperback books shipped in 1^73 through 1975 were returned to the publishers for refund pursuant to legal right and would qualify as sales for display purposes under H. R. 5161.

In brief, excess distributions of mass market paperback publications meet the definition of "sales for display purposes" set forth in H. R. 5161. The excess

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3/ A recent article from the Washington Post which describes the marketing of mass market paperbacks is appended to this memorandum. Based on industry sources the article indicates that "the book has to display well," and "if it displays, it sells." Further, it is stated that "Our ad campaigns are so tiny, they are laughable. We don't rely on grand promotions. Each paperback that we display is an advertisement for itself."

distributions are made to assure adequate display at retail outlets, and mass market paperback publishers and distributors are legally bound to accept all returns. Furthermore, as with periodicals publishers, the distorting effect of treating as income excess distributions of mass market paperbacks may be substantial, since such excess distributions amount to more than one-third of all mass market paperback shipments. And with inflation a continuing problem, the distortion of income problem promises to be even more serious in future years.

C. Short Retail Display Period of Mass Market Paperbacks

While the definition of "sales for display purposes" contained in H. R. 5161 is not explicitly limited to publications that have short retail shelf-lives, it is clear that this characteristic of most periodicals is an important part of the rationale underlying the proposed legislation. Like periodicals, mass market paperback books also typically possess very short retail shelf-lives. Thus, this characteristic distinguishes mass market paperbacks as well as periodicals from other publications and different kinds of goods sold at retail outlets.

In the case of mass market paperbacks, a short retail display period is a matter of practical necessity. A publisher who releases 25 to 35 new titles each month must have assurances that older titles will be regularly removed from limited display space as new titles reach the retailer. In practice, this is what occurs.

Mass market paperback publishers release approximately 400 new books on a monthly basis. These monthly distributions are prescheduled for months in advance. In order to provide adequate retail shelf space, many older titles must be withdrawn each month. A recent survey of publishers who are members of AAP's Mass Market Paperback Division indicates that the expected retail display period of newly released mass market paperbacks ranges from one to 12 weeks, with most of the paperbacks having an average shelf-life of four to seven weeks.[4/] Monthly paperback return figures requested as part of this survey bear out the publishers' estimates. Given the short retail display period involved, excess distributions of mass market paperbacks in the latter part of a taxable year are just as likely to produce distortions of income under present tax law as are excess distributions of periodicals.

While it is true that magazines are dated and mass market paperbacks are undated, this has no significance from the standpoint of adopting a proper tax accounting rule. All a date indicates is that there is a great likelihood that the magazine will be returned for credit; for paperbacks, this same point is demonstrated by historical statistics and the monthly publication schedules. Thus, dating has no bearing on the real issue -- that is, whether it is appropriate to change a tax accounting rule which (1) fails to take into account the unique nature of the business (e.g., the need for significant display distributions subject to an unlimited right of return), and (2) produces a serious distortion of income.

4/ The shelf-life of a periodical will vary depending upon whether new issues are releases on a weekly, monthly, quarterly, or less frequent basis.

D. Destruction of Mass Market Paperback Returns

Mass market paperback books and periodicals have still another characteristic in common which distinguishes them from the products of many other taxpayers. Like periodicals, mass market paperbacks generally have little or no economic value to the publisher once their initial retail display period has ended. Therefore, rather than incur the freight charges which would be involved in requiring returns of full books, mass market paperback publishers -- like periodicals publishers -- accept as returns either covers stripped from books or affidavits from wholesalers and retailers certifying that the books have been destroyed. The recent AAP survey of members of the Mass Market Paperback Division indicates that more than 90 percent of all returns of mass market paperback books accepted for refund or credit take the form of stripped covers or affidavits. The small proportion of full-books which come back to publishers are for the most part damaged and, therefore, not saleable.

Within the context of H. R. 5161, the foregoing practice, which is universal among mass market paperback publishers, has double significance. First, it shows that the excess distributions of mass market paperbacks are, in fact, made for display purposes. Publishers have no expectation that they will be able to resell returned books and therefore do not require full-book returns. On the other hand, mass market paperback publishers do require physical documentation that the excess distributions for which refunds are sought have been rendered nonsaleable.

Without altering their existing practices they are, therefore, in a position to meet the requirement under H. R. 5161 that the taxpayer establish that a book to be excluded from income "has not been sold and will not be sold."

E. Conclusion

Because the sale-for-display practice prevails among publishers and distributors of mass market paperbacks and the marketing arrangements in that segment of the industry are in all relevant respects similar to the methods used by periodicals publishers and distributors, the Association of American Publishers urges that the mass market paperback industry be permitted to adopt the more realistic accounting rules provided in H. R. 5161. Their exclusion would result in discriminatory treatment of taxpayers which are similarly situated.

IV. REVENUE EFFECT

Based on the recent AAP survey of members of the Mass Market Paperback Division and the 1975 amended Industry Sales Statistics (adjusted for 1976 sales), it is estimated that the extension of the provisions of H. R. 5161 to mass market paperback publishers -- assuming they all make the election -- will result in a one-time revenue loss of $16 million, spread evenly over a 10-year period.[5/]

V. SUGGESTED AMENDATORY LANGUAGE

The change in H. R. 5161 proposed by the Association of American Publishers can be accomplished by including specific

5/ The House Report indicates that the adjustment in the transition year is to be spread over a ten-year period.

references to "mass market paperback books" in paragraphs (1), (2) and (3)(B), of the bill as approved by the House of Representatives. These changes are reflected in the proposed revision of H. R. 5161 which is attached to this memorandum.

[Language to be added is underscored; language to be deleted is indicated in brackets.]

Attachment

Proposed Amendment to H. R. 5161

(e) SPECIAL RULE FOR CERTAIN PUBLICATIONS WHICH ARE RETURNED.--

(1) IN GENERAL.-- In the case of sales of magazines, [or] other periodicals or mass market paperback books for display purposes, a taxpayer who is on an accrual method of accounting may elect not to include in gross income for the taxable year the income attributable to the sale of any magazine, [or] other periodical or mass market paperback book which is returned not later than the 15th day of the third month after the close of the taxable year (or with respect to which the taxpayer otherwise establishes in the manner provided by regulations prescribed by the Secretary or his delegate that the periodical has not been sold and will not be sold).

(2) SALES FOR DISPLAY PURPOSES DEFINED.-- For purposes of this subsection, a sale is for display purposes if such sale is made in order to permit an adequate display of the magazine, [or] other periodical or, mass market paperback book and if at the time of sale the taxpayer has a legal obligation to accept returns of such magazine, [or] other periodical or mass market paperback book.

(3) DISPLAY SALES TO WHICH SUBSECTION APPLIED.--

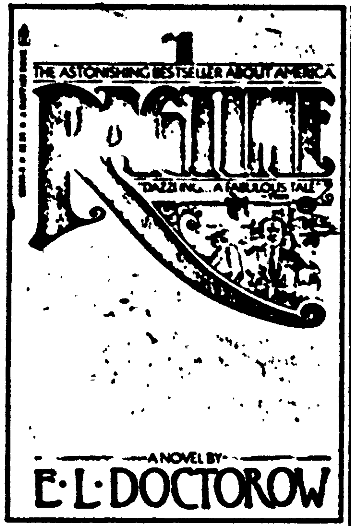
(A) ELECTION OF BENEFITS.-- This subsection shall apply to sales for display purposes if and only if the taxpayer makes an election under this subsection with respect to the trade or business in connection with which such sales are made. An election under this subsection may be made only with respect to a taxable year beginning after December 31, 1975, and may be made only with the consent of the Secretary or his delegate. The election shall be made at such time and in such manner as the Secretary or his delegate may by regulations prescribe.

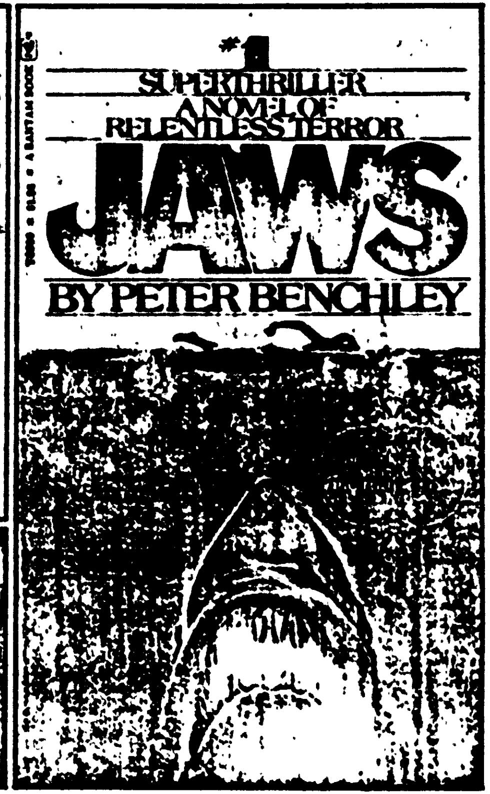
(B) SCOPE OF ELECTION.-- An election made under this subsection shall apply to all sales of magazines, [and] other periodicals and mass market paperback books made for display purposes in connection with the trade or business with respect to which the taxpayer has made the election. An election made under this subsection shall not apply to any sales made for display purposes before the first taxable year for which the election is made.

(C) PERIOD TO WHICH ELECTION APPLIES.-- An election under this subsection shall be effective for the taxable year with respect to which it is 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.

(D) TREATMENT AS METHOD OF ACCOUNTING.-- For purposes of this title, the computation of taxable income under an election made under this subsection shall be treated as a method of accounting.

"The covers beg, blur and boast. Part ad, part art, part poster, they promise, as they have for years, detectives hard as Hammer, tales weird as Bridey Murphy's, lands marvelous as Middle Earth, and women as desirable as Scarlett, Amber and O. Covers sell."





Paperbacks: The Super Sell

By Paul Richard

You can tell a mass-market paperback by its cover. One glance at the rack reveals [illegible] worlds, Carter's face and World War II, [illegible] die-cut holes and frightened virgins fleeing from The Big House on the Hill.

The covers beg, blur and boast. Part ad, part art, part poster, they promise, as they have for years, detectives hard as Hammer, tales weird as Bridey Murphy's, lands marvelous as Middle Earth, and women as desirable as Scarlett, Amber, O.

Covers sell.

In drugstores, bookshops, newsstands, bus stations and markets, around 400 million paperbacks will be bought this year, lots of them on whim.

This book has the "blockbuster look." That one sells a [illegible]. The next may hint of movies, of [illegible] or Nazis. That one with the characters [illegible] on the cover may evoke a memory of a book read long ago. Readers, undecided, wait for an impulse, a memory, a sign.

Last week, the bestselling paperback in America was something called "The Omen."

Signet's "terrifying new chamber of supernatural evil" is the child of a screenplay written by David Seltzer for 20th Century-Fox. "People love to be frightened," says Robert Haynie, editor of "The Omen," which is in its 17th printing and has sold more than 2.5 million copies since the first [illegible] in July.

The previous week's bestseller was Pyramid's "The Titans," "a thundering, savage saga of love and war in a land aflame." "The Titans," a paperback original, is volume No. 5 in "The American Bicentennial Series," a still-expanding set of historical-spectaculars produced by Lyle Kenyon Engel and written by John Jakes.

"The beauty of the thing," says James [illegible], the creative director at Pyramid, "is that if you like volume five, you're hooked; you'll probably go out and buy volumes one through four."

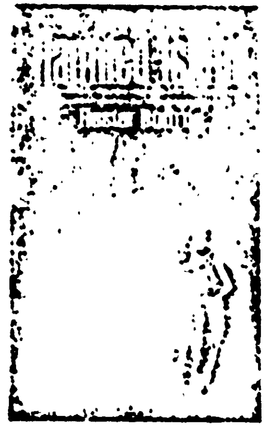
They cost $1.95 each. Three million copies of "The Titans," and seven million copies of the other novels in Jakes' series, already have been sold.

Because the average paperback today costs about $2, and is produced for millions, a hit can make a fortune. The stakes are very high. Pyramid was lucky. It paid less than [illegible] for the first novel by slightly known John Jakes.

"Ragtime" was already famous when it sold to Bantam Books for $1.85 million. But mass-market paperbacks hit the stands without "Ragtime's" fanfare. Those that do not come equipped with [illegible] reviews and movie tie-ins are dependent on the ad campaigns conducted by their covers in this ruthlessly competitive [illegible]-million market.

See PAPERBACKS, B6, Col. 1

Paperbacks' Big Sell, or You Can Tell a Market By Its Cover



JOINT STATEMENT OF

SANFORD J. GOLDBERG

FOR THE NATIONAL ASSOCIATION
OF RECORDING MERCHANDISERS

and

STANLEY M. GORTIKOV

PRESIDENT, RECORDING INDUSTRY
ASSOCIATION OF AMERICA, INC.

RE: H.R. 5161

Before the

COMMITTEE ON FINANCE

UNITED STATES SENATE

NINETY-FOURTH CONGRESS, SECOND SESSION

August 24, 1976

75-946 O - 76 - 5

SUMMARY

It is standard business practice in the sound recording industry for distributors and manufacturers to sell records and tapes with a guaranteed right of returning unsold copies. Where sound recordings sold in a given tax year are not returned before the end of that year, but are expected to be returned during the following year, Generally Accepted Accounting Principles require that an accrual method taxpayer reduce its current income by the amount of the estimated future returns. This principle is designed to insure that income is not artificially inflated.

By contrast, the IRS permits the accrual method taxpayer to exclude from income only the revenues attributable to returns actually received, regardless of the likelihood of returns during the following year. This is so even when the purchaser has bought an excess supply of sound recordings for display purposes, with a guaranteed right of return, and where there is no expectation by the parties that all of the products will ultimately be resold to consumers. The result is a distortion of income for federal tax purposes.

H.R. 5161 is designed to remedy an identical distortion of income problem for magazine distributors and publishers. It would permit the accrual method seller of periodicals to exclude from income amounts attributable to sales for display purposes, where the products are returned to the vendor within 2-1/2 months after the close of the tax year in which the sales were made. The bill is equitable, has little revenue impact, and can readily be administered by the IRS.

The merchandising of sound recordings is closely parallel to, if not identical with, that of periodicals. Both industries sell their products with a guaranteed right of return, and both experience a high percentage of returns. Abrupt declines in sales occur frequently in both businesses. Demand for the product is transient, for its life cycle is brief, and consumer demand typically cannot be restimulated by price decreases. Thus, the products, once returned, usually have little more than scrap value.

It is therefore inequitable to bar members of the sound recording industry from reducing their income for tax purposes when they are required to do so for financial accounting purposes. For smaller companies, the adverse impact on cash flow of this tax accounting rule is an onerous burden to bear. Yet the cost to the federal government of curing this inequity is relatively inconsequential -- a one-time deferral of approximately $18 million. Moreover, if the

Commissioner of the IRS were to elect to require that the impact of the change be spread over 10 years, the revenue loss would diminish to $1.8 million annually for 10 years.

Because the sound recording industry directly parallels the periodical industry in every relevant regard, it is respectfully urged that H.R. 5161 be amended as proposed in Appendix A to encompass the sound recording industry.

STATEMENT

Mr. Chairman and Members of the Committee:

We are grateful for the opportunity to submit this Statement on behalf of the National Association of Recording Merchandisers (NARM) and the Recording Industry Association of America (RIAA). NARM is a trade association which represents the merchandising segment of the sound recording industry. Among its membership are retailers, distributors (wholesalers) and "rack-jobbers" (which supply display racks and stock them with current sound recordings, primarily for department stores). RIAA is a trade association which represents the manufacturing segment of the business. Its members create and market about 85 percent of the recorded music and dramatic works sold in the United States.

H.R. 5161 would permit magazine distributors and publishers to exclude from gross income sales of periodicals returned within 2 1/2 months after the close of their taxable year. We urge that it be amended as proposed in Appendix A to encompass distributors and manufacturers of sound recordings. Such an amendment would reduce the distortion of income for federal tax purposes that exists under current law.

A. Present Law

Under existing law, taxpayers using the accrual method of accounting must include in income gross revenues from sales during the taxable year. Revenues are considered earned when all of the events fixing the right to receive those revenues have occurred, and the amounts can be determined with reasonable accuracy. The determination of when these factors warrant the inclusion of such earnings in income is required to be based on accounting methods approved by the Internal Revenue Service. In most instances, the approved methods accord with Generally Accepted Accounted Principles.

One instance, however, in which tax accounting differs from Generally Accepted Accounting Principles is where products are sold by an accrual method taxpayer with a guaranteed right of return. It is standard business practice in the sound recording industry for records and tapes to be sold with such a return privilege. When it is known that a statistically ascertainable percentage of sold products will be returned in future years, Generally Accepted Accounting Principles require maintenance of a reserve account for returns so that income for the year in which the sales occur will not be artificially inflated. By contrast, the IRS does not permit deductions based on estimates of such future returns for tax accounting purposes, even though such estimates accord with business reality. Quite recently, this rule was held applicable to a member of the sound recording industry. See Ertegun v. Commissioner, 531 F.2d 1156 (2d Cir. 1976).

Thus, even though it is understood that the purchaser is buying an excess supply of sound recordings, and that a reasonably predictable percentage of them will be returned in the following year, tax accounting does not now permit an offset in the year in which the sound recordings were sold. The result is a distortion of income for federal tax purposes.

B. Explanation of H.R. 5161

H.R. 5161 is designed to remedy an identical distortion of income problem for magazine distributors and publishers. Its purpose and effect is to more properly reflect the income of members of the periodical industry by reducing the impact of this inequitable and unjustified aberration from Generally Accepted Accounting Principles.

The bill provides that, in the case of sales of periodicals for "display purposes," an accrual method taxpayer may elect not to include in gross income the revenue attributable to the sale of any periodical which is returned within two-and-a-half months after the close of the taxpayer's taxable year. A sale is for "display purposes" if it is made in order to permit an adequate display of the periodical and, if at the time of sale, the taxpayer has a legal obligation to accept returns of the products.

This legislation can readily be administered by the IRS. The taxpayer's election is subject to IRS consent. Furthermore, once an election is made, it is effective prospectively until the IRS consents to its revocation.

C. The Provisions Of H.R. 5161 Should Be Extended To The Sound Recording Industry

Like periodical vendors, distributors and manufacturers of records and tapes sell far more copies of a sound recording than it is anticipated will ultimately be resold to customers. The volatile nature of the recording industry, in which the artist and his recorded repertoire rise and fall with astonishing rapidity, underlies the need for such intentional overstocking, as part of the industry's mass merchandising and advertising techniques. When a recording is released, no one knows whether it will become an overnight sensation or a dismal failure. But retailers must be provided with an adequate supply for display purposes in anticipation of the hoped-for demand.

In light of this merchandising technique, it has become standard, industry-wide practice for sound recordings to be sold for resale with full return privileges. And, in fact, the percentage of records returned is high. A 1974 survey of the industry by the Cambridge Research Institute disclosed that returns on all records averaged 21 percent of gross sales.

It is apparent that the merchandising of sound recordings is closely parallel to, if not identical with, that of periodicals. Both industries sell their products with a guaranteed right of return, and both experience a high percentage of returns. Abrupt declines in sales occur frequently in both businesses, such as when radio stations stop playing a song or when the next issue of a magazine is released. Demand for the product is transient, for the life cycle of a sound recording, like a magazine, is brief, and consumer demand typically cannot be restimulated by price decreases. Thus the product, once returned, usually has little more than scrap value; the vast majority of sound recordings returned to the manufacturer are destroyed. (The few thought to have any market appeal are redistributed by the manufacturer, usually with physically altered covers, at a fraction of their prior cost.)

In spite of the long-standing and well-documented fact of returns in the business, members of the sound recording industry are barred from reducing their income for tax purposes, even though they are required to do so for financial accounting purposes. The result is an unfair distortion of income for federal tax purposes. In some cases, this distortion of income may have a substantial and adverse impact on cash flow, particularly on the smaller manufacturers, distributors and rack jobbers. Thus, the sound recording industry is in essentially the same situation as the publishers and distributors of periodicals, and should similarly be afforded the relief provided for in H.R. 5161.

The cost to the federal government of correcting this inequity is relatively inconsequential -- a one-time deferral of approximately $18 million. Moreover, since the procedure described in H.R. 5161 constitutes a change in accounting method, it is reasonable to assume, as suggested in the House

Committee Report, that the IRS will require the resulting adjustments to be spread over a 10-year period. Thus, the revenue loss may diminish to $1.8 million annually, for 10 years.

D. Conclusion

In conclusion, it is respectfully urged that the benefits of H.R. 5161 be extended to the sound recording industry, because its marketing practices directly parallel those in the periodical business and because it suffers similar distortions of tax income. Such legislation will help to eliminate the inequity and cash flow problems of income distortion, and yet will have a relatively small revenue impact.

Appendix A

The following amendment to H.R. 5161 is suggested to extend to sound recordings the proposed rule for the inclusion in income of magazine sales for display purposes.

Amend H.R. 5161 as follows:

On page 1, line 7, after "Magazines," insert
-- or sound recordings --

On page 1, line 9, after "of," insert
-- sound recordings or --

On page 2, line 3, after "any," insert
-- sound recordings or --

On page 2, line 9, before "periodical" insert
-- sound recording or --

On page 2, line 13, after "the" (first occurrence) insert
-- sound recording or --

On page 2, line 15, after "such," insert
-- sound recording or --

On page 3, line 6, after "of" insert
-- sound recordings or --

TO

COMMITTEE ON FINANCE

UNITED STATES SENATE

STATEMENT ON BEHALF OF WINE INSTITUTE

IN SUPPORT OF H.R. 8283

AUGUST 24, 1976

JOHN DE LUCA
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Tel: (415) 986-0878

ARTHUR H. SILVERMAN
Washington Counsel, Wine Institute
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STATEMENT IN SUPPORT OF H.R. 8283

My name is Arthur H. Silverman. I am Washington Counsel for Wine Institute, the trade association of the California wine and brandy industry. However, I speak for the entire domestic wine industry in urging the passage of H.R. 8283.

An important segment of the wine industry is composed of special natural wines, such as vermouth, sangria, and other flavored wines, which are produced on bonded wine cellar premises. The Internal Revenue Code provides that natural flavors must be used in the production of special natural wines. For many years, the Bureau of Alcohol, Tobacco and Firearms and its predecessors have recognized that said statute permitted the use of trace quantities of other flavors in order to replace the effect of flavor lost in the processing of fruits. Although the quantity of such flavoring has consisted of less than 1/10 of one percent of the flavoring material, its use is essential in most such wines in order that the finished flavor have the characteristic taste of the fresh fruit from which the flavor is made, i.e., that a strawberry flavor tastes like a fresh strawberry.

Trace amounts of other flavorings in alcoholic beverages have been used in Europe and other foreign countries over a long period of time, and in most cases, in greater quantities than the trace amounts American producers use. It is the worldwide consensus of opinion of winemakers, enologists, and flavor manufacturers that a satisfactory flavor, for use in most flavored wines, is difficult, if not impossible, to produce without the addition of these trace amounts of other flavorings.

The provision of the Internal Revenue Code which we are seeking to amend, 26 USC 5386(a), does not apply to wines produced in other countries. It applies only to wines produced in the United States.

26 USC 5386(a) deals only with the production of special natural wine on bonded wine cellar premises. It does not concern itself in any way with the labeling of wine.

However, a recent change in the regulations for the food industry by the Food and Drug Administration, 21 CFR 1.12, effective June 30, 1975, established a highly restrictive definition of the term "natural flavor". Since the manufacture and distribution of flavoring materials falls within the jurisdiction of these FDA regulations, flavor manufacturers are required to state on the containers of flavors shipped to their customers that any flavor, even though it contained less than 1/10 of one percent of other flavorings, would have to be labeled as a "natural and artificial" flavor.

The significance of the Food and Drug requirement dealing with labeling is that the American wine producer, unlike the producer of similar foreign products, cannot continue to produce on bonded wine cellar premises vermouth, sangria, and other flavored wines of the quality to which its customers have become accustomed. Flavored wine producers would be forced to establish a distilled spirits plant at great cost and pay an additional rectification tax of thirty cents per proof gallon, in addition to the applicable wine tax, with the resultant higher cost to the consumer. However, foreign producers would not be confronted with these problems and would continue to pay only the applicable wine tax even though their product may contain greater quantities of other flavorings.

BATF, because of its long history of recognizing the high quality of these products, is cognizant of the plight of the American wine industry and has agreed to language that would amend 26 USC 5386(a) to continue to permit trace amounts of other flavorings in the production of special natural wines on bonded wine cellar premises.

The Department of the Treasury has interposed no objection to the enactment of this legislation, which is intended to permit the continuation of the production of special natural wines on bonded wine cellar premises. Said legislation is not intended to be determinative as to how these products will be labeled.

In fact, we know of no objection to the enactment of this legislation.

August 24, 1976

STATEMENT OF DONALD STEVENS
VICE PRESIDENT, JEWEL COMPANY
OF AMERICA, 25 HOLDEN ST., PROVIDENCE,
RHODE ISLAND 02908, IN SUPPORT OF
H.R. 8656
AT HEARINGS BEFORE THE
SENATE FINANCE COMMITTEE

* * *

Outline of Mr. Steven's Remarks on Behalf of the Jewel Company of America in Favor of Enactment of H.R. 8656

I. H.R. 8656 should be enacted because:

(a) it will remove an anomaly in the U. S. Tariff Schedules which discourages the use of American labor in the linking of crystal used for chandeliers;

(b) the duty-free entry of loose glass prisms would create an incentive to establish a competitive U. S. chandelier industry and would create new jobs for U. S. workers.

II. Brief outline of U. S. chandelier industry.

A. Glass prisms for chandeliers have never been a U. S. made product.

B. Relevant import statistics for the years 1973-75 of items in TSUSA Nos. 545.5700 and 653.3720.

75-946 O - 76 - 6

III. Reasons for absence of a U. S. chandelier industry.

A. Modes of production and lower wage levels in European countries.

B. The anomalous U. S. tariff structure with built-in disincentives.

C. Present loophole in the Tariff Schedules.

D. Canadian decision to give loose glass prisms a duty-free preference.

IV. H.R. 8656 will create new jobs for U. S. workers and a U. S. chandelier industry.

A. Duty-free entry will not adversely affect any domestic industry or its workers.

B. Immediate creation of jobs for linking operations in U. S.

C. Creation and expansion of U. S. production of chandelier frames and new jobs associated therewith.

D. Available domestic labor-intensive technology could be immediately employed in linking operations.

E. U. S. manufacturers would become increasingly competitive against imports.

F. Increased sales of domestic chandeliers could result in reduced costs of U. S. chandeliers to American consumers.

V. The Departments of Treasury, State, Commerce and Labor, together with the AFL-CIO, have all expressed support for H.R. 8656.

STATEMENT OF DONALD STEVENS, VICE PRESIDENT OF THE JEWEL COMPANY OF AMERICA, INC.

My name is Donald Stevens. I am Vice President of the Jewel Company of America, Inc., which is located in Providence, Rhode Island. Our company is a major importer and user of loose glass prisms.

I appreciate this opportunity to testify in support of the enactment of H.R. 8656, the bill to amend the Tariff Schedules of the United States to provide for the duty-free entry of loose glass prisms used in chandeliers. I support this bill because it will remove an existing anomaly in the Tariff Schedules which presently discourages the employment of American labor in the production of chandeliers. The bill would provide the necessary economic incentive to establish a U. S. based chandelier industry and thereby create new employment opportunities for U. S. workers at a time when wide-spread unemployment is of vital concern to us all. Before addressing our specific reasons for supporting this legislation, I will outline briefly the state of the U. S. chandelier industry.

I. THE U. S. CHANDELIER INDUSTRY

Crystal chandeliers, over the years, have been very popular in the United States, not only for residential but for commercial use. Glass prisms for chandeliers have <u>never</u> been an American made product. They have been imported primarily from Austria, Germany, Italy, Japan and Czechoslovakia, the traditional centers for the production of crystal. American manufacturers import linked-up (assembled) rather than loose crystal for use in chandeliers. The great majority of chandelier frames, however, are imported since most frames used with crystal are of cast bronze or brass, also a specialty of European craftsmanship and technology. Available statistics attest to the outflow of U.S. dollars for the import of these items.

For example, combined U.S. imports of loose and linked-up glass prisms and finished chandeliers in chief value of crystal glass amounted to approximately 12 million dollars in 1973, 11 million dollars in 1974 and 7 million dollars in 1975 */ (TSUSA No. 545.5700). Loose glass prisms account for a very small proportion of these imports, the balance representing linked-up ornaments and finished chandeliers. In addition, imports of chandeliers and lighting

*/ The low 1975 figure reflects the general decline in U.S. imports in 1975.

fixtures designed for permanent indoor installation in chief value of brass, many of which employ glass prisms, amounted to approximately 12 million dollars in 1974 and 7 million dollars in 1975 (TSUSA No. 653.3720).

II. REASONS FOR THE ABSENCE OF A U. S. CRYSTAL CHANDELIER INDUSTRY

The fundamental reasons for the lack of the development of a U. S. based chandelier industry, apart from the obvious fact that crystal ornaments are not produced here, are (1) traditionally lower wage levels in European countries and, in particular, (2) the current U. S. duty structure which has a built-in disincentive for U. S. concerns to undertake domestic linking of glass prisms for chandeliers.

A. The European Situation

Since Western and Eastern Europe have been the major production centers of crystal prisms, a whole industry was opened to jobbers or manipulators of crystal who, very economically, through the use primarily of many home workers, housewives, children, etc., were able to furnish linked crystal chains of varying lengths to U. S. importers and manufacturers, thereby reaping substantial profits and work for their communities. Because of higher labor costs and the fact that such homework is effectively precluded by widespread collective bargaining agreements in the United States, American chandelier manufacturers never became involved in the pinning or linking of glass prisms. Since the wages of U.S. workers continue to be higher than those paid by the European jobbers, who farm out their work to homeworkers, American chandelier manufacturers still remain in a non-competitive position vis-a-vis European final-pinned crystal.

B. The Anomalous U.S. Tariff Structure

There is little doubt that the current U.S. duty structure applicable to loose glass prisms is the chief obstacle to the establishment of a domestic chandelier industry. At the present time, the duty rate on loose prisms is exactly the same as that for linked-up (assembled) ornaments. Under TSUS No. 545.57, both items are subject to a 12% ad valorem duty. Since a great deal of the work of linking glass prisms, as previously noted, is done in European countries with low-labor cost, homework operations, there clearly is no price advantage to U.S. concerns to utilize an American linked article.

The net result of this anomaly has been a complete lack of enthusiasm by the lighting industry to develop a competitive American industry. Moreover, the same 12% duty rate is also applicable to a completely finished chandelier, fully assembled and trimmed with glass ornaments, where the chief value of the finished chandelier consists of glass.

However, for chandelier parts or even finished chandeliers, fully assembled and trimmed with glass ornaments, where the main value consists of metal, for instance, a brass frame, the duty rate under TSUS No. 653.37 is only 9.5% ad valorem.

It is not surprising, therefore, that most of the major chandelier distributors in America are not interested in developing chandeliers of their own design for manufacture in this country since they can take advantage of this "loophole" in the Tariff Schedules which permits the importation of a completely finished chandelier at an extremely favorable duty rate. The dollar value of imports of finished chandeliers, in chief value of brass, as noted on page 3, bespeaks of the attractiveness of this loophole to American importers.

I would like to point out that a similar anomaly was also present in Canada's tariff structure. After a complete review of its duty rates, the Canadian Government in 1973 decided to permit loose glass prisms a duty-free preference until October 31, 1974 in order to encourage the manufacture of finished chandeliers in Canada. This preference was renewed for an additional year, and on October 31, 1975, was extended once again.*/

It is clear that unless and until the present 12% U. S. duty rate is completely eliminated on loose glass prisms, there will be no incentive for U. S. companies to start up linking operations and begin the manufacture of chandeliers utilizing these items.

III. H.R. 8656 WILL CREATE NEW JOBS FOR AMERICAN WORKERS AND A U. S. CHANDELIER INDUSTRY

The elimination of the existing duty rate on loose glass prisms, by vitiating the present anomaly in the U. S. Tariff Schedules, will result in the immediate creation of new jobs for American workers and will foster the beginnings of a competitive domestic crystal chandelier industry.

I want to emphasize in this regard that duty free entry of these articles will not, in any way, adversely affect any domestic industry or its workers for the simple reason that glass prisms used in chandeliers, as previously noted, have never been manufactured in America. Thus, the elimination of duty on these prisms can only inure to the

*/ See appended pages of Canada's Customs Tariff "A", item 32675-1.

benefit of American workers and manufacturers.

A. New Opportunities for Workers

The elimination of import duty would result in a considerably expanded production of linked crystal by American labor and thus would immediately improve our competitive position. Many American importers and manufacturers would readily shift from buying completed articles from European jobbers and begin doing their own assembly and pinning operations.

By setting up linking operations, a substantial portion of which is presently done in Europe, in the United States, we estimate that initially 1,000 new jobs would be created for U. S. workers. For example, the State of Rhode Island and, particularly, the Providence area, the traditional center of the American jewelry industry, has a substantial number of presently unemployed, experienced and skilled workers who could be immediately employed in linking operations for the production of assembled ornaments for use in domestic chandeliers. The creation of new, productive jobs in this and other geographic areas of the country attendant with the passage of this bill is an important consideration in this period of widespread unemployment.

B. New Opportunities for Industry

The duty free entry of glass ornaments also will stimulate the creation and expansion of domestic production facilities for chandelier frames made of cast bronze, brass, and other metals. This country has the basic technical know-how, designs, and assembly methods to produce entire lighting fixture lines to compete with finished chandeliers presently imported at a very favorable duty rate.

We estimate, that in addition to the 1,000 jobs associated with linking activities, another 2,000 American workers could find employment in new or expanded domestic production of frames and finished chandeliers.

Moreover, at a time when wide-spread concern has been voiced about the export of U.S. technology and jobs to lower labor cost countries, passage of this bill will enable U.S. firms employing U.S. workers to utilize domestic technology to produce chandeliers which will compete with imported ones which have enjoyed a virtual monopoly in the U.S. market by default. Further, since the best available technology for linking operations is labor intensive, growing demand for assembled ornaments will increase the need for and not displace American workers in this activity.

I would like to point out again that the Canadian Government has waived all import duty on loose glass prisms for the very reasons I have noted -- to give Canadian importers and manufacturers the right and opportunity to compete with foreign imports.

C. Reduced Costs to the U. S. Consumer

While we do not envision that the cost of chandeliers will be greatly reduced with the passage of the bill, it is anticipated that the resulting savings will enable American manufacturers to be increasingly competitive against imports. An increased volume of sales, however, should permit a lowering of profit margins which could result eventually in reduced costs of domestic made chandeliers to the American consumer. These savings to the consumer would be matched by a significant increase in the use of American as opposed to European labor as demand for domestic articles increases.

IV. THE GOVERNMENT AGENCIES AND THE AFL-CIO SUPPORT H.R. 8656

The Departments of Treasury, State, Commerce, and Labor have all expressed support for H.R. 8656. Thus, in its comments on the bill to the House Ways and Means Committee, the Department of Commerce noted:

> ". . . [E]limination of the duty on loose glass prisms would be advantageous in helping to control production costs and would place the domestic industry in a better position to compete with foreign manufacturers in supplying crystal chandeliers to U. S. consumers."

Similarly, the Department of State observed that the bill "would end the tariff cost burden, and, in so doing, help to maintain and improve domestic production and employment opportunities." The comments of the Departments of Labor and Treasury were to the same effect.

The AFL-CIO commented to the Ways and Means Committee that the bill "is supported by the glass unions because no U. S. production of the item is available, and therefore imports create jobs at this time."

We are aware of no opposition that has been expressed to this bill.

* * *

I firmly believe that the present anomaly in the U. S. Tariff Schedules must be eliminated if this country is to establish a domestic chandelier industry and create new opportunities for U. S. workers and manufacturers. Accordingly, for the reasons stated herein, I urge enactment of H.R. 8656 in order to accomplish these objectives.

Tariff Items	Goods Subject to Duty and Free Goods	British Preferential Tariff	Most-Favoured-Nation Tariff	General Tariff	Effective Date No. of Memo
32669-1	Reflectors and refractors of glass designed for use with lighting fixtures, not further manufactured than moulded, when of a class or kind not made in Canada and imported to be silvered, aluminized, acid-etched or combined with a spun aluminum cover in Canada .... *(Expires February 28, 1975)*	Free	Free	10 p.c.	O.C. 13/7/71, D47-515,515-10
32671-1	Rectangles of glass, in single sheets, coated with a transparent electrically conductive material, whether or not equipped with bus bars, for use in the manufacture of doors for refrigerators and freezers .... *(Expires June 30, 1975)*	5 p.c.	7½p.c.	30 p.c.	O.C. 13/6/72, D47-515-6,515-14
32675-1	Glass pendants, unstrung, for use in the manufacture of trimmings for lighting fixtures .... *(Expires October 31, 1974)*	Free	Free	30 p.c.	O.C. 4/10/73, D47-515-18
32700-1 *	Spectacles; eyeglasses, and ground or finished spectacle or eyeglass lenses, n.o.p.	17½p.c.	17½p.c.	30 p.c.	4/6/69, D47-492
*	*From February 20, 1973 to February 19, 1974*	12½p.c.	12½p.c.	30 p.c.	20/2/73, D47-519
12701-1	Shapes of glass or plastic for use in the manufacture of spectacle and eyeglass lenses .... *(Expires October 31, 1974)*	10 p.c.	12½p.c.	22½p.c.	O.C. 4/10/73, D47-515-18
2705-1	Contact lenses and anterior chamber implants for the human eye....	Free	Free	Free	18/6/58, D47-410
800-1	Spectacle and eyeglass frames and parts thereof, n.o.p.	15 p.c.	17½p.c.	20 p.c.	19/5/48, D47-253
	GATT		15 p.c.		30/6/56, D48-28-32
*	*From February 20, 1973 to February 19, 1974*	12½p.c.	12½p.c.	20 p.c.	20/2/73, D47-519
105-1	Parts, unfinished, for the manufacture of spectacle and eyeglass frames	Free	5 p.c.	5 p.c.	26/2/37, D47-2
10-1	Parts, unfinished, for use in the manufacture of spectacle and eyeglass frames .... *(Expires October 31, 1974)*	Free	Free	5 p.c.	O.C. 4/10/73, D47-515-18

End of Group 7.

Tariff Items	Goods Subject to Duty and Free Goods	British Preferential Tariff	Most-Favoured-Nation Tariff	General Tariff	General Preferential Tariff	Effective Date No. of Memo
32669-1	Reflectors and refractors of glass designed for use with lighting fixtures, not further manufactured than moulded, when of a class or kind not made in Canada and imported to be silvered, aluminized, acid-etched or combined with a spun aluminum cover in Canada .... *(Expires February 28, 1977)*	Free	Free	10 p.c.		O.C. 13/7/71, D47-515,515-29
	C.P.T. rate from 1/7/74 to 30/6/84				Free	1/7/74, D47-518-1
• 32671-1	Expired, 30/6/75, D47-515-14.					
32675-1	Glass pendants, unstrung, for use in the manufacture of trimmings for lighting fixtures .... *(Expires October 31, 1976)*	Free	Free	30 p.c.		O.C. 4/10/73, D47-515-18,26
	C.P.T. rate from 1/7/74 to 30/6/84				Free	1/7/74, D47-518-1
• 32680-1	Hollow spheres of glass, 20 to 80 microns in diameter, for use in the manufacture of explosives .... *(Expires June 30, 1977)*	Free	Free	22½ p.c.		O.C. 27/6/74, D47-515-24,515-32
	C.P.T. rate from 1/7/74 to 30/6/84				Free	1/7/74, D47-518-1
32700-1 ■	Spectacles; eyeglasses, and ground or finished spectacle or eyeglass lenses, n.o.p.	17½p.c.	17½p.c.	30 p.c.		4/6/69, D47-492
	From November 19, 1974 to June 30, 1976	*12½p.c.*	*12½p.c.*	*30 p.c.*	-	*19/11/74, D47-525*
	C.P.T. rate from 1/7/74 to 30/6/84				11½p.c.	1/7/74, D47-518-1

• Revised June 24, 1975

STATEMENT OF ALEN S. YORK

on Behalf of

NEW YORK FOAM SALES CO.

before

U.S. SENATE COMMITTEE ON FINANCE

August 24, 1976

Mr. Chairman, members of the Committee, my name is Alen S. York. I am the President of New York Foam Sales Co.

I appreciate the opportunity given me to present the views of my firm with regard to House passed HR 11605, a Bill to suspend for a three year period the rate of duty on mattress blanks of rubber latex.

HR 11605 would temporarily suspend, for a period of three years, the 15% import tariff on latex foam buns used in the manufacture of latex foam bed pillows and mattresses manufactured and sold in the United States. We feel that this would be beneficial to the consumer from a cost and availability standpoint while causing absolutely no disruption to American industry.

To review the reason for this legislation, let me go back to March of 1975. At that time, there existed only one firm in the United States producing latex foam buns -- Sponge Rubber Products Co. of Shelton, Conn. This firm had purchased the sole latex foam manufacturing facility from the B. F. Goodrich Co. Then it happened! On a Saturday night in March of 1975, someone blew up the plant. Result: an end to all production of latex foam in the United States.

During the last year much talk has occurred concerning the rebuilding of this manufacturing facility. Thousands of Connecticut residents were put out of work in an already depressed labor market. In the meantime, because of contractural agreements and consumer demand, the manufacturers of finished latex foam products had to look elsewhere for a continued source of supply. The only practical source was in Canada.

This posed a significant problem: import tariffs of 15% ad valorem. This tariff caused much disruption resulting in contracts being cancelled and a declining consumer demand due to lack of availability. The tariff, by design, was enacted to protect a domestic industry. Unfortunately, that domestic industry no longer exists and, therefore, the tariff should be eliminated.

The domestic manufacturers of finished latex foam products would be delighted to see another domestic source created -- be it a rebuilding of the Shelton, Connecticut facility or elsewhere. Due to this fact we have asked that the import tariff of 15% be suspended for a period of three years rather than be eliminated entirely. We want a domestic source, but we haven't seen any positive effort being made in this direction. In the meantime, we must survive as a viable product classification.

As I mentioned, HR 11605 was introduced in the House of Representatives to eliminate the 15% ad valorem tariff for a period of three years. Following favorable responses from all Executive Agencies contacted by the House Ways and Means Committee, hearings before its Trade Subcommittee, and favorable reporting of the Bill by the full House Ways and Means Committee, the House of Representatives passed HR 11605 on May 17, 1976.

With this background presented, I now ask that this august Committee consider and report favorably HR 11605 to the full Senate of the United States. Only by your affirmative action can this product classification be preserved for the American consumer. The effect of the present situation has had a devastating effect on our firm and its labor force as well as many other firms producing finished latex foam filled products and their employees throughout the United States. Your speedy consideration will be appreciated by all.

Thank you for allowing me to present my views here today.

75-946 O - 76 - 7

SUMMARY

The total U.S. production of latex foam mattress and pillows buns was eliminated by a bombing in March, 1975. Manufacturers of finished products using latex foam mattress and pillow buns now must seek the aforementioned buns from sources outside the United States. The current import tariff on the affected imports, found in classisification No. 727.86 of the TSUSA is 15% ad valorem for Column I countries.

As there is presently no production of latex foam mattress and pillow buns in the United States, the 15% ad valorem tariff serves no purpose and is merely an additional cost to be borne by the manufacturers and consumer.

Because of the possibility that the U.S. production capability will be rebuilt in the future, we ask only a three-year suspension. Should the U.S. production capacility be rebuilt before the end of the three year suspension period, U.S. manufacturers would immediately turn to that source of supply because of the excessive motor freight charges involved in the importation of the product from Canada.

It is important to make available to the consumer this product classification at reasonable prices to preclude its elimination. My firm, New York Foam Sales, is aware of no opposition to HR 11605.

August 24, 1976

Statement by Mac Asbill, Jr.
On Behalf of
World Airways, Inc.
Before the Senate Finance Committee
On
H. R. 11997, the Bank Holding Company
Tax Act of 1976

Summary

Congress should promptly enact legislation along the lines of H. R. 11997, passed by the House of Representatives on March 15, 1976, which would grant appropriate tax relief to divestitures certified by the Federal Reserve Board as "necessary or appropriate" to effectuate the purposes of the Bank Holding Company Act Amendments of 1970.

Statement

This statement is submitted by Mac Asbill, Jr., a lawyer practicing in Washington with the Washington and Atlanta firm of Sutherland, Asbill & Brennan, on behalf of World Airways, Inc., a Delaware corporation headquartered in Oakland, California. It advocates the prompt enactment of H. R. 11997, or its equivalent in purpose and effect. That bill would grant appropriate tax relief to divestitures certified by the Federal Reserve Board as "necessary or appropriate" to effectuate the purposes of the Bank Holding Company Act Amendments of 1970.

Following the Committee's request in its press release of August 10 that witnesses with common interests consolidate their testimony, I am authorized to state that Lykes Corporation of New Orleans, Sperry and Hutchinson Co., GATX Corporation, and Powell Lumber Co., each of which has submitted, or will submit, a statement for the record, join World Airways in this general recommendation.

The adoption by the Congress of the Bank Holding Company Act Amendments of 1970 subjected so-called one-bank holding companies to the Bank Holding Company Act for the first time. Generally speaking, these Amendments required such holding companies to divest themselves of either their banking or their non-banking assets before December 31, 1980. It was contemplated in 1970 that appropriate tax relief would be provided with respect to such divestitures, as had been done in the case of earlier bank holding company legislation. Thus, the report of the Senate Committee on Banking and Currency, S. Rep. No. 91-1084, provided:

> "It is anticipated that the Congress will follow precedent and will pass a bill providing companies required to make divestitures under this legislation with relief from an undue tax burden as a result of such divestiture. It would be

> inequitable to require these divesting companies to commit themselves to a divestiture plan without knowing precisely what their tax situation will be in regard to such divestiture. Accordingly, it was deemed necessary to provide a divestiture period of sufficient length that these companies will have adequate time to make their divestiture plans after the appropriate tax relief measure is passed by Congress."

Pursuant to this commitment, the Treasury began the formulation of such relief legislation and first submitted a proposal, S. 3111, to the Congress in 1972. In 1973 an identical draft bill was introduced as S. 407. That bill provided for the tax-free spinoff (i.e., distribution to stockholders) of stock divested pursuant to the 1970 Amendments and also provided for the deferral of gain realized upon the sale of divested property if the proceeds were reinvested in certain other property (the so-called "rollover" provision).

World Airways, which is an international and domestic supplemental air carrier, had in May 1968, through its wholly-owned subsidiary, Worldamerica Investors Corp., purchased over 99% of the stock of First Western Bank & Trust Company, a California corporation. By virtue of this purchase, World Airways was a one-bank holding company of the type subjected to the divestiture requirements of the Bank Holding Company Act Amendments of 1970. Although it might have been permitted, under the "grandfather" provision in the 1970 Amendments, to retain its bank if it were willing to forego forever expansion of its non-banking activities, World was forced, as a practical matter, to choose between retention of its bank or its non-banking businesses. Being primarily in the air carrier business, it decided to divest itself of the bank, in that way carrying out the Congressional mandate to separate its banking from its non-banking businesses.

It was concluded for several reasons that a spin-off of the bank's stock to the shareholders of World Airways was not feasible. Worldamerica had borrowed a substantial part of the purchase price of the bank stock, and had pledged all of that stock to secure the loan. It needed the earnings produced by the bank, or the proceeds of sale, in order to pay off that loan. The pledgee, Bank of America, would not permit a spinoff of the bank stock so long as the loan was outstanding. Moreover, another loan agreement covering loans to acquire aircraft prohibited distribution of any substantial part of World's assets, including the stock of Worldamerica or the bank stock owned by that subsidiary. Thus, the only way that divestiture could be accomplished was by a sale.

It soon became obvious that because of antitrust considerations, and provisions of the Bank Holding Company Act which prevented bank acquisitions across state lines, it would be difficult to find a suitable purchaser. Indeed, the Department of Justice in 1972 challenged on antitrust grounds the sale of the bank to Wells Fargo Bank which appeared to be the only qualified California buyer with the means to acquire the bank. World concluded that as a practical matter it would probably be necessary to sell the bank to a foreign purchaser. Following termination of the Wells Fargo transaction, World began negotiations with Lloyds Bank Limited of London which resulted in the sale of the bank in January, 1974, to Lloyds First Western Corporation (a wholly-owned subsidiary of Lloyds Bank Limited). This sale was approved by the Federal Reserve Board. Of the approximately $7,650,000 tax attributable to the sale, about $6,800,000 had been paid by September 15, 1975; the remaining $850,000 was deferred in anticipation of being eliminated by a loss carryback from 1975.

At the time of the decision to dispose of its bank, World Airways was, of course, aware that in 1970 Congress had committed itself ultimately to providing appropriate tax relief from the hardships caused by divestitures prompted by the Bank Holding Company Act Amendments of 1970. However, because of the limited number of financially competent and qualified buyers to whom the bank could be sold without violating the antitrust laws and other applicable government restrictions, World Airways was unable, as a matter of practical economics, to await final passage of such relief legislation. Rather, faced with a narrow class of potential buyers who could be expected to avoid challenge on antitrust or other grounds, World Airways was compelled as a matter of business prudence, once a suitable buyer could be found, to make the sale in reliance upon the promise of subsequent tax relief.

After full hearings and almost three years of deliberation, the Ways & Means Committee on March 4 reported out, and the House of Representatives on March 15 passed, H. R. 11997, a bill designed to grant relief from the tax consequences of divestitures required by the Bank Holding Company Act Amendments of 1970. That relief takes two forms.

The first is a provision permitting a holding company to "spin off" (i.e., to distribute to its stockholders) tax-free either its non-banking assets (including stock) if the corporation elects to continue to be a bank holding company, or its banking assets (including stock) in the event the corporation elects to cease to be a bank holding company.

In recognition of the fact that such a spinoff would often be inappropriate, and in some instances impossible, for reasons such as those applicable in World's situation, the bill provides an alternative type of relief, the "installment payment method" pursuant to which a bank holding company which sells banking or non-banking property pursuant to the Bank Holding Company Act Amendments of 1970, may pay in equal annual installments the tax attributable to that sale. The installment period ends in 1985, or, if later, ten years after the due date of the return for the year of sale. In order to encourage early dispositions in compliance with the 1970 Amendments, the bill provides that interest will not be imposed upon the annual installments due in 1985 or earlier years, but that it will be imposed on any installments due thereafter. In those situations where -- as in World's own case -- the sale has been made and the tax paid before the effective date of H. R. 11997, the bill provides for a refund of that portion of such tax representing installment payments which would not become due until after that effective date.

The Ways & Means Committee and the House of Representatives rejected the "rollover" type of relief (i.e., treating the sale as an involuntary conversion, the gain on which would not be recognized provided the proceeds were reinvested in specified types of property and provided that the basis of such replacement property was appropriately reduced), because of the complexities inherent in that type of relief, especially where the sale's proceeds were invested in stock of a corporation rather than directly in replacement assets.

Because of a procedural provision in the Congressional Budget and Impoundment Control Act of 1974 (i.e., that, except in the event of a waiver in the Senate, neither House shall consider a bill which produces a decrease in revenues effective during the next fiscal year until the first concurrent resolution on the budget for such year has been agreed to), H. R. 11997 provides that its effective date will be October 1, 1977, the beginning of fiscal year 1978, and that no refunds will be paid pursuant to the bill prior to that date.

We believe that H. R. 11997 reasonably fulfills Congress' commitment to provide appropriate tax relief for divestitures pursuant to the 1970 Amendments. World Airways would recommend only one change, namely that the effective date provision be modified so that the Act will become effective upon enactment. Otherwise, World will be denied a portion of th relief contemplated under the installment payment method. We know of no substantive reason why the effective date should be postponed beyond the date of enactment.

More than half of the 10-year period for divestiture prescribed by the 1970 Amendments has already elapsed. Consequently, it seems reasonable to expect that both those one-bank holding companies which have already accomplished that divestiture and those which have not yet done so, be apprised soon of the ground rules which will govern the tax consequences of such divestitures. Consequently, we urge this Committee and the Senate to take prompt action along the lines of H. R. 11997.

STATEMENT ON BEHALF OF AMERICAN ASSOCIATION OF BICYCLE IMPORTERS, INC. PRESENTED BEFORE THE SENATE COMMITTEE ON FINANCE

MR. CHAIRMAN AND MEMBERS OF THE COMMITTEE:

My name is Philip Kamler. I am President of the American Association of Bicycle Importers, Inc., a non-profit organization of independent American bicycle importing businesses. Our respective businesses are American owned and managed.

The issues in contention of HR 12254, a bill to suspend payment of duties on certain bicycle parts and accessories, were never clearly defined or fully expressed to the U.S. Senate Committee on Finance in previous enactments in 1970 and 1973.

First, the parties to this issue should be defined. Proponents would have you believe that this is an issue between foreign producers and domestic bicycle manufacturers. Nothing could be further from the truth. The parties to this matter are:

1. American businesses whose principal activity is the importation of complete bicycles.
2. The eight American bicycle factories.

The American Association of Bicycle Importers, Inc. first came into being in March, 1975, and thus the reasons for opposition to enactment, which were as persuasive in 1970 and 1973 as they are today, could not have expression for the benefit of the Committee on Finance. The issues in contention do not belong nor should they occupy the time of this Committee since the issues involved are particular to the bicycle industry and have never been revealed to the Committee.

The bicycle industry is like no other industry. Bicycles are assembled in the United States by eight industry factories. However, the bicycles produced are not made up of American produced component parts. The principal component parts of an American bicycle are imported from foreign producers. It is reliably reported that these imported parts constitute in excess of 50% of the dollar value of all purchased parts installed in domestic bicycles. At the request of the Committee, we would be pleased to submit our analysis of American production costs in documentation of our argument.

We list herewith the imported parts which usually are installed on American bicycles:

Tires and tubes

Rim strips

Spokes

Chains

Pedals

Hand brakes - front and rear

Derailleur components and controls

Multi-speed free wheels

Front hubs

Rear hubs

Three-speed hubs

Coaster brake hubs

You may then ask, exactly what does the so-called American bicycle producer actually produce? The answer is that he produces very little.

That brings us to the issue in contention. The proponents have pictured themselves as American producers. The facts indicate they are substantial importers of foreign bicycle parts which they assemble into domestic bicycles. Bicycle importers are industry people whose companies are U.S. tax payers, employ labor, make substantial expenditures for goods and services, and whose principal activity is the import of complete bicycles from foreign producers.

In our opinion, the issue is one of the market place - an industry competition between bicycle industry people for their share of the U.S. market consumption.

We should like to express our strong protest and to bring to the attention of the Committee the unfair and biased treatment which our Association received relating to passage of HR 12254 by the Ways and Means Committee of the House.

1. Public hearings before the House Subcommittee were held on February 19 and 20. Our Association was not notified nor given the opportunity to present oral testimony and relevant factual material affecting our business interests. The proponents of HR 12254 would have this advantage. Despite our continued protests up to the moment of passage of the Bill on

June 23, our Association was not afforded a public hearing.

2. We first learned of the public hearings from the March 2 Congressional Record. After our attorney protested to the Staff, we were then permitted to file a written submission.

3. The House Committee report dated April 29, 1976, gave broad conclusions favorable to the proponents which were unsupported by the evidence and fundamental questions raised by our submission were virtually ignored. We point out the following:

   a. Misleading and incomplete statistics known or available to the Committee for the most current year 1975 were omitted. The report stated the import of bicycles increased from 18% of market consumption in 1965 to 28% in 1974. This represents an important omission of fact which we reported in our submission and which was not stated in the report, namely that in the year 1975, the market percentage of bicycles imported declined to 23% and, further, that 1976 projections supplied by our submission and supported by domestic industry sources concluded that imports would decline to 17% of market consumption. Current bicycle import statistics indicate a decline even more drastic than that projected:

Jan. 1 - May 31	No. of Bicycles Imported
1975	791,977
1976	543,645
Decline:	32%

b. Report Conclusion

The Committee recommended continuation of the duty suspension . . . "to remove price advantage of foreign bicycle producers." Again, reference is made by the House Committee to foreign bicycles and again the interests of American bicycle importers have been ignored.

The proponents of the original passage of the Bill to suspend duties cited the following basic reasons for the need of their legislation:

1. The paradoxical inequities of tariff treatment of complete bicycles as opposed to component parts.
2. Lack of domestic sources of supply for certain parts.

We address ourselves to the second reason and submit that conditions have changed in the interim (1973-1976) period which makes this argument no longer valid. There is new evidence, not existing in 1973, to conclude that:

1. Present domestic capacity does exist.
2. Duty suspension acts to prevent domestic industry from establishing production in the future.

Domestic industry contention that domestic sources do not exist to supply component parts of bicycles listed for duty suspension are without foundation in fact. There can be no argument that there is an American manufacturer of derailleurs, Excel Dynamic Co., Carol Stream, Illinois, whose product is advertised in the bicycle trade magazine, American Bicyclist. We understand that there is information available in the International Trade Commission to indicate that this company has an annual capacity of 1,000,000 derailleurs. A second American company, Williams Engineering Company, Elk Grove, Illinois, producing bicycle hand brakes, has been forced into bankruptcy during the past month. We understand that Mr. Lynn Williams, President of the company, will testify during this hearing and we believe his testimony will further support the urgent reasons for opposition to this bill.

Finally, there is the case of Bendix Corporation. This company produced coaster brakes in their Elmira, New York, factory, for many years up until 1973. In 1973, the year that corresponds to the duty suspension reenactment year, the company made the decision to transfer their factory production to Mexico. It is important to keep in mind that the original bill did not list coaster brakes as eligible for duty suspension. The reasoning was apparent, namely that duty suspension would not be granted as long as domestic industry existed.

We are informed by representatives of the AFL-CIO, United Auto Workers Union, that 200 workers were thrown out of work when the Elmira factory was shut down in 1973. The UAW bitterly opposed this move; nevertheless, Bendix relocated their bicycle coaster brake production to Mexico.

Now we are informed that the renewal duty suspension bill has added the following component parts as eligible for duty suspension:

Coaster brakes
Alloy butted tubing
Alloy cotterless crank sets
Alloy rims
Frame lugs

Heading the list is coaster brakes. The domestic industry has repeatedly stated that the purpose of duty suspension was the protection of the security of American jobs. Shall we now give duty suspension to coaster brakes? Shall we reward domestic industry by granting duty suspension on coaster brakes at the cost of the loss of employment of 200 workers? We urge you to reject the premise of granting duty free importation of foreign parts by the domestic producers, which is facilitated by the benefits available under the duty suspension bill now under consideration. Indeed, this now creates a new category of unemployment: "Duty Suspension-induced unemployment".

Finally, we submit the most current statistics of the bicycle industry presently available:

Year	Domestic Bicycles	Imported Bicycles	Total Market Consumption	Ratio of Imports
1973	10.0 M	5.2 M	15.2 M	34%
1974	10.2 M	4.0 M	14.2 M	28%
1975	5.6 M	1.7 M	7.3 M	23%

The startling decline of imported bicycles continues into 1976 and bears out the import projections previously submitted by the American Association of Bicycle Importers, Inc.:

Year	Domestic Bicycles	Imported Bicycles	Total Market Consumption	Ratio of Imports
Jan 1 - May 31				
1975	1,898,292	791,977	2,690,269	34%
1976	2,573,024	543,645	3,116,669	17%
Domestic Industry Increase	674,732 35%			
Imported Bicycle Decline		248,332 31%		

Two of the largest bicycle producers, Murray of Ohio Manufacturing Company and Huffmann Manufacturing Company, producing an estimated 50% of domestic production, have both announced glowing financial reports in financial publications for the most current 1976 period. In the July 30 Wall Street Journal, the President of Huffmann Manufacturing Company announced:

"Sales in fiscal 1976 were about 107 million up from 92.1 million from continuing operations a year earlier . . . Huffmann expects U.S. retailers to buy 8.1 million bicycles in 1976, about 7.0 million from domestic producers. That would boost sales by domestic producers about 25% this year."

The continuing precipitous decline in import bicycles, indicating a decline of 32% for the current year to date, should cast a new light upon the necessity of continued duty suspension. The sharp increase in domestic production of 35% for the current year must raise a question as to the validity of the proponents' arguments claiming injury to domestic industry.

The basic position of the American Association of Bicycle Importers, Inc. relating to duty suspension of certain bicycle parts and accessories has been set forth in the submission provided for the House Ways and Means Committee and we submit that statement herewith.

STATEMENT ON BEHALF OF AMERICAN ASSOCIATION OF BICYCLE IMPORTERS, INC. PRESENTED BEFORE THE COMMITTEE ON WAYS AND MEANS, U.S. HOUSE OF REPRESENTATIVES

MR. CHAIRMAN AND MEMBERS OF THE COMMITTEE:

My name is Philip Kamler. I am President of the American Association of Bicycle Importers, Inc. (AABI), a non-profit trade organization of American bicycle importers. Our respective businesses are American owned and American managed.

We thank you for this opportunity to express our views and to state the position of our Association opposing the continuation of the suspension of duty on bicycle component parts for an additional 3-year period to December 31, 1979. Our opposition is predicated upon the fact that such proposed action would be tantamount to a discriminatory import assessment against American companies whose principal activity is the import of complete bicycles. The effect of the presence of imported bicycles in the United States market has been to keep price levels competitive which has led to increased consumer demand and sales for the entire industry. Imports have contributed to the great bicycle expansion in the United States market without displacing domestic production.

To fully understand the issues in contention, there should be a clear statement of what is meant by bicycle production. An American bicycle factory and most foreign bicycle factories fabricate only the frame of the bicycle. The great preponderance of all other component parts are purchased from component sub-suppliers. In the case of domestic bicycle manufacturers, it is reliably reported that 65% or 2/3 of the value of all purchased components are imported from foreign suppliers. Foreign bicycle manufacturers purchase their components in most cases from the identical foreign components parts sub-suppliers as U.S. factories. Thus, we have the picture of domestic and foreign bicycles varying in essence only in the composition of the bicycle frames while the remaining bicycle components are made up of comparable or even identical foreign component parts. American bicycle manufacturers are thus the largest U.S. importers of parts far exceeding replacement parts importers in the quantity of parts imported.

American importers import complete bicycles and thus, in effect, import large quantities of bicycle components fabricated into these complete bicycles having comparable or identical components as those assembled into U.S. produced bicycles. American importers pay import duties on the entire bicycle of 5 1/2 - 11% including the components upon which duty suspension is sought by domestic manufacturers. Importers do not object to the payment of import duties of 5 1/2 - 11% on complete bicycles but to grant duty suspension to domestic manufacturers on the import of comparable or identical components constitutes a preference in favor of the American manufacturer and acts to discriminate against American business men whose principal activity is bicycle importation.

To make the issue even more concrete, let us assume that the f.o.b. values of the components upon which duty suspension is sought is $10 per bicycle and let us assume an average duty of 8.25% (5 1/2 - 11%). An American bicycle importer would then pay duties of $ .825 per bicycle. An American bicycle manufacturer, assembler of components, would receive preferential treatment on the importation of $10 value of components by duty suspension and have a $ .825 trade competitive advantage over an American importer. Duty suspension must be viewed as discriminatory against the ability of an American bicycle importer to compete in the market place.

The proponents of duty suspension have made important omissions of fact in their submissions to the Ways and Means Committee. Statistics have been offered for the period 1965 thru 1974. However, important changes have taken place in 1975 and 1976 which are well known to the domestic industry and which should be brought to the Committee's attention. A precipitous decline in both the number of bicycles imported and per cent share of market consumption has developed in 1975 and continues in 1976. We submit the following statistics:

Year	Domestic Bicycles	Import Bicycles	Total Market Consumption	Ratio of Imports
1965	4.6M	1.0M	5.6M	18%
1972	8.7	5.2	13.9	37%
1973	10.0	5.2	15.2	34%
1974	10.2	4.0	14.2	28%
1975	5.6	1.7	7.3	23%
(estimate) 1976	7.5	1.5	9.0	17%

From the foregoing, it is obvious that import bicycles have suffered a most devastating decline. The number of bicycles imported have declined in each year from 5,200,000 in 1972 to 1,700,000 in 1975. The ratio of imports to total market consumption has declined in each year since 1972 from 34% to 23% in 1975. One would believe from the oral presentations and reading the written submissions of the proponents of duty suspension that the businesses of American bicycle importers are flourishing. This could not be farther from the truth. Imports declined from 4,000,000 bicycles in 1974 to 1,700,000 bicycles in 1975 - a decline fo 56.8%. While the domestic industry complained bitterly that 1975 production declined 44.8% from 10,200,000 to 5,600, 000 bicycles, it is obvious that bicycle imports have declined even more drastically than domestic production. Many importers' businesses are threatened; a number have discontinued operations; the remaining importers are "fighting for their lives". This is a far cry from the picture painted by the domestic industry. The projections for 1976 are not favorable to American importers and indicate a further erosion in both the number of bicycles imported and the market share. We submit the projections of a domestic manufacturer, Huffman Manufacturing Company, in their 1975 report to stockholders:

> Imported bicycles comprise a significant but currently decreasing share of the total U.S. market ... and we feel imports will decrease further in 1976.

This statement is in sharp contrast to statements of proponents of duty suspension. Statements made in the Congressional Record - House H 1477, dated March 2, 1976, conclude that "imports have increased their share of the market ... from 18% in 1965 to 28% in 1974."

Domestic industry proponents of duty suspension picture virtual industry extinction, viz, "the future of domestic bicycle manufacturing industry is threatened." The market forecasts of the two largest U.S. bicycle manufacturers paint a picture to the contrary.

In the January 1976 Bicycle Journal, Bill Keyes, Murray, Ohio manufacturing Company, Executive Vice President, states, "1976 should have a 15 - 20% increase over 1975."

Huffman Manufacturing Co., in a Jan. 15, 1976 news release projected retail sales and shipments in 1976 at approximately 9,000,000 units (1975 - 5,600,000 units)"... we believe imports will be somewhat less than the estimated 1,750,000 units imported in 1975." This statement contrasts with the information which the domestic industry has submitted to the Committee.

We of the Association oppose the continuation of the suspension of duty on bicycle parts as provided in H.R. 12254. The reason for our opposition is that such action would provide unequal and inequitable duty assessment on imported goods. If, indeed, the domestic industry's concern was with discrimination in the tariff schedules, that situation could be remedied by adjustments far short of total duty suspension. Indeed, to continue the suspension would continue the unfair advantage to domestic producers under which the domestic industry has developed an increased market share. The association of domestic manufacturers reasons that disadvantages such as wage rates, workmen's compensation, occupational safety and pollution control, etc., must be remedied by action on the proposed legislation. This request ignores the existence of safeguards for domestic industry under Title II of the Trade Reform Act of 1974. Certainly if the injury and relationship to importations existed as stated by the domestic industry, relief thereunder would be granted after they have proven, through a detailed investigation by the International Trade Commission, that they are entitled to such relief.

The domestic industry association also justifies the present legislation on the grounds of foreign subsidies and grants and foreign unfair competition. The trade laws of the United States, as amended by the Trade Reform Act of 1974, provide ample machinery, under the countervailing duty sections and 337 sections, for complaint to be made and relief given after a full investigation.

Certainly until the machinery available has been utilized, such extraordinary relief as requested in the proposed bill would not be appropriate. As a matter of fact, with the continuing trend towards monetary adjustment favorable to U.S. producers, there is no reason to believe that imports will not continue to drop off at their rapid pace. In fact, as noted in the February 9, 1976, U.S. News and World Report, the cost of labor situation between the domestic industry and many of the bicycle producing countries has turned in the domestic industry's favor. (See page 65, Five-Year Pay Scale Record.)

Conclusions:

The Association submits that the duty suspension on the foreign purchased bicycle components listed in the original Fulton bill and those listed in the proposed new legislation (HR 12254) will have an important impact upon the competitive conditions in the domestic market. The granting of duty suspension on the following bicycle components:

1. Generator lighting sets
2. Derailleurs
3. Caliper Brakes
4. Drum brakes
5. 3-speed hubs incorporating coaster brakes
6. 3-speed hubs not incorporating coaster brakes
7. Click twist grips
8. Click stick levers
9. Multiple free wheel sprockets

is tantamount to granting a legislative advantage to one segment of the American bicycle industry and the Association opposes such duty suspension.

The Association similarly finds the extension of duty suspension to the following additional bicycle components to be discriminatory:

1. Coaster brakes
2. Alloy butted frame tubing
3. Alloy cotterless crank sets
4. Alloy rims
5. Frame lugs

and the Association opposes the inclusion of the additional foregoing components for duty suspension.

The Association submits that there are ample and adequate remedies and safeguards to domestic industry under existing laws and regulations to which the domestic industry may avail themselves.

Finally, most current statistics reveal a startling decline in the number and market share of bicycle imports. The domestic industry's claim that importation of bicycles is the root cause of injury, is without foundation in fact.

It is the belief of the Association that there is no justification for the continuance and expansion of the bicycle parts duty suspension as proposed in HR 12254. In view of the sharply conflicting evidence before the Committee, we urge the Committee to give the appropriateness and necessity of the proposed legislation more detailed scrutiny. The Association would be pleased to give oral testimony to substantiate its position and to assist the Committee in any other way possible.

STATEMENT OF JOHN S. MONAGAN
IN SUPPORT OF H. R. 12254 AND
PROPOSED AMENDMENTS
ON BEHALF OF
SHIMANO AMERICAN CORPORATION

STATEMENT SUPPORTS H. R. 12254 BECAUSE IT WILL STRENGTHEN U. S. BICYCLE INDUSTRY BY SUSPENDING DUTIES ON BICYCLE PARTS AND REQUESTS INCLUSION OF THREE ITEMS NOT NOW CONTAINED IN H. R. 12254

My name is John S. Monagan. I am a partner in the firm of Whitman & Ransom, practicing in Washington.

We represent Shimano American Corporation, a New York company, engaged in the importation and sale of bicycle parts.

Our client supports H. R. 12254 and respectfully urges the Committee to give this bill a favorable report because it will benefit the workers and proprietors in the American bicycle industry.

Only a few years ago this traditional American industry was in serious straits and threatened with complete destruction. Today it is beginning to breathe again, but only because the Congress has allowed it to remain competitive with imports and to compensate for its increasing costs by allowing certain parts to be admitted duty-free and thus lower expenses to the U. S. manufacturer.

The instant bill will extend for 18 months the suspension of duty on certain parts (most of which are now under suspension) and we strongly support this bill as a means of preserving the jobs and economic activity which are by-products of a healthy U. S. bicycle industry.

In addition to the items listed in the instant bill, our clients request the committee to add certain other parts to the list of those upon which duties will be suspended.

These parts are: front free-wheeling systems, disc brakes and free wheeling hubs. It is requested that H. R. 12254 be amended by adding these items to those already included in the bill.

None of these parts is presently being produced in the United States and therefore a suspension of duty will not affect U. S. manufacturers and workers producing like articles.

The disc brakes are a relatively new item and only recently have attained a substantial volume of sales. The front free wheel systems are in production and the first imports will be arriving in the next month or so. The production of free-wheeling hubs is about to begin and deliveries will commence after manufacture has developed a sufficient inventory.

For these reasons, it is appropriate to request a provision for suspension at this time and we respectfully request that these items be added to the list established by the House and contained in H. R. 12254.

PROPOSED AMENDMENT

Paragraph (b) of H. R. 12254 is amended by inserting the words "front free wheeling systems, disc brakes, rear free wheeling hubs" after "alloy rims" and before "and parts * * *".

BEFORE THE

FINANCE COMMITTEE

UNITED STATED SENATE

RE

H. R. 12254

STATEMENT

OF

BICYCLE MANUFACTURERS ASSOCIATION OF AMERICA, INC.

BY: STUART J. NORTHROP
PRESIDENT
HUFFMAN MANUFACTURING COMPANY

Dated: August 24, 1976

75-948 O - 76 - 9

Mr. Chairman and Members of the Committee:

I am Stuart J. Northrop, President of the Huffman Manufacturing Company, Dayton, Ohio. Huffman is a member of the Bicycle Manufacturers Association of America, Inc. ("BMA"), on whose behalf this statement is presented. BMA is a non-profit, voluntary trade association whose members are domestic bicycle manufacturers. Collectively, the BMA companies[1/] manufacture a substantial majority of the bicycles produced in the United States. In addition, this statement sets forth the views of Chain Bike Corporation and Iverson Cycle Corporation, a subsidiary of Stelber Industries, Inc. While not members of BMA, Chain Bike and Iverson are domestic manufacturers of bicycles and have an interest in this matter which is common to that of BMA member companies. Thus, this statement speaks for all American bicycle manufacturers with the singular exception of the Schwinn Bicycle Company which will offer its own statement.

H.R. 12254 essentially represents a continuation, for a limited 18 month period[2/], of the suspension of duty on certain bicycle component parts originally

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1/ Appendix A is a list of BMA member companies.

2/ January 1, 1977 to July 1, 1978

suspended as of January, 1971 3/. The relief contemplated by the provisions of H.R. 12254 is vital to domestic bicycle manufacturers because it at least partially offsets the inherent bias against domestic manufacturers in the existing tariff schedule. Without a continuation of this duty suspension, the competitive posture of domestic bicycle manufacturers will be severly undermined and the tenuous economic viability of this small industry could be destroyed. Therefore BMA offers this statement in support of H.R. 12254, which was the subject of an overwhelming positive vote in the House, and urgently requests your support for its passage.

As a predicate to discussing the specific bases for the relief sought it is appropriate to present a brief picture of the economic plight of the United States bicycle manufacturing industry. Collectively, the industry is a small one, comprised of only eight companies. These companies are individually small, and for the most part their businesses are limited to the production and sale of bicycles. Unfortunately, their economic outlook is grim. Beginning at the end of the 1960's and during the early 1970's bicycle sales reached record

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3/ The original bill was introduced by Congressman Fulton in 1970 and covered a three year period. In 1974, by P.L. 93-490, it was extended through 1976. The original bill and P.L. 93-490 covered generator lighting sets in TSUS 912.05 and derailleurs, caliper brakes, drum brakes, three-speed hubs incorporating coaster brakes, three-speed hubs not incorporating coaster brakes, click-twist grips, click stick levers, and multiple freewheel sprockets in TSUS 912.10. H.R. 12254 would add coaster brakes, alloy butted frame tubing, frame lugs, alloy cotterless crank sets, and alloy rims to the latter, none of which are domestically produced, and would cover "parts" of the items contained in both TSUS 912.05 and 912.10.

levels to the point where those years are commonly referred to as the "bicycle boom." However, in more recent years, the "boom" has turned to "bust", as a dramatic drop-off of sales and the difficult economic recession have combined to debilitate the industry to the point where the very survival of a number of segments of our industry is in jeopardy and to the point where it can fairly be called a depressed industry. During this past year alone, the H.P. Snyder Manufacturing Company was forced to close its doors after 81 continuous years of bicycle production, and the Iverson Cycle Corporation and its parent, Stelber Industries, Inc., were forced into Chapter 11 bankruptcy. As between 1974 and 1975, bicycle sales dropped more than 50 percent. The prospects for 1976 are not very much brighter and all indications point to a continued struggle for industry survival in the years to come.

Within that framework, the urgent need for a continuation of the duty suspension on certain bicycle components is most clear and the discrimination against domestic bicycle producers inherent in the existing tariff schedules is starkly revealed.

Under the tariff schedules, the involved bicycle parts are assessed a duty of 15 percent. In contrast, completed bicycles manufactured abroad and imported into this country are assessed a duty of only

5.5 percent.[4] That this tariff bias discriminates against and disadvantages the competitive posture of American manufacturers is thus clear. An imported bicycle incorporating the very same components as an American bicycle is bestowed with a 9.5 percent cost advantage on those component parts. The deplorably anamoly created presents the domestic manufacturer with the unacceptable choice of passing the additional cost on to the consumer thereby becoming non-competitive or absorbing the cost increases and thereby reducing margins to an intolerable level. Either way, the American producer suffers, and in light of the economic situation of the industry, that disadvantage cannot be assimilated.

Yet, the bias inherent in the existing tariff schedules is not the only basis for passage of H.R. 12254. The components which are the subject of the bill are domestically unavailable to American bicycle producers either because, as in most cases, they are not manufactured in this country at all or, in a few cases, because the supply from domestic producers is of an unproven product or is not available in quantities nearly sufficient to satisfy the needs of the collective domestic bicycle industry.

4/ The duty on completed bicycles imported into the United States ranges from 5.5 to 11 percent. However, the majority of bicycles imported are of a character which subject them to only the nominal 5.5 percent duty, and the overwhelming majority, and perhaps almost all the imported bicycles utilizing the components covered by H.R. 12254, are only subject to the 5.5 percent duty. Pursuant to TSUS 732.18, if both wheels of the bicycle are over 25" in diameter, and are valued over $16.66 2/3, the duty is 5.5 percent. Thus, bicycle duty at rates over 5.5 percent are virtually irrelevant to the matter of H.R. 12254.

In either event, the American bike-maker has no choice but to utilize foreign-made components and in turn be subject to the discriminatory duty. Of all the components encompassed in the bill before you, only derailleurs and caliper brakes are made, to any extent at all, in this country and, as will be shown, their "availability" is, at best, only ostensible.

One U.S. company, Excel, a subsidiary of Beatrice Foods, Inc., recently undertook the production of one model of derailleur. While each bicycle manufacturer will individually form an opinion as to the acceptability of that single derailleur for use within its product line, Excel cannot be in a position to produce a sufficient derailleur supply for the entire domestic bicycle manufacturing industry, which requires and utilizes a substantial variety of derailleur models. In fact, after originally introducing its derailleur approximately one year ago, it withdrew same for, as I understand it, purposes of redesign. Even assuming for purposes of discussion the acceptability of the Excel product from a design standpoint, it does not serve to significantly diminish the need of the domestic industry to obtain derailleurs from abroad. As a relatively new entrant into the complex derailleur market with a single model, the capacity of this one company to provide sufficient supply to the industry collectively is unlikely and the need for many additional models remains unaddressed in this country.

Similarly, the Pennsylvania Wire Rope Corporation has indicated that it has developed a caliper brake prototype although, to the best of our knowledge, if such a prototype exists, it is not generally available for evaluation. Thus, bicycle manufacturers cannot be assured that it meets their individual performance criteria or braking requirements of the mandatory federal bicyle standard promulgated by the U.S. Consumer Product Safety Commission. Further, in a letter to Huffman Manufacturing Company dated June 25, 1976, an official of Pennsylvania Wire Rope Corporation indicates that it does not yet even have tooling in its plant to make the brakes, and the letter implies that the company does not intend to make a major selling effort and thus presumably no major production effort, if any, at this time.

Thus it is clear that the "availability" of caliper brakes domestically from Pennsylvania Wire Rope Company, even putting aside any considerations of quality, is not real and could not presently effect, to any meaningful extent, the need of bicycle manufacturers to look to foreign sources for caliper brakes.

Finally, the Lynn A. Williams Engineering Company makes a product only related to a component covered by the bill. Its product is a <u>hydraulic</u> caliper brake, as opposed to the <u>mechanical</u> caliper brake which is widely used throughout the industry. This hydraulic brake, having been marketed for approximately two years and offered generally to the industry for one, has met with only very limited acceptance, having been utilized, to the best of our knowledge, by only one retailer for a segment of its private label merchandise. Even assuming acceptability however, Williams is in no position to satisfy the brake component needs of the collective bicycle manufacturing industry. According to an article published in the June 30, 1976 issue of the Chicago Daily News, the Williams brake was found to be faulty due to leaks of hydraulic fluid and the first 60,000 units made were recalled and ultimately replaced. This forced the company into bankruptcy leaving grave questions as to the production capabilities, if any at this point, of the company. In any event, this single company which offers a hydraulic brake may not offer a product useable by or satisfactory to all bicycle manufacturers and, under the circumstances, standing alone, cannot respond to the needs of the collective industry.

The foregoing discussion concerning the "availability" of components in this country should in no way be interpreted as a lack of support by BMA and its members for the evolution of domestic sources of supply. To the contrary, BMA encourages the development of products and production in this country, and its members welcome intiatives in that regard. BMA members have cooperated with Excel, Pennsylvania Wire Rope, and Williams in the development, testing, and evaluation of their products and will continue to be receptive to and cooperative regarding product development intiatives. The fact is however, that until and unless those or other companies develop satisfactory products in production lot quantities, the bicycle industry has no choice but to purchase abroad. Thus, as to all of the components covered by H.R. 12254, there is no viable domestic alternative to the purchase of foreign goods, and, as discussed, that includes derailleurs and brakes as well.

BMA acknowledges that the day may well come where one or more of the components addressed by H.R. 12254 is available from domestic sources, but that day has not arrived and cannot be foreseen anytime very soon. However, it is with an eye toward the development of domestic capacity that H.R. 12254 only envisions the extension of duty suspension a mere 18 months. While this relatively brief extension is vital to the bicycle manufacturers, it creates no prejudice for domestic industries which may wish to undertake or expand production of components. At the end of the 18 month period the Congress can again review the situation and if, at that time, a domestic supply of a given component is available, appropriate changes in the duty situation can readily be made to accommodate the change in circumstances.

At the present time, continuation of the suspension of duties is clearly warranted. BMA urges you to pass H.R. 12254 and thereby avoid aggravating the difficulties faced by domestic manufacturers of bicycles. The tariff inequities are clear and, given the lack of supply in this country of components which are necessary to the production of bicycles, the passage of H.R. 12254 is vital to our struggling industry.

Thank you for your consideration and providing this opportunity to comment.

APPENDIX A

MEMBERSHIP

BICYLE MANUFACTURERS ASSOCIATION OF AMERICA, INC.

1. AMF Wheel Goods Division
   P.O. Box 344
   Olney, Illinois 62450

2. Columbia Manufacturing Co., Inc.
   Westfield, Massachusetts 01085

3. Huffman Manufacturing Co.
   P.O. Box 1204
   Dayton, Ohio 45401

4. LRV Industries
   2536 North Seamna Street
   South El Monte, California 91733

5. Murray Ohio Manufacturing Co.
   Franklin Road
   Brentwood, Tennessee 37027

UNITED STATES SENATE FINANCE COMMITTEE

COMMENTS REGARDING
H. R. 12254
A BILL TO SUSPEND THE
DUTIES ON CERTAIN BICYCLE
PARTS

Schwinn Bicycle Company
1856 North Kostner Avenue
Chicago, Illinois 60639
(312) 292-2900

Keck, Cushman, Mahin & Cate
8300 Sears Tower
233 South Wacker Drive
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(312) 876-3400

Attorneys for
SCHWINN BICYCLE COMPANY

SCHWINN BICYCLE COMPANY

REMARKS ON H.R. 12254

BEFORE SENATE FINANCE COMMITTEE

SUMMARY OF ARGUMENT

1. What H.R. 12254 does:
   - A. Extends for eighteen months the duty suspension on nine bicycle parts which has been in effect for six years.
   - B. Adds five additional parts to the duty-free category.

2. Reasons for the duty suspension:
   - A. The Tariff Schedules create a distinct disadvantage to American bicycle manufacturers in that most imported parts are assessed at 15% *ad valorem* while most imported bicycles are assessed at 5.5% *ad valorem*.
   - B. Twelve of the fourteen parts covered by the bill have *no* domestic sources of supply. Caliper brakes and derailleurs are not available in sufficient quantity and sufficient quality from domestic suppliers. Schwinn must still rely on foreign sources for these components.

3. Effect of Expiration of the Tariff Suspension:
   - A. Inflated bicycle prices to consumers.
   - B. Loss of sales to foreign-made bicycles.

4. Economic State of the industry is perilous:
   - A. Two of the American bicycle manufacturers filed for bankruptcy in 1976.
   - B. Schwinn has been forced to drastically reduce its labor force as orders have significantly diminished.

5. It is essential to Schwinn and the other American bicycle manufacturers that H.R. 12254 pass the Senate prior to adjournment in early October.

I N D E X

Schwinn Bicycle Company submits these comments in support of H.R. 12254 to supplement the oral testimony of Mr. Jay C. Townley, Schwinn's Director of Product Safety and Governmental Affairs, which was presented to the Committee on August 24, 1976. Schwinn respectfully requests that the Committee on Finance favorably report this bill to the full Senate at the earliest opportunity so that the bill may be considered prior to adjournment of the session. Without the passage of H.R. 12254, the current duty suspension of bicycle parts in T.S.U.S. Item No. 912.05 and 912.10 will expire on December 31, 1976.

Schwinn is an Illinois corporation with its sole place of business in Chicago, Illinois. Since 1895, Schwinn has produced and sold high quality bicycles and component parts and has established a reputation for high standards of performance and workmanship. In 1975, Schwinn's sales accounted for approximately twelve percent (12%) of all bicycles sold in the United States. Schwinn has perhaps the best vantage point of any American bicycle producer in commenting on the problems of foreign competition, imports and exports. Like other domestic producers, Schwinn imports a great many foreign parts which are either unavailable, not of sufficient quality or not available in sufficient quantities in the domestic market. In addition, Schwinn also imports complete bicycles including its Schwinn-approved "Traveller", "LeTour" and "Voyageur II" models. These are high quality lug-framed bicycles ranging in price from approximately $137 to $335. However, Schwinn is primarily a domestic manufacturer of bicycles and wants to foster the well-being of the American bicycle industry. It is in pursuit of this goal that we are advocating the extension of the current duty suspension on certain bicycle parts.

A. History of the Tariff Suspension of Bicycle Parts

In 1970, Representative Fulton of Tennessee first proposed the tariff suspension for certain bicycle parts. Public Law 91-689, commonly known as the "Fulton Bill," created two duty-free categories in the tariff schedules, T.S.U.S. Items No. 912.05 and 912.10 which encompassed nine parts: generator lighting sets, derailleurs, caliper brakes, drum brakes, three-speed hubs incorporating coaster brakes, three-speed hubs not incorporating coaster brakes, click twist grips, click stick levers, and multiple free-wheel sprockets. These duty-free categories were extended for an additional three-year period in 1974 by Public Law 93-490. A copy of the relevant tariff schedule is included as Exhibit A. Absent the legislative relief of H.R. 12254, these provisions will expire on December 31, 1976.

B. Background of H.R. 12254

The proposed legislation now before the Senate was introduced by Representative Daniel Rostenkowski of Illinois on March 2, 1976. The House of Representatives overwhelmingly approved the bill on June 22, 1976.

H.R. 12254 has three operative provisions. First, the suspension of tariffs on nine parts which is currently in effect would be extended until June 30, 1978. This is clearly the most important feature of the legislation. Second, five parts - coaster brakes, alloy butted frame tubing, frame lugs, alloy cotterless crank sets, and alloy rims - would be added to the duty-free category. These new parts are not available from domestic sources of supply and thus fit squarely within the rationale of the original tariff suspension legislation.

Third, the words "and parts of all the foregoing" would be inserted in T.S.U.S. Items No. 912.05 and 912.10. This language would allow subcomponents of the duty-free parts to also be exempt from duty. The Customs Service takes the position that unless subcomponents are specifically mentioned in a tariff classification, they are not included. See for example, Ruling Number ORR 209-71 issued by Mr. A. P. Schifflin, Director of Tariff Classification Rulings, regarding parts of caliper brakes which appears as Exhibit B. While this issue has a minor financial impact on Schwinn and other manufacturers, it often causes considerable confusion in liquidating entries through Customs.

C. <u>Reasons for the Duty Suspension</u>

1. <u>Tariff Disparity Between Parts and Complete Bicycles</u>

There are two basic reasons for the continuing tariff suspension on bicycle parts. First and most importantly, there is an anomalous disparity in the tariff schedules between the treatment afforded bicycle parts which are imported into this country for assembly into American-made bicycles and the treatment given to imported, foreign-made bicycles. Most bicycle parts fall within T.S.U.S. Item No. 732.36 and are assessed at a rate of 15% ad valorem. Complete bicycles, on the other hand, fall within T.S.U.S. Item No. 732.02 through 732.26 and are assessed at rates ranging from 5-1/2% to 11%. The vast majority of these imports fall within T.S.U.S. Item No. 732.18:

> "Bicycles:
>
> Having both wheels over 25 inches in diameter:
>
> Valued over $16.66-2/3 each."

This category carries a rate of 5.5% ad valorem for column 1 countries. This strange feature of the tariff schedules creates an inequitable competitive disadvantage for American bicycle manufacturers. For example, Schwinn imports spokes from Germany for use in its bicycle production in Chicago. These spokes are assessed at 15% ad valorem. If the very same spokes were incorporated into a European bicycle and sent to this country, they would be assessed, as part of the complete bicycle, at 5.5% of their value. Obviously, this gives foreign manufacturers a significant cost advantage in marketing their bicycles. A sus-

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pension of tariffs on the parts embodied in T.S.U.S. Items No. 912.05 and 912.10 partially compensates for this ongoing disparity.

Absent the legislative relief embodied in H.R. 12254, on January 1, 1977 the nine parts which ~~have for the last six~~ years been entered into this country duty-free will be subject to 15% *ad valorem* duty. The increased ~~cost to the~~ manufacturer, particularly in light of the depressed state of the American bicycle manufacturing industry, will inevitably have to be passed on to the consumer in the form of higher prices. The more costly American-made bicycles are, the more favorable will be the position of foreign bicycles in the American market. The truth of this assertion is best illustrated by the interest of the American Association of Bicycle Importers in the consideration of H.R. 12254. In opposing the legislation, the AABI implicitly confirms that the defeat of this bill and the expiration of the duty-free categories will increase the cost of American bicycles and hence improve the business interests of foreign bicycle manufacturers and importers.

The report which accompanied the original tariff suspension (Senate Finance Committee Report No. 91-1536, December 30, 1970) stated that the purpose of the bill was

> "...to improve the competitive ability of domestic manufacturers of bicycles

> by temporarily suspending the duty on imports of certain bicycle parts and accessories, thereby reducing their costs." 1970 U.S. Code Cong. and Admin. News, p. 6115.

At that time imports comprised approximately 28% of the total U.S. market. Since that time market share percentages have varied greatly. Encouraged by the Kennedy Round staged reduction of tariffs on complete bicycles from 1968 through 1972, bicycle imports climbed to a level of 37% of the total U.S. market in 1972. In subsequent years these market share percentages have subsided substantially but imports still constitute a significant portion of the American market and in 1976 occupied only slightly less than the percentage they did in 1970 when the suspension on certain bicycle parts was first introduced. See Exhibit C for complete statistics from 1895 through 1975.

2. Lack of Domestic Sources of Supply

The second major reason for enacting the "Fulton Bill" in 1970 was the fact that the parts included were not generally available from domestic sources of supply. It seemed pointless to assess duties on parts, and hence raise the cost of the bicycle to manufacturers and to consumers alike, when the manufacturers were compelled to purchase parts from abroad anyway. Although the domestic supply situation has changed somewhat since the last extension of the duty suspension, Schwinn is still completely dependent on foreign sources of supply for the fourteen parts covered by H.R. 12254. With or without the passage of H.R. 12254 Schwinn will still out of necessity, purchase all of the fourteen parts included in this bill from its Asian and European suppliers. Twelve of the fourteen parts have <u>no</u> domestic sources of supply whatever. The new, limited sources for derailleurs and caliper brakes are explained in detail below. However, because of insufficient quality, Schwinn cannot utilize these sources.

In 1975 alone, Schwinn purchased $6,098,990 worth of parts currently in the duty-free categories. If the tariff suspension had not been in effect, this would have resulted in additional payments to the U.S. Customs Service of $928,968.90. See Exhibit D for a detailed breakdown of Schwinn's 1975 purchases of parts covered by H.R. 12254. As will be explained in more detail below, Schwinn lost money in its bicycle production operations in 1975. There is no feasible way in which this additional duty could have been absorbed by the Company. Of necessity, consumer prices would have been raised to absorb these increased costs.

It is also significant to look at the statistics on Schwinn's importation of five parts which H.R. 12254 would add to the duty-free categories. In 1975 Schwinn purchased 261,352 coaster brakes from Mexico and Japan at a cost of $741,717. Schwinn paid duty on these entries of $111,257.55, yet there is not a single source of coaster brakes in the United States at this time.

Schwinn submits that this situation is a strong illustration of the need for duty suspension on fourteen selected parts in H.R. 12254.

D. The New Domestic Source of Supply

Of the fourteen parts in H.R. 12254, twelve have absolutely no domestic sources of supply. The American sources of the other two parts, caliper brakes and derailleurs, as explained below, are new, largely untested and available only in limited quality and limited quantity. For these reasons, Schwinn must still look to foreign sources for these parts.

Since October 1974 when the last tariff suspension bill was enacted limited domestic production of derailleurs has been initiated by Excel Incorporated, a Division of Beatrice Foods. Quotations which Schwinn has received from Excel are below prices charged by foreign derailleur makers. Schwinn has examined in detail and tested the Excel derailleur and made a business decision that it cannot incorporate this component due to insufficient quality. Similarly, the Pennsylvania Wire Rope Company has recently developed prototypes of a caliper brake although Schwinn is not aware of any production sales of this component as of this date. Schwinn conducted extensive testing on this component, as well, and similarly rejected its inclusion on Schwinn merchandise because of insufficient quality.

Another brake manufacturer, Lynn A. Williams Engineering

Company, has within the last year developed and offered for sale a new "hydraulic" braking system. Schwinn engineers have been in contact with their counterparts at the Lynn A. Williams Engineering Company since 1972, advising as to the performance specifications which Schwinn required in its brakes and suggesting changes and improvements which they felt might be of value. Schwinn thoroughly tested the Williams hydraulic brake when it was finally developed and concluded that it did not meet Schwinn's standards of quality.

Subsequent events may have mooted the whole question of the viability of the Lynn A. Williams Engineering Company as a domestic supplier. As described in a June 30, 1976 article in the Chicago Daily News, 100,000 of the Williams' brakes were sold for use on Sears, Roebuck & Company bicycles. After 60,000 units had been manufactured, a defect was discovered which required either repair of the brakes at a cost of $1.91 per unit or complete replacement. Although the company had, according to the article, expected a profit of $100,000 in 1975, a time when the tariff suspension on caliper brakes was in effect, the cost of replacing the defective brakes drove the company into severe financial difficulties. On May 24, 1976, a petition under Chapter XI of the bankruptcy laws was filed in the United States District Court for the Northern District of Illinois.

Prior to the consideration of H.R. 12254 in the House of

Representatives, the Commerce Department and International Trade Commission reviewed in detail the American production of parts covered by the bill. In the Subcommittee on Trade Hearings, Mr. Sterling Nicholson of Commerce recommended that the bill be passed but suggested that the three-year extension, which was originally in the bill when introduced, be reduced to eighteen months. Commerce Department representatives reasoned that after that shorter period, it would be possible to evaluate whether the new American parts producers could supply adequate quality and quantity to the bicycle manufacturers. The Committee on Ways and Means in the House of Representatives accepted this recommendation and limited the extension to June 30, 1978.

Schwinn does not object to this shortened period. The Company has no preference whatsoever as to where it purchases its parts. It simply seeks a combination of top-flight quality coupled with competitive pricing in choosing its suppliers. However, the quality consideration is foremost. Schwinn, the fourth largest American bicycle manufacturer, is dependent on its quality image and reputation in maintaining its viability in the market. In addition, under the new United States Consumer Product Safety Commission bicycle safety regulation, Schwinn and other manufacturers must certify that their bicycles meet sixty-four detailed manufacturing requirements. Failure to comply with any of these comprehensive specifications subjects the manufacturer to a repurchase of all noncomplying units. It is thus absolutely essential that Schwinn be perfectly sure that all components meet both the minimum federal requirements and Schwinn's own high standards of performance and design.

Schwinn respectfully submits that it will be forced to purchase both derailleurs and caliper brakes from abroad with or without the passage of H.R. 12254 until such time as domestic producers match the quality of foreign components. Schwinn does not believe that its costs and consumer prices should be artificially inflated with extra tariff duties to protect unproven sources of supply. Schwinn further submits that the Commerce Department suggestion, as now embodied in H.R. 12254, provides an early reevaluation of the American supply situation and is equitable for all parties concerned.

E. Financial Condition of Schwinn and the American Bicycle Industry

The relief offered by this tariff suspension bill is of critical importance to Schwinn particularly at this point of time. Schwinn and other bicycle manufacturers are facing one of the most difficult periods in their history. In the late 1960's and early 1970's, demand for bicycles, both imported and domestic, exploded. However, the famed "bicycle boom" has evidently run its course. In 1974 total market consumption slumped by over 1,000,000 units to 14,105,775. In 1975 the total market was down almost 50% to 7,293,784 units. Schwinn alone experienced a staggering 36% decline in 1975. As can be seen from Exhibit E, Schwinn's sales figures for 1976 are running significantly behind the 1975 pace.

The effect of the reduced sales on the workers at Schwinn has been devastating. Included as Exhibit F are Monthly Reports on Labor Turnover for 1972 through July, 1976 which Schwinn has filed with the Illinois Department of Labor. In 1972 monthly employment levels were consistent and steady in the 1,900 to 2,200 range. During every month of 1973, over 2,200 Chicago workers were on the Schwinn payrolls. This trend continued through much of 1974 until market demand lagged drastically in the fall. With no orders to fill, Schwinn was forced to lay off over 1,000 employees in late 1974. January 1975 was the worst month in this period with only 841 workers on the payrolls.

Although many of these workers were rehired, there have been periodic layoffs throughout 1975 and 1976 as sales continued to decline. The official labor reports clearly show that the monthly average of employees at Schwinn during 1975 was 1,525. So far in 1976 the average has sunk to 1,486 - a far cry from the 2,200 of 1973.

As sobering as these figures are, they do not reflect the full scope of our difficulties. In an effort to keep as many Schwinn workers as possible on the job, the Company has been forced to resort to many four-day work weeks throughout 1975 and 1976. The very week these hearings are being held, there will only be four days of bicycle production in our Chicago plant.

When Schwinn and other manufacturers speak of economic hardship and serious erosion of our work force, it is not based on abstract philosophizing or unsubstantiated theories. Schwinn faces the unpleasant prospect of laying-off large numbers of its workers on a month-by-month, week-by-week basis.

The financial picture at Schwinn is similarly distressing. The bicycle manufacturing operations resulted in a significant loss in 1975. It is clear that Schwinn would not have been able to absorb the approximately $1,000,000 in additional duties which would have resulted if the tariff suspension had not been in effect in that year. These additional costs would, of necessity, have been passed on to the consumers.

Other manufacturers have experienced even greater difficulties. Iverson Cycle Corporation filed Chapter XI proceedings in bankruptcy in March of this year. H. P. Snyder Company, a subsidiary of O. F. Mossberg & Sons, Inc., terminated its bicycle production on May 7, 1976 after 81 continuous years in business. Shortly thereafter, on June 18, 1976, that company also filed a petition under Chapter XI of the bankruptcy laws.

It is clear that the small and dwindling American bicycle manufacturing industry is suffering a severe depression. Without the extension of the duty suspension, the American bicycle manufacturers will be forced to make a decision between equally unacceptable choices. They must either absorb the increased duty, even though most manufacturers have been operating at a loss for the last eighteen months, or they must increase the cost of their product to the consumer. This latter action would cause a senseless inflation of prices and would inevitably result in a loss of sales for American bicycle manufacturers.

Conclusion

For all the foregoing reasons, Schwinn Bicycle Company respectfully requests that the Committee on Finance favorably report H.R. 12254 to the full Senate at the earliest opportunity. Time is of the essence. The current tariff suspension expires on December 31, 1976. If H.R. 12254 is not passed by the full Senate prior to its adjournment in early October, the tariff suspension will expire causing bicycle prices to be unnecessarily inflated, losses to manufacturers to be compounded and American jobs to be jeopardized. Schwinn submits that the logic which justified the tariff exemption of 1970 and 1974 is stronger than ever in the troubled market of 1976.

Respectfully submitted,

Jay C. Townley

Jay C. Townley

Schwinn Bicycle Company
1856 North Kostner Avenue
Chicago, Illinois 60639
(312) 292-2900

Brock R. Landry

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Chicago, Illinois 60606
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Attorneys for
SCHWINN BICYCLE COMPANY

EXHIBIT A

TARIFF SCHEDULES OF THE UNITED STATES ANNOTATED (1975)

APPENDIX TO THE TARIFF SCHEDULES
Part 1. - Temporary Legislation

Item	Stat. Suf-fix	Articles	Units of Quantity	Rates of Duty 1	Rates of Duty 2		Effective Period
911.13	1/	Copper bearing ores and materials (provided for in items 602.13 or 603.50, part 1, schedule 6).	1/	Free of duty imposed on copper content under items 602.39 or 603.50	No change		On or before 6/30/75
				Rates of Duty 1-a	**1-b**	**2**	**Effective Period**
911.14	1/	Cement copper and copper precipitates (provided for in item 612.02, part 2C, schedule 6)	1/	Free	No change	No change	On or before 6/30/75
911.15	1/	Black copper, blister copper, and anode copper (provided for in item 612.03, part 2C, schedule 6).	1/	Free	No change	No change	On or before 6/30/75
911.16	1/	Other unwrought copper (provided for in item 612.06, part 2C, schedule 6)...	1/	Free	No change	No change	On or before 6/30/75
				Rates of Duty 1	**2**		**Effective Period**
911.25	00	Synthetic rutile (provided for in item 603.70, part 1, schedule 6).	[illegible]	Free	No change		On or before [illegible]
911.60	[illegible]	Catalysts of platinum and carbon (provided for in item 6[illegible], part [illegible], schedule 6) [illegible] imported for use in [illegible]		Free	Free		On or before 10/31/[illegible]
911.70		[illegible]		Free	Free		On or before 6/30/76
912.05	00	[illegible] (provided for in item 6[illegible], part [illegible], schedule [illegible])		Free	No change		On or before 12/31/76
912.08		[illegible] (provided for in item [illegible], part [illegible], schedule [illegible])		Free	No change		On or before [illegible]
912.10		[illegible] (provided for in item [illegible], part [illegible], schedule [illegible])		Free	No change		On or before 12/31/76

1/ [illegible] period for special tariff treatment has expired.

BEST COPY AVAILABLE

EXHIBIT B

CUSTOMS INFORMATION EXCHANGE
U.S. Customhouse Bowling Green
New York, New York 10004

ORR Ruling 209-71
May 12, 1971
Bureau File: MFG 433.7 c
Date: March 26, 1971

REFERENCE: Item 732.36, TSUS.

SUBJECT: Brake cables, brake shoes and levers for caliper brakes classifiable under item 732.36, TSUS.

In a letter dated February 16, 1971, you inquired as to the dutiable status of brake cables, brake shoes, and levers for caliper brakes. ORR 209 5/1

For the purpose of this reply it is assumed that the subject merchandise is not the product of any of the communist countries listed in the attached copy of General Headnote 3(e), Tariff Schedules of the United States (TSUS).

It is the opinion of the Bureau that while the subject articles are parts of caliper brakes they are excluded from free entry under item 912.10, TSUS, because there is no provision for parts thereunder.

Accordingly, such parts are classifiable under the provision for other, parts of bicycles in item 732.36, TSUS, with duty at the rate of 15 percent ad valorem.

Sincerely yours,

(Signed) A. P. Schifflin

Acting Director
Division of
Tariff Classification Rulings

- - - - - - - - - -

Paul Kasper
Acting Director

NOTE: This circular may be released to the public only if the name and address of recipient and other identifying material are deleted.

EXHIBIT C

U.S. Bicycle Market Statistics—1895 To 1975

	1	2	3	4	5	6	7	8	9	10	11	12
					TOTAL U.S. MARKET APPARENT CONSUMPTION				SCHWINN BICYCLE COMPANY			
YEAR	U.S.A. RESIDENT POPULATION (THOUSANDS)	DOMESTIC INDUSTRY SHIPMENT BICYCLES —	EXPORTS U.S.A. BICYCLES +	IMPORTS U.S.A. = BICYCLES	BICYCLES	BICYCLES PER 1000 POPULATION	DOMESTIC INDUSTRY % OF TOTAL MARKET	IMPORTS % OF TOTAL MARKET	SHIPMENTS BICYCLES	BICYCLES PER 1000 POPULATION	PERCENT OF MARKET	PERCENT OF INDUSTRY
1895	69 580	800 000			800,000	15 1	100 0		Estimated Total 190 982 Average of 24 630 Per Year			
1896	70 885			.	..	..	..	...				
1897	72 189	2 000,000			2,000,000	27 7	100.0	. .				
1898	73 494				....	.		.				
1899	74,799	1 182 691			1,182,691	15 8	100.0	..				
1900	76 094	1 182 850			1 182 850	15 6	100 0					
1901	77 585				.			.				
1902	79 160		.		.....	.	.	..				
1903	80 632				..	.		..	53 466	7		
1904	82 165	250 487			250,487	3 0	100.0		20 215	2	8 0	8 0
1905	83 820								38 979	5		
1906	85 437					.	. ..	. .	46 991	6		
1907	87 000				.		.		54 284	6		
1908	88 709							.	31 096	4		
1909	90 492	233 707			233,707	2 6	100.0	.	46 454	5	19 8	19 8
1910	92 407								73 360	8		
1911	93 868				.			.	73 401	8		
1912	95 331				.		.		72 942	8		
1913	97 227					.	.	.	75 181	8		
1914	99 118	396 899		.	396.899	4 0	100.0	.	59 382	6	15 0	15 0
1915	100 549								53 796	5		
1916	101 966	526 076			526 076	5 2	100.0	.	85 937	8	16 2	16 2
1917	103 266	606 918			606.918	5 9	100 0		82 581	8	13 6	13 6
1918	103 203	567 297			567 297	5 5	100 0		46 868	5	8 3	8 3
1919	104 512	479 163		.	479 163	4 6	100 0		46 028	4	9 6	9 6
1920	106 466	750 000			750 000	7 1	100 0		46 207	4	6 2	6 2
1921	108 541	149 192			149 192	1 4	100 0		14 763	1	9 9	9 9
1922	110 055	150 000			150 000	1 4	100.0	.	23 480	2	15 7	15 7
1923	111 950	525 000			525,000	4 7	100 0	.	49 395	4	9 4	9 4
1924	114 113	350 000	6 967		343 033	3 0	102 0	.	32 715	3	9 5	9 3
1925	115 832	[illegible]	[illegible]		257 296	2 2	103 0		29 023	3	11 5	11 2
1926	117 399	300 000	5 344		294 656	2 5	101 8	.	22 382	2	7 6	7 5
1927	119 038	255 000	4 632		250 368	2 1	101 9		22 149	2	8 9	8 7
1928	120 501	348 200	5 289		342,911	2 8	101.5		24 963	2	7 3	7 2
1929	121 770	310 000	8 108		301 892	[illegible]	102 7		29 620	2	9 8	9 6
1930	123 077	300 000	5 746		294 254	2 41	101 2		23 552	2	7 9	7 9
1931	124 040	262 000	3 434		258 566	2 08	100 6		20 739	17	8 0	8 0
1932	124 840	260 100	795		259 235	2 08	100 3		17 152	14	6 6	6 6
1933	125 579	320 000	1 033	5 000	323 967	2 58	98 5	1 5	46 595	37	14 2	14 7
1934	126 374	512 459	1 177	7 500	518 773	4 11	98 6	1 4	86 786	69	16 6	17 0
1935	127 250	597 [illegible]	1 129	13 300	568 830	5 24	98 2	1 9	107 215	84	16 3	17 2
1936	128 053	1 218 415	2 372	17 100	1 233 193	9 63	98 3	1 4	201 443	1 57	16 3	16 3
1937	128 825	1 131 300	3 849	16 000	1 143 160	8 87	98 9	1 4	168 457	1 31	14 8	14 9
1938	129 825	851 526	3 237	16 500	864 989	6 66	98 5	1 9	121 729	94	14 1	14 3
1939	130 880	1 252 486	6 [illegible]	12 216	1 258 380	9 61	99 6	1 0	189 937	1 45	15 1	15 2
1940	[illegible]	[illegible]	[illegible]	21 329	[illegible]	9 [illegible]	100 [illegible]	2 0	[illegible]	1 [illegible]	[illegible]	17 8
1941	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]
1942	[illegible]	560 [illegible]	4 [illegible]	548	[illegible]	[illegible]	[illegible]	0 1	113 359	84	20 3	20 1
1943	[illegible]	[illegible]	[illegible] 13 448	631	[illegible]	1 1	111 1	0 1	16 365	12	10 4	9 2
1944	[illegible]	172 965	[illegible] 24 229	43	148 799	1 12	116 2		18 929	14	12 7	[illegible]
1945	[illegible]	454 [illegible]	[illegible]	3 [illegible]	[illegible]	4 1	101 [illegible]	0 [illegible]	[illegible]	[illegible]	8 [illegible]	[illegible]

(Continued on other side)

EXHIBIT C

U.S. Bicycle Market Statistics—1895 To 1975

(Continued)

0 →	1	2	3	4	5	6	7	8	9	10	11	12
					Total U.S. Market Apparent Consumption				Schwinn Bicycle Company			
Year	U.S.A. Resident Population (1) (Thousands)	Domestic Industry Shipments Bicycles —	Exports U.S.A. Bicycles +	Imports U.S.A. Bicycles =	Bicycles	Bicycles per 1000 Population	Domestic Industry % of Total Market	Imports % of Total Market	Shipments Bicycles	Bicycles per 1000 Population	Percent of Market	Percent of Industry
1946	141 [illegible]	1 653 373	35 436	46 840	1 664 327	11.88	99.3	2.8	362 271	2.16	18.1	18.3
1947	143 446	2 875 000	93 984	19 758	2 800 774	19.52	97.4	.7	486 783	3.39	17.4	16.9
1948	146 093	2 794 516	195 100	16 776	2 706 186	18.82	96.8	.6	602 408	4.12	22.3	21.6
1949	148 665	1 483 099	67 290	15 908	1 481 686	9.76	97.9	1.1	352 308	2.37	24.3	23.8
1950	151 234	1 963 716	25 141	67 789	2 006 364	13.27	97.9	3.4	510 019	3.38	25.5	26.0
1951	153 384	1 925 797	17 396	176 644	2 085 047	13.59	92.4	8.5	466 849	3.05	22.4	24.3
1952	155 761	1 920 179	12 302	245 763	2 153 740	13.83	90.2	11.4	478 838	3.08	22.2	24.9
1953	158 313	2 111 839	9 290	592 999	2 695 629	17.03	78.3	22.0	501 379	3.17	18.6	23.7
1954	161 191	1 531 887	6 167	963 667	2 487 357	15.43	61.6	38.7	356 790	2.21	14.3	23.2
1955	164 303	1 794 968	7 217	(c) 1 223 990	3 011 741	18.33	59.6	40.6	413 395	2.52	13.7	23.9
1956	167 259	1 746 816	5 212	(c) 1 173 346	2 914 952	17.43	59.9	40.2	454 933	2.72	15.6	26.0
1957	170 333	1 884 846	7 981	(d) 748 609	2 625 554	15.41	71.8	28.5	439 482	2.58	16.7	23.3
1958	174 882	2 116 344	9 118	(d) 823 614	2 930 840	16.76	72.2	28.1	451 158	2.58	15.4	21.3
1959	177 830	2 562 330	3 446	(d) 1 013 396	3 572 280	20.09	71.7	28.3	546 230	3.07	15.3	21.3
1960	179 983	2 584 622	2 961	(c)(d) 1 188 914	(a) 3 769 606	20.95	68.6	31.5	516 726	2.86	13.7	19.9
1961	181 543	2 579 993	2 748	(c)(d) 1 087 318	(a) 3 663 663	20.62	70.4	29.6	471 536	2.58	12.9	18.3
1962	185 822	2 954 215	4 920	1 266 790	4 216 177	22.69	70.1	29.9	528 721	2.85	12.5	17.9
1963	189 290	3 118 200	3 512	1 294 901	4 408 689	23.30	70.7	29.3	666 603	3.46	14.9	21.0
1964	192 119	4 082 963	4 113	1 010 836	5 089 686	26.46	80.2	19.8	849 818	4.42	16.7	20.8
1965	194 483	4 619 741	3 503	938 604	5 554 126	28.56	83.6	16.8	876 908	4.51	15.3	19.0
1966	196 756	4 829 122	8 642	927 223	5 747 703	29.30	83.9	16.1	845 249	4.26	14.7	17.5
1967	199 550	5 100 392	5 474	1 117 246	6 292 194	31.46	82.2	17.8	931 306	4.66	14.8	18.3
1968	200 755	5 966 184	5 466	1 534 168	7 495 886	37.3	79.5	20.5	1 032 499	5.14	13.8	17.3
1969	202 [illegible]	5 100 023	6 134	1 978 526	7 063 417	34.9	72.1	27.9	863 761	4.27	12.2	17.8
1970	205 [illegible]	4 943 879	[illegible]	1 947 396	6 891 082	33.6	71.7	28.3	895 819	4.36	13.0	18.1
1971	207 [illegible]	6 518 666	9 636	2 339 470	8 848 240	42.7	73.6	26.4	1 161 796	5.61	13.1	17.8
1972	209 486	8 750 987	9 636	5 154 068	13 896 967	66.3	63.0	37.0	(f) 1 420 813	6.82	10.3	16.3
1973	211 939	10 072 356	16 977	5 154 903	15 210 283	71.9	66.2	33.8	(e) 1 550 213	7.32	10.2	15.4
1974	212 [illegible]	10 161 [illegible]	34 741	3 979 [illegible]	14 [illegible] 779	66.6	71.8	28.2	(e) 1 552 549	7.31	11.0	15.3
1975	213 925	5 456 501	30 082	1 717 845	7 203 706	34.0	76.4	23.6	(e) 891 [illegible]	4.16	12.2	15.9

(1) All census figures based on July 1 population. Source—Series P25 #300 current population reports—Bureau of Census.

Footnotes:

- (a) Preliminary Tariff Commission figure.
- (b) Includes Lend Lease shipments.
- (c) Includes bicycles from Communist-dominated countries.
- (d) Includes imported Tricycles and Velocipede bicycles.
- (e) Includes imported Tricycles, Velocipedes and Le Tour bicycles.

Sources and Descriptions

Column #1 — Population, from U.S. Department of Commerce Bureau of Census—Resident Population.

Column #2 — U.S. Domestic Industry—[illegible]

Column #3, Column #4 — Figures from U.S. Department of Commerce through U.S. Tariff Commission.

Column #5 — Total U.S. Market—Apparent Consumption. Industry figures minus Exports plus Imports—per U.S. Tariff Commission.

Column #6 — Bikes per 1000 Population—Total Market Column #5 divided by Column #1.

Column #7 — Domestic Industry % of Total Market. Column #2 divided by Column #5.

Column #8 — Imports % of Total Market. Column #4 divided by Column #5.

Column #9 — Schwinn Bicycle Company Bicycles net yearly shipments of all bicycles [illegible]

Column #10 — Schwinn Bicycle Company Bicycles per 1000 Population. Column #9 divided by Column #1.

Column #11 — Schwinn Bicycle Company % of Market. Column #9 divided by Column #5.

Column #12 — Schwinn Bicycle Company % of Industry. Column #9 divided by Column #2.

EXHIBIT D

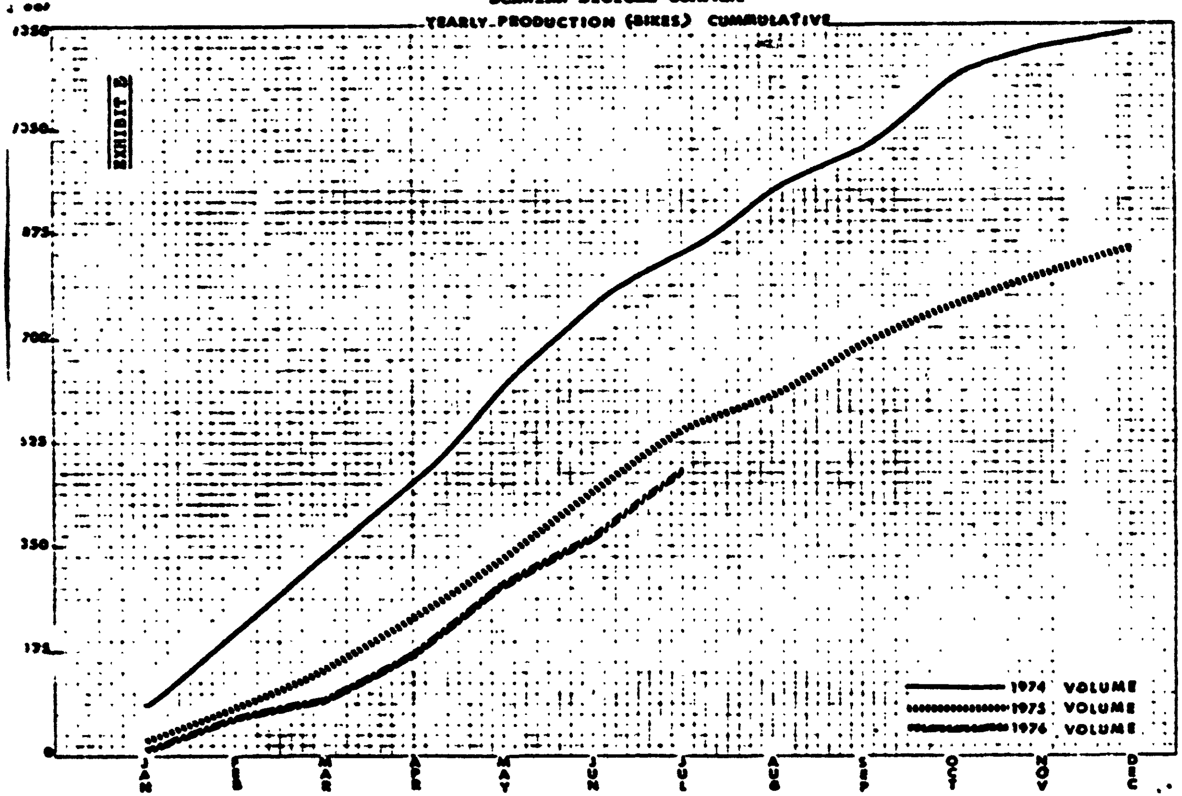
Rostenkowski Bill - Schwinn Import Statistics

Part	Volume Purchases in 1975	Cost
Parts currently duty-free under T.S.U.S. Item No. 912.05 and 912.10:		
1. Generator lighting sets	111,127	$ 353,010
2. Derailleurs	984,743	2,031,633
3. Caliper brakes	1,141,199	2,019.778
4. Drum brakes	2,347	10,069
5. Three-speed hubs incorporating coaster brakes	4,494	52,500
6. Three-speed hubs not incorporating coaster brakes	47,042	272,844
7. Click twist grips	-0-	-0-
8. Click stick levers	-0-	-0-
9. Multiple free wheel sprockets	508,952	1,359,156
	Subtotal	$6,098,990
Parts which H.R. 12254 adds to duty-free category:		
1. Coaster brakes	261,352	741,717
2. Alloy butted frame tubing (sets for 1 bicycle)	775	11,400
3. Frame lugs (for 1 bicycle)	775	4,007
4. Alloy cotterless crank sets	775	44,175
5. Alloy rims (pairs)	775	6,123
	Subtotal	$ 807,422
	TOTAL	$6,906,412

75-948 O - 76 - 11

SCHWINN BICYCLE COMPANY

YEARLY PRODUCTION (BIKES) CUMMULATIVE



BL-1319

STATE	REPORT NO.	IND			AREA	LOCAL OFF

O.M.B. No. 44-R[illegible]
Approval expires January 31 [illegible]

EXHIBIT F

U.S. DEPARTMENT OF LABOR
BUREAU OF LABOR STATISTICS
and
THE MANPOWER ADMINISTRATION
WASHINGTON D.C. 20212

MONTHLY REPORT ON JOB OPENINGS AND LABOR TURNOVER

Enter the data requested and return in the enclosed envelope as soon as the information is available each month

ILLINOIS DEPARTMENT OF LABOR
BUREAU OF EMPLOYMENT SECURITY
RESEARCH AND STATISTICS SECTION
[illegible]
CHICAGO, ILLINOIS [illegible]

CHANGE NAME AND MAILING ADDRESS IF INCORRECT—INCLUDE ZIP CODE

1972

:1432 379-51 X 761 C03022

SCHWINN BICYCLE CO-PERS MGR
1856 N KOSTNER CHICAGO ILL 60639

The Bureau of Labor Statistics, the Manpower Administration, and the State agencies cooperating in their statistical programs will hold all information furnished by the respondent in strict confidence.

LOCATION ____________
(City) (County) (State)

Before entering data see explanations on other side

I LABOR TURNOVER DURING CALENDAR MONTH / II EMPLOYMENT (one pay period)

YEAR AND MONTH (1)	PERIOD COVERED (Cols. 4 through 11) From— (2)	Through (3)	SEPARATIONS (during calendar month) Total Separations (Sum of cols. 5 thru 8) (4)	Quits (5)	Discharges (6)	Layoffs (7)	Other Separations (8)	ACCESSIONS (during calendar month) Total Accessions (Sum of cols. 10 & 11) (9)	New hires (10)	Other Accessions (11)	TOTAL NUMBER who worked during or received pay for any part of the pay period which includes the 12th of the month (12)
1971 Dec.	1	31	42	40	0	0	2	20	23	0	1936
1972 Jan.	1	31	44	38	0	0	6	91	91	0	1933
Feb.	1	29	48	44	0	0	4	94	94	0	1959
Mar.	1	31	52	51	0	0	1	88	86	2	1989
Apr.	1	30	82	77	0	0	5	102	102	0	1993
May	1	31	75	72	2	0	2	140	140	0	2027
June	1	30	83	79	0	0	4	110	112	0	2112
July											
Aug.	1	31	143	140	0	0	3	162	160	2	2140
Sept.											
Oct.	1	31	106	98	2	0	6	148	147	1	2198
Nov.	1	30	92	83	7	0	2	88	87	1	2255
Dec.	1	31	33	31	0	0	1	23	21	5	2291

III JOB OPENINGS for which workers from outside the firm were actively being sought as of close of last business day of most recent month. (If "NONE," enter "0", do not leave blank.)

YEAR AND MONTH	CURRENT JOB OPENINGS (unoccupied and ready for immediate filling) Number of Current Job Openings (13)	No. included in col. 13 remaining unfilled for a month or longer (14)	NUMBER OF OPENINGS WITH FUTURE STARTING DATES (not included in column 13) (15)	DO NOT USE Empl. Code (16)
1971 Dec.	10	5	0	
1972 Jan.	9	4	—	
Feb.	10	3	—	
Mar.	14	7	—	
Apr.	16	5	—	
May	16	6	—	
June	13	6	—	
July	12	4	—	
Aug.				
Sept.	—	—	—	
Oct.	10	6	—	
Nov.	8	2	—	
Dec.				

IV. YOUR COMMENTS

Enter main factors responsible for any significant month-to-month changes in SECTIONS I, II, and III. Examples are:

More business	Weather
Strike	Temporary summer help
Fire	Seasonal increases

(17)

STATE	REPORT NO	IND			AREA	LOCAL OFF

Office of Management and Budget No. 44-R1064
Approval expires January 31, 19

EXHIBIT F (cont'd.)

MONTHLY REPORT ON JOB OPENINGS AND LABOR TURNOVER

U.S. DEPARTMENT OF LABOR
BUREAU OF LABOR STATISTICS
and
THE MANPOWER ADMINISTRATION
WASHINGTON D.C. 20212

Enter the data requested and return in the enclosed envelope as soon as the data are available each month

Return to
ILLINOIS DEPARTMENT OF LAB[OR]
Bureau of Employment Security
165 North Canal Street
Chicago, Illinois 60606
Telephone: 793-4498

CHANGE NAME AND MAILING ADDRESS IF INCORRECT—INCLUDE ZIP CODE

01632 379-51 X 761 003022

SCHWINN BICYCLE CC-PERS PER
1856 N KOSTNER CHICAGO ILL 60639

The Bureau of Labor Statistics, the Manpower Administration, and the State agencies cooperating in their statistical programs will hold all information furnished by the respondent in strict confidence

LOCATION ____ (City) (County) (State)

Before entering data see explanations on other side

I LABOR TURNOVER DURING CALENDAR MONTH

YEAR AND MONTH (1)	PERIOD COVERED (Cols. 4 through 11): From— (2)	Through (3)	SEPARATIONS (during calendar month): Total Separations (Sum of cols. 5 thru 8) (4)	Quits (5)	Discharges (6)	Layoffs (7)	Other Separations (8)	ACCESSIONS (during calendar month): Total Accessions (Sum of cols. 10 & 11) (9)	New Hires (10)	Other Accessions (11)	II EMPLOYMENT: TOTAL NUMBER who worked during or received pay for any part of pay period which includes the 12th of the month (13)
1972 Dec	1	31	[illegible]	21	0	0	1	[illegible]	[illegible]	[illegible]	[illegible]
1973 Jan	1	31	35	32	2	0	1	66	62	4	[illegible]
Feb	1	28	66	60	0	0	6	62	61	1	2234
Mar	[illegible]	31	[illegible]	77	[illegible]	[illegible]	[illegible]	[illegible]	66	[illegible]	[illegible]
Apr	1	[illegible]	64	61	0	0	[illegible]	74	73	1	[illegible]
May	[illegible]	[illegible]	[illegible]	[illegible]		[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]
June		[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]
July	1	31	43	39	1	0	3	74	74	[illegible]	2210
Aug.	1	31	127	122	0	0	5	112	111	1	[illegible]
Sept.	1	30	93	90	0	0	3	83	81	2	[illegible]
Oct.	1	31	97	95	1	0	1	115	114	1	2229
Nov	1	30	54	52	0	0	2	48	47	1	[illegible]
Dec.	1	31	42	42	0	0	0	18	18	0	2226

III JOB OPENINGS for which workers from outside the firm were actively being sought as of close of last business day of most recent month (If "NONE," enter "0". Do not leave blank.)

YEAR AND MONTH	CURRENT JOB OPENINGS (unoccupied and ready for immediate filling): Number of Current Job Openings (13)	Number included in col. (13) remaining unfilled for a month or longer (14)	NUMBER OF OPENINGS WITH FUTURE STARTING DATES (not included in column 13) (15)	DO NOT USE Empl. Code (16)
1972 Dec.	1	1	[illegible]	
1973 Jan.	7	[illegible]	–	
Feb.	6	1	–	
Mar.	[illegible]	[illegible]	–	
Apr.	[illegible]	[illegible]	–	
May	[illegible]	[illegible]		
June	14	5		
July	15	5		
Aug	10	4		
Sept	12	4		
Oct	6	5		
Nov	4	3		
Dec.	10	3		

IV YOUR COMMENTS

Enter main factors responsible for any significant month-to-month changes in SECTIONS I, II and III. Examples are:
More business — Weather
Strike — Temporary summer help
Fire — Seasonal increases

(17)

2

Office of Management and Budget No. 44-R1064
Approval expires January 31, 1975

MONTHLY REPORT ON JOB OPENINGS AND LABOR TURNOVER

U.S. DEPARTMENT OF LABOR
BUREAU OF LABOR STATISTICS
and
THE MANPOWER ADMINISTRATION
WASHINGTON D.C. 20212

Return to:
ILLINOIS DEPARTMENT OF LABOR
Bureau of Employment Security
165 North Canal Street
Chicago, Illinois 60606
Telephone: 793-4698

CHANGE NAME AND MAILING ADDRESS IF INCORRECT—INCLUDE ZIP CODE

1974

EXHIBIT F (cont'd.)

01632 375-51 A 761 003022

SCHWINN BICYCLE CO-PERS MGR
1856 N KOSTNER CHICAGO ILL 60639

LOCATION ______ (City) (County) (State)

Before entering data see explanations on other side

I. LABOR TURNOVER DURING CALENDAR MONTH; II. EMPLOYMENT (one pay period)

Year and Month (1)	Period covered: From (2)	Through (3)	Total separations (4)	Quits (5)	Discharges (6)	Layoffs (7)	Other separations (8)	Total accessions (9)	New hires (10)	Other accessions (11)	Total number (12)
1973 Dec	1	31	42	42	0	0	0	18	18	0	2226
1974 Jan	1	31	61	56	0	0	5	48	47	1	2209
Feb.	1	28	[illegible]	46	0	0	4	[illegible]	[illegible]	2	[illegible]
Mar	1	31	67	62	0	0	5	100	99	1	2252
Apr.	1	30	71	66	0	0	5	60	60	0	2258
May	1	31	60	58	0	0	2	65	65	0	2208
June	1	30	64	71	0	0	5	108	107	1	2249
July	1	31	52	52	0	0	0	75	75	0	2262
Aug	1	31	31	31	0	0	0	69	69	0	2161
Sept.	1	30	42	42	0	0	0	26	26	0	2258
Oct.	1	31	464	30	0	432	2	3	3	0	2074
Nov	1	30	[illegible]	17	18	[illegible]	[illegible]	4	4	0	1658
Dec	1	31	57	1	3	53	2	2	2	0	1328

III. JOB OPENINGS for which workers from outside the firm were actively being sought as of close of last business day of month (If "NONE," enter "0"; do not leave blank)

IV. YOUR COMMENTS

Enter main factors responsible for any significant month-to-month changes in SECTIONS I, II, and III. Examples are: Slow business, Strike, Fire, Weather, Temporary summer help, Seasonal increases

Year and Month	Current job openings: Number of current job openings (13)	Number included in col. 13 (14)	Number of openings with future starting dates (15)	Do not use (16)	Comments (17)
1973 Dec					
1974 Jan.					
Feb.					
Mar					
Apr.					
May					
June					
July					
Aug					
Sept.					
Oct.					Decrease in Sales
Nov.					Decrease in Sales
Dec					

DO NOT COMPLETE PART III

Dennis J. Birkeister — Pers Mgr. — 227-3000

[illegible]

MONTHLY REPORT ON LABOR TURNOVER

U.S. DEPARTMENT OF LABOR
Bureau of Labor Statistics
and
The Manpower Administration
Washington, D.C. 20212

Return to
ILLINOIS DEPARTMENT OF LA.
BUREAU OF EMPLOYMENT SECURITY
165 North Canal Street
Chicago, Illinois 60606
Telephone: 793-4497, 4498

EXHIBIT P (cont'd.)

1975
OUR COPY

(Change name and mailing address if incorrect - include ZIP code)

01632 379-51 X 761 003022

SCHWINN BICYCLE CO-DEPS MFR
1856 N KOSTNER CHICAGO ILL 60639

The Bureau of Labor Statistics, the Manpower Administration and the State agencies cooperating in their statistical programs will hold all information furnished by the respondent in strict confidence.

LOCATION ____ (City) (County) (State)

Before entering data see explanations on other side

I. LABOR TURNOVER DURING CALENDAR MONTH — ALL EMPLOYEES; II. EMPLOYMENT

Year and month (1)	Period covered: From (2)	Through (3)	Separations: Total separations (4)	Quits (5)	Discharges (6)	Layoffs (7)	Other separations (8)	Accessions: Total accessions (9)	New hires (10)	Other accessions (11)	Employment: Total number (12)
1974 Dec.	1	31	59	1	3	13	2	2	2	0	1328
1975 Jan.	1	31	44	8	6	26	4	70	0	70	841
Feb.	1	28	26	5	8	10	3	71	3	68	1354
Mar.	1	31	29	4	6	18	1	20	3	17	1366
Apr.	1	30	32	29	1	2	0	354	3	351	1363
May	1	31	64	60	1	0	3	338	136	146	1932
June	1	30	45	41	0	6	1	103	100	3	2054
July	1	31	148	0	0	148	0	36	36	0	2049
Aug.	1	31	451	24	32	390	5	1	1	0	1721
Sept.	1	30	47	6	22	16	3	47	3	44	1505
Oct.	1	31	236	8	12	213	3	8	4	4	1495
Nov.	1	30	17	2	5	9	1	16	1	15	1317
Dec.	1	31	16	0	1	9	1	7	2	5	1322

III. YOUR COMMENTS

Enter main factors responsible for any significant month to month changes in SECTIONS I and II. Examples are: more business, strike [illegible], temporary summer help, seasonal increases, etc. (14)

Year and month	Comments
1974 Dec.	
1975 Jan.	INVENTORY
Feb.	
Mar.	
Apr.	Recall From Layoffs In Late [illegible]
May	" " " & New Hires - More Business
June	" " " " " - More Business
July	
Aug.	Decrease In Sales
Sept.	
Oct.	
Nov.	
Dec.	

Person to be addressed if questions arise regarding this report: [illegible signature] Prepared by: [illegible signature] Telephone no. 227-2000

162

BL 1219 | State | Report No. | Ind. | OMB No. 44-R1061 Approval expires Jan. 31, 19__

EXHIBIT F (cont'd.)

U.S. DEPARTMENT OF LABOR
Bureau of Labor Statistics
and
The Manpower Administration
Washington, D.C. 20212

MONTHLY REPORT ON LABOR TURNOVER

Enter the data requested and return in the enclosed envelope as soon as the information is available each month

Return to
ILLINOIS DEPARTMENT OF LABOR
Bureau of Employment Security
910 South Michigan Avenue
Chicago, Illinois 60605
Telephone: (312) 793-4497

(Change name and mailing address if incorrect - include ZIP code)

01632 379-51 X 761 003022

SCHWINN BICYCLE CO-PRES MFR
1856 N KOSTNER CHICAGO ILL 60639

1976 OVR COPI

The Bureau of Labor Statistics, the Manpower Administration, and the State agencies cooperating in their statistical programs will hold all information furnished by the respondent in strict confidence.

MIL LOA MAT LOA ... [illegible]

LOCATION [illegible] (City) (County) (State)

Before entering data see explanations on other side

I. LABOR TURNOVER DURING CALENDAR MONTH — ALL EMPLOYEES; II. EMPLOYMENT (one pay period)

YEAR AND MONTH (1)	Period covered From- (2)	Through (3)	Separations: Total separations (sum of cols. 5 thru 8) (4)	Quits (5)	Discharges (6)	Layoffs (7)	Other separations (8)	Accessions: Total accessions (sum of cols. 10-12) (9)	New hires (10)	Recalls (11)	Other accessions (12)	Total number who worked during or received pay for any part of the pay period which includes the 12th of the month (13)
1975 Dec	1	31	16	0	6	9	1	7	2	0	5	1322
1976 Jan	1	31	20	7	5	[illegible]	6	23	3	26	–	1235
Feb	1	29	22	7	8	3	4	15	3	12	–	1321
Mar	1	31	18	3	12	–	3	[illegible]	7	[illegible]	–	1385
Apr	1	30	[illegible]	9	[illegible]	–	3	251	133	118	–	1696
May	1	31	191	30	76	82	3	134	134	–	–	1838
June	1	30	322	17	21	282	2	9	6	3	–	1579
July	1	31	16	12	4	–	–	11	2	9	–	1410
Aug												
Sept												
Oct.												
Nov												
Dec												

III. YOUR COMMENTS

Enter main factors responsible for any significant month-to-month changes in SECTIONS I and II. Examples are: more business, strike, fire, weather, temporary summer help, seasonal increases, etc.

YEAR AND MONTH	(14)
1975 Dec	
1976 Jan	
Feb	
Mar	
Apr	
May	
June	
July	
Aug	
Sept	* [illegible]
Oct	" " " " 43 " " " "
Nov	" " " " 38 " " " " "
Dec	

Person to be addressed if questions arise regarding this report: Dennis J [illegible]

Position: Personnel [illegible]

Telephone no.: 275-2966 ~~227-3000~~

INSTRUCTIONS FOR COMPLETING THIS FORM

EXHIBIT F (cont'd.)

I. LABOR TURNOVER

PERIOD COVERED - Information on labor turnover, columns 4 through 12, is requested for the most recent *entire calendar month* specified in column 1, or, if this is not possible, for a period which most closely covers that calendar month. In either case, enter in columns 2 and 3 the beginning and ending dates for the monthly period for which turnover data are reported.

SEPARATIONS (ALL EMPLOYEES)

Column 4 TOTAL SEPARATIONS - Enter the sum of columns 5 through 8.

Column 5 QUITS - A quit is a termination of employment *initiated by the employee* for any reason except to retire, to transfer to another establishment of the same firm, or for service in the Armed Forces. Include a person who fails to report after being hired (if previously counted as an accession) and an unauthorized absence if on the last day of the month the person has been absent more than 7 consecutive calendar days.

Column 6 DISCHARGE - A discharge is a termination of employment *initiated by the employer* for such reasons as incompetence, violation of rules, dishonesty, laziness, absenteeism, insubordination, failure to pass probationary period, etc. Inability to meet organization's physical standards should be reported in other separations, column 8.

Column 7 LAYOFFS - A layoff is a suspension from pay status (lasting or expected to last more than 7 consecutive calendar days without pay) initiated by the employer *without prejudice to the worker* for such reasons as lack of orders, model changeover, termination of seasonal or temporary employment, inventory taking, introduction of labor saving devices, plant breakdown, shortage of materials, etc. *Include temporarily furloughed employees and employees placed on unpaid vacations.*

Column 8 OTHER SEPARATIONS - Include only terminations of employment for military duty lasting or expected to last more than 30 calendar days, retirement, death, permanent disability, failure to meet required physical standards, and transfers of employees to another establishment of the company. NOTE - If you include any other types of separations in this column, mention the number and type under Comments. Employees involved in labor-management disputes should not be counted as separations.

ACCESSIONS (ALL EMPLOYEES)

Column 9 TOTAL ACCESSIONS - An accession is any permanent or temporary addition to the employment roll whether of new or former employees, or transfers from another establishment of the company. Enter in column 9 the sum of columns 10 thru 12. Employees involved in labor-management disputes should not be counted as accessions when they return to work.

Column 10 NEW HIRES - New hires are temporary and permanent additions to the employment roll of (1) persons who have never before been employed in this establishment, or (2) former employees you did not call back. Persons transferred from other establishments of the company should be reported in "other accessions."

Column 11 RECALLS - Recalls are permanent or temporary additions to the employment roll of persons specifically recalled to a job in the same establishment of the company following a period of layoff lasting more than seven consecutive days. Employees called from a layoff in a different establishment of the company are to be classified as a transfer and reported in column 12 - OTHER ACCESSIONS.

Column 12 OTHER ACCESSIONS - Include all additions to the employment roll other than new hires and recalls. This includes transfers from other establishments of the company, and former employees returning from military leave or other absences without pay who have been counted as separations. Employees involved in labor-management disputes should not be counted as accessions when they return to work.

II. EMPLOYMENT

PERIOD COVERED - Employment information, column 13 is requested for one pay period (preferably one week) which includes the 12th of the calendar month for which labor turnover data are reported.

Column 13 TOTAL NUMBER - Enter the total number of persons on the payrolls of the establishment(s) covered in this report who worked full- or part time or received pay for any part of the pay period (preferably one week).

Include salaried officers of corporations, executives and their staffs and employees engaged on force account construction but exclude proprietors, members of unincorporated firms, and unpaid family workers. Include persons on vacations and sick leave if they received pay directly from your firm for the pay period covered.

Exclude persons on leave without company pay the entire period and pensioners and members of the Armed Forces carried on the rolls but not working during the pay period covered.

III. COMMENTS

Column 15 YOUR COMMENTS - Enter the main factors responsible for significant month-to-month changes in Labor Turnover (columns 4 through 12) and Employment (column 13).

GPO 895-030

August 20, 1976

Mr. Michael Stern, Staff Director
Committee on Finance
2227 Dirksen Senate Office Building
Washington, D.C. 20510

STATEMENT ON BEHALF OF THE
LYNN A. WILLIAMS ENGINEERING COMPANY
IN REFERENCE TO HOUSE BILL HR 12254

Mr. Chairman & Members of the Committee:

My name is Lynn A. Williams and I request that brakes and other bicycle components be deleted from the referred to duty suspension bill.

There are facilities for the domestic manufacture of bicycle brakes.

There are facilities for the domestic manufacture of bicycle derailleurs.

Sears, Roebuck & Company is now marketing a bicycle with the domestic-made William's hydraulic brake and with a domestic-made derailleur.

Bicycle components should be made in the U.S.A. in order to provide additional jobs.

In 1971, the Lynn A. Williams Engineering Company began the development in the USA of a bicycle caliper brake system. Without any large financial backing we spent two years in the development of a hydraulic caliper brake which is competitive in cost and, we believe, safer in operation that the conventional caliper brakes imported mostly from the Orient (and also from Switzerland and Germany).

The development was carried out in such a way as to yield good and safe performance and, equally important, to utilize the American manufacturing technology which is the most advanced for mass production at low cost. Unlike the imported brakes made by a rather unusual slush forging process not well advancedin this country, our brakes were designed to use metal stamping for the load bearing parts and plastic injection molded parts for the others. These are among the two most advanced manufacturing processes in America. Highly automatic and not dependent on low labor cost, they can and do compete successfully with manufacturing anywhere in the world.

Page Two
August 20, 1976

Moreover there is abundant available capacity for the production of pressed metal parts and the plastic molded shells and covers.

One (and only one) large U.S. firm, Sears, Roebuck & Company, showed an immediate interest in our brake, this based upon a preliminary riding test in January 1974.

Thereupon, a long test program by the Sears laboratories ensued: stopping tests, road tests, endurance or life tests, corrosion tests, etc.

Then, at Sear's request, the handlebar actuator was redesigned for better style.

By June of that year, Sears placed an order conditioned upon compliance with (then inchoate) federal safety standards and upon additional tests to be performed by Sear's bicycle supplier, The Murray Ohio Manufacturing Co. Those tests ran through the fall of 1974, through the winter and into the spring of 1975.

The brakes have now been installed upon thousands of Sears bicycles, thousands have gone into service. Thus far there have been very few service complaints. A copy of an ad from the Chicago Daily News dated August 19, 1976, is attached. Note the reference to hydraulic brakes. These are the brakes we manufactured. The dies, molds and tools for parts have been fabricated for a production rate (single shift) of one million brakes per year. To increase the capacity requires only additional shifts or additional duplicate dies and tools.

When we embarked upon this venture we were told by prospective buyers that upon establishing U.S. manufacturing facilities, the basis for the tariff exemption under the Fulton Act would no longer exist. This was an important encouragement to our development and our entry into this business.

But now we read in the testimony that there is no U.S. manufacturer of caliper brakes.

Mr. Shannon for the Bicycle Manufacturers Association of America testified for ". . . continued suspension of duty on bicycle parts such as brakes, hubs and sprockets which are not presently manufactured domestically and on derailleurs which is (sic) manufactured by one sole source in limited quantities".

In addition to our domestic manufacture of brakes, there is a new factory for brakes established by a Japanese firm in North Carolina selling a well-known and widely used Oriental style caliper brake under the trade name Dia-Compe. Pennsylvania Wire Rope Company has the design, capital equipment and plant space to manufacture bicycle caliper brakes.

Obviously, U.S. component makers manufacture no more than they can sell. But a bicycle brake is not a big item. If properly designed for high production the productive capacity can be expanded to meet the demand all within normal lead times.

Page Three
August 20, 1976

Sears also markets an American made derailleur of an improved type. The firm which makes this derailleur is a part of a four billion dollar company, Beatrice Foods. Like our brake, the derailleur is not a large item. Manufacturing capacity can be made available as rapidly as demand calls for.

The same paragraph by Mr. Shannon which flatly asserts that brakes are not made in the U.S.A. is careless about the duty charged on complete bicycles. It speaks of ". . . completed bicycles assembled from these very same parts, at duty rates of 5.5 per cent". This is partly true. Some larger lightweight bicycles carry a duty of 5.5 per cent. But omitted is the fact that smaller bicycles carry a duty of 11 per cent.

There is no reason why bicycle components should not be made in the U.S.A. so as to provide additional jobs. Estimates vary as to the share of bicycle cost represented by components. This varies with the model and type of bicycle and with the manufacturing. Some make relatively more of their own parts and components than others. A very conservative estimate is that 30% of bicycle cost is in purchased components. For some manufacturers and some models this will range up to 60%. By bringing this part of the work back into the U.S.A. it would be possible to provide more than half again as much work in the U.S.A. as now goes into bicycle manufacturing.

We believe that there is a compelling basis for removing from the bill the exemption for caliper brakes and derailleurs. Alternatively there will be a basis for reducing the term of extension from three years to one year.

If we are right in the facts, and we know we are, the very basis for the exemption, the asserted lack of manufacturing in this country, fails.

We have spent long years and a good deal of money to become manufacturers of bicycle brakes. We were startled to discover legislation enroute to passage based upon the assertion that we did not exist.

Respectfully,

Lynn A. Williams


CHICAGO DAILY NEWS
89.99
24-in. 10-speed
79.99
26-in. 10-speed
79.99
Save $20 10-speed
with hydraulic brakes
Regularly $140
119.99
Sears new hydraulic brake bike has no brake cables to adjust. Gives smooth, steady stops. Flat black frame has chrome-plated front fork tips. Easy-to-reach stem mounted shifters. Men's model.
Bikes at Sears low take-with prices
Complete expert assembly and service available at additional cost.
Sale prices thru August 21
In the CITY
SOUTH/EAST
Sears
Celebrating Our 90th Anniversary Year

SUMMARY OF STATEMENT

OF

AMERICAN CEMETERY ASSOCIATION
NATIONAL ASSOCIATION OF CEMETERIES
SOUTHERN CEMETERY ASSOCIATION
WESTERN CEMETERY ALLIANCE

IN SUPPORT OF

H.R. 1142

This bill amends the Revenue Act of 1954 to provide for a distribution deduction for perpetual care funds created pursuant to local law by a taxable cemetery in order to provide for care and maintenance of cemetery property in which interment rights have been sold to and have been held by the public. It provides a special deduction in computing the income of such a fund for amounts actually expended by the fund but only in the amount actually distributed during the year for such care and maintenance and in any case not more than $5.00 per grave site.

Under existing Internal Revenue practice these irrevocable trusts could be denied deductions for amounts distributed in carrying out the purposes for which they were created by local law.

We are urging the Congress to rectify the problem. The bill has been thoroughly reviewed by the Service and by the Treasury and, in deed, is in the exact form and language requested by the Treasury. It was unanimously reported favorably by the Committee on Ways and Means.

We know of no opposition to the bill.

Respectfully,

R. L. McNitt, Jr.

STATEMENT OF

AMERICAN CEMETERY ASSOCIATION
NATIONAL ASSOCIATION OF CEMETERIES
SOUTHERN CEMETERY ASSOCIATION
WESTERN CEMETERY ALLIANCE

SUPPORTING H.R. 1142

SUBMITTED TO THE
COMMITTEE ON FINANCE
UNITED STATES SENATE

94TH CONGRESS
2ND SESSION

August 24, 1976

MR. CHAIRMAN AND MEMBERS OF THE COMMITTEE:

My name is R. L. McNitt, Jr. As a past president of the National Association of Cemeteries, I am filing this statement on behalf of the American Cemetery Association, the National Association of Cemeteries, the Southern Cemetery Association, and the Western Cemetery Alliance. The membership of these associations include municipal, fraternal, religious, community non-profit, and private cemeteries situated throughout the United States. These organizations have asked me to present for your consideration the federal tax problems confronting state-created perpetual care funds, which funds are used solely for the care, maintenance and upkeep of cemeteries.

Forty-three states have laws which require cemetery companies to place a portion of the sale price of every grave space in an irrevocable trust. (See Exhibit "A" attached.) The income of the trust can be used only for the upkeep of the cemetery. The remaining states recognize the problem but treat it differently. For example, Massachusetts, Connecticut and Rhode Island prohibit profit-oriented entities from cemetery operation, thereby channeling all profits toward cemetery upkeep. Such states provide for the creation of irrevocable trust funds.

The sole legislative purpose of these statutes is to assure that dedicated resources will be available in perpetuity for the care, maintenance and upkeep of the cemeteries within the state, thus relieving the states and municipalities of this burden. The funding provisions in the state perpetual care statutes represent legislative determinations of the methods and levels of funding required for the perpetual care funds to fulfill their purpose.

From 1921 until the mid-1950's, the Internal Revenue Service treated Section 501(c)(13) of the Internal Revenue Code of 1954 and its predecessor sections as providing a total exemption from federal income taxation for cemetery perpetual care funds. Tax exemption letters were freely granted upon application. Beginning in the mid 1950's, although there had been no change in the law, the Internal Revenue Service revised its position and revoked existing tax exemption letters. The Service then established a distinction between perpetual care funds associated with cemeteries operated by non-profit organizations and those associated with cemeteries operated by taxable cemeteries and to hold the latter perpetual care funds, but not the former, taxable on their income. The statutes requiring such funds make no distinctions based upon the identity of the cemetery company as a non-profit organization or a profit-seeking entity.

Implicit in these state legislative determinations was the assumption based upon the then existing administrative position of the Internal Revenue Service that the income of perpetual care funds would not be taxed. Thus, the Internal Revenue Service's change in its administrative position is frustrating the original state legislative purpose.

After the Internal Revenue Service's change of position on exemption, rulings were sought from the Internal Revenue Service that perpetual care funds were taxable as trusts and that amounts distributed by such trusts in fulfillment of their purposes were allowable deductions in computing taxable income pursuant to the provisions of Subchapter "J" of the Internal Revenue Code. In 1965 the Internal Revenue Service ruled that perpetual care funds were taxable as trusts but that no deductions were allowable under Subchapter "J" because there were no ascertainable trust beneficiaries.

As a result of the changed attitude of the Internal Revenue Service, many Members of Congress have, in the past, introduced several bills to amend the Internal Revenue Code in an attempt to alleviate the tax burden placed on perpetual care funds by the changed position of the Internal Revenue Service.

The Ways and Means Committee of the House of Representatives recognized the vital interest of every state and community in the continued care, maintenance and upkeep of cemeteries. In the last analysis the state must bear the burden of such upkeep when other sources fail. Many cities, towns, counties, cemetery districts and similar municipal authorities have had to take over and maintain abandoned, unkept and ugly properties by taxing the community for the purpose now served by these perpetual care funds. As indicated earlier, almost every state in the Union has enacted legislation requiring the creation of a perpetual care trust to assume the ultimate burden of maintenance and upkeep. These funds have for their sole purpose the prevention of cemeteries from becoming a public nuisance. The investments of these funds and the expenditure of these funds is carefully regulated and their financial statements are examined regularly and with the same careful scrutiny that one associates with a bank examiner.

As indicated earlier, generally, these funds take the form of trusts, and as trust funds can be used only for one purpose. The economic plight of the perpetual care fund is very real and can only be remedied by a decision of the Congress to clarify that, in fact, these funds serve a public function and rule that such funds when organized and operated under the circumstances have the right to compute taxable income by taking a deduction from gross income for what is paid out in furtherance of a state function.

We know of no opposition to the bill.

Respectfully submitted,

R. L. McNitt, Jr.

EXHIBIT "A"

The following States have statutes which require cemeteries to create a perpetual care fund by placing the listed percentage of the purchase price of grave spaces in an irrevocable trust.

STATES	PERCENTAGE
Alabama	15%
Alaska	Voluntary
Arizona	50¢ per sq. foot
Arkansas	10%
California	$1.00 per sq. foot
Colorado	15%
Connecticut	No profit cemeteries
Delaware	$25,000 on establishing cemetery
D. C.	Voluntary
Florida	10%
Georgia	10%
Hawaii	$1.00 per sq. foot
Idaho	10%
Illinois	20¢ per sq. ft. or 15%
Indiana	40¢ per sq. ft. or 15%
Iowa	20%
Kansas	15%
Kentucky	20%
Louisiana	10%
Maine	30%
Maryland	35¢ per sq. ft. or 10%

EXHIBIT "A"

STATES	PERCENTAGE
Massachusetts	No profit cemeteries
Michigan	15%
Minnesota	20%
Mississippi	40¢ per sq. ft. or 15%
Missouri	10%
Montana	15%
Nebraska	50¢ per sq. ft.
Nevada	$1.00 per sq. ft.
New Hampshire	
New Jersey	15% plus % of memorial and interment
New Mexico	25%
New York	25%
North Carolina	At least $15 per grave
North Dakota	20%
Ohio	10%
Oklahoma	10%
Oregon	15%
Pennsylvania	40¢ per sq. ft. or 15%
Rhode Island	No profit cemeteries
South Carolina	10%
South Dakota	20%
Tennessee	50¢ per sq. ft. or 20%
Texas	50¢ per sq. ft.
Utah	50% per sq. ft.

STATES	PERCENTAGE
Vermont	20%
Virginia	10%
Washington	10%
West Virginia	10%
Wisconsin	No profit cemeteries
Wyoming	90¢ per sq. ft.

NATIONAL TIRE DEALERS and RETREADERS Association, Inc.

1343 L Street, N.W., Washington, D.C. 20005 • Area Code (202) 638-6650

Statement of National Tire Dealers &
Retreaders Association on H.R. 2474
for the Senate Finance Committee, August 24, 1976

The National Tire Dealers and Retreaders Association represents independent tire dealers and retreaders, small businessmen in all fifty states. Our membership numbers 4,000, who have a total of some 10,000 retail outlets. We urgently need the passage of H.R. 2474.

This legislation deals with the several instances under current law where a manufacturers' excise tax is imposed on tread rubber, when in a similiar situation the manufacturers' excise tax is not imposed (or a credit or refund of the tax is allowed) for the tax on new tires.

The summary of H.R. 2474 (House report 94-1334) states:
H.R. 2474 provides for credits or refunds of the manufacturers' excise tax on tread rubber where tax-paid tread rubber (1) is wasted in the recapping or retreading process, (2) is used in the recapping or retreading of tires the sale of which is later adjusted under a guarantee or warranty, or (3) is used in the recapping or retreading of tires which are exported, are sold to State or local governments, are sold to nonprofit educational institutions, or are sold as supplies for vessels or aircraft. In addition, the bill imposes a tax on tread rubber used in recapping or retreading tires abroad, if those tires

are then imported in the United States.

"The bill also clarifies the treatment of credits or refunds for the manufacturers' excise tax on new tires where sales are later adjusted as the result of a warranty or guarantee. The bill also modifies the statute of limitations so that a credit or refund of the tread rubber or new tire tax can be obtained for a period of one year after the warranty or guarantee adjustment is made."

This Association has long sought the passage of legislation which would correct inequities we believe have been inadvertently imposed on retreaders by the Highway Revenue Act. In the past similiar legislation to provide the relief from these inequities on the Tread Rubber Tax have passed the House and the Senate. Unfortunately, an unrelated last minute amendment on the Senate side prevented the final legislation from being adopted.

The inequities according to the Internal Revenue Service in the treatment of tread rubber have been caused by the fact that the tax of 5¢ a pound is on the raw material rather than on the finished product, as it is in the case of new tires. The Internal Revenue Service states that there is nothing they can do to solve the problem without a change in the law. The Internal Revenue Service has ruled on numerous occasions that losses due to waste in the retreading process could not be designated for refunds. In the case of new tires, if a new tire is lost in production, the new tire is not subject to the Highway Excise Tax. However, if something happens to the tread rubber during processing (i.e. some of the rubber not used or something occurs to the tire during the retreading process), there is no method for recovering this loss. The tax liability on tread rubber is already created and no refund or credit is permitted.

Also in the case of tread rubber used in the retreading of tires, the sale of which is later adjusted under a guarantee or warranty, there is no method for securing a credit or refund on the tax. The consumer gets his tax back on a pro-rated basis but the retreader gets no refund on this tax. In the case of new tires, a tire returned for adjustment results in a refund being given to the consumer, the dealer, and the manufacturer. The inequity for the retreader is clear.

Third, when a retreaded tire is sold to State and local governments, there is no method of getting a credit or refund. If a new tire is sold to a local or State government, there is an exemption available. Since tread rubber is a raw material, and the taxed item, the Internal Revenue Service says that the finished retreaded tire is neither taxable or exempt. Therefore, the retreader pays the manufacturer the excise tax on tread rubber but can not recover it from the State government nor can he get an exemption such as in the case of the new tire.

In the case of the independent retreader, there have been a significant number of cases where the Internal Revenue Service has come in where the retreader unfortunately has not been paying tax on rubber which has been wasted, or has taken a reduction on the tax on returned adjusted retreaded tires, or has made some adjustment on his records for a tax credit relative to tires sold to a state. In every case, the Internal Revenue Service has disallowed this, and the retreader has found himself in a financial bind.

We have retreaders who have had a tax liability as much as $25,000.

This legislation would correct all of these inquities. The inequities occurred because of the language of the original law, and there never was an intent by Congress to penalize the retreader as far as this tax was concerned.

In addition, the Treasury Department suggested that smooth casings shipped out of this country to such places as Mexico or Canada, which are in turn retreaded and shipped back to this country should be required to have a tax the same as retreads made in the United States. This Association supports this suggested change as equitable, and feels that no one should be allowed to use this as a tax advantage in a competitive situation. Therefore, we support the Treasury's proposal in this regard.

The problems relative to the tread rubber tax have been going on for a number of years, and have caused great difficulty for these small business people. Hopefully, the Senate will understand this plight, and will finally move with the House of Representatives to correct these inequities.

Submitted by Philip P. Friedlander, Jr., General Manager, National Tire Dealers & Retreaders Association.

RMA

RUBBER MANUFACTURERS ASSOCIATION

1901 PENNSYLVANIA AVE., N.W. • WASHINGTON, D.C. 20006 • (202) 785-2602

STATEMENT OF

Edward E. Wright, Vice President
Rubber Manufacturers Association

On H.R. 2474

For Presentation to the
Senate Committee on Finance

Hearing on Various Revenue and Tariff Bills

August 24, 1976

I am Edward E. Wright, Vice President for Government Relations and Economic Affairs of the Rubber Manufacturers Association. This statement is submitted on behalf of all U.S. tire manufacturing companies.

H.R. 2474 is a bill with two distinct parts. One part, sections (a), (b) and (c) of the bill as introduced, deals with the federal excise tax on tread rubber and retreaded tires. The second part, section (d) as introduced, deals with the federal excise tax on tires when a tire fails and is returned by a consumer for adjustment pursuant to a warranty or guarantee.

With respect to tread rubber and retreaded tires, H.R. 2474 would provide manufacturers of retreaded tires the same tax treatment that is accorded to manufacturers of new tires, and thus would eliminate a tax bias against retreaded tires under present law. Our companies strongly support enactment of these provisions to correct the unjustifed discrimination that exists under present law. The House Ways & Means Committee has made some minor changes in the text of the bill as originally introduced, suggested by Treasury, and we concur in these changes.

With respect to excise tax adjustments in tire warranty situations, the basic intent of the bill is to provide a clear statutory basis for handling excise tax adjustments. At the present time no statutory language clearly governs this technical area. A basic excise tax principle, however, is that where a product fails to give normal use and a warranty adjustment is made, then the purchaser is also entitled to a proportionate excise tax adjustment. This has been the practice ever since the federal tire excise tax was first instituted. Thus, the purposes of H.R. 2474 as introduced were:

1. to assure continued uniform excise tax treatment of ultimate consumers receiving warranty adjustments on tires, irrespective of numerous variations that exist in manufacturers' marketing arrangements;
2. to codify the longstanding administrative and marketing practice (40 years duration) of granting the ultimate consumer an excise tax credit based on the simple and practical method of determining the undelivered service remaining in a tire which fails to deliver full service and is adjusted under a warranty; and
3. to prevent serious administrative problems which would be caused in the trade by requiring a shift to ad valorem tax concepts. Such a shift would be inappropriate moreover since the tire tax is not an ad valorem tax but is based on weight.

The original intent of the bill would not be served by certain changes in the text of section (d) of the bill made by the House Ways & Means Committee. These changes, inadvertent we believe, would cause serious and expensive administrative problems for our companies by introducing novel ad valorem concepts into warranty adjustments on tires, and would result in unequal treatment of consumers. This outcome would of course defeat our original purpose in urging enactment of section (d) of the bill. But adoption of some brief amendatory language by this Committee, which we are preparing in consultation with the Committee's staff, will restore the original purpose of the bill. This language will be presented to the Committee before mark-up and we are strongly hopeful of its adoption.

I would like to emphasize that section (d) of H.R. 2474, as introduced, and the requested change we will be making in the House version, do not present issues that involve any actual or potential loss in federal revenues. Section (d) basically is without revenue impact.[1/] Basically section (d) raises a technical question of tax administration. We believe our desire to have 40 years of industry and IRS practice recognized as sound, and allowed to continue, is based on eminently practical considerations, is fully reasonable, and best serves the interests of consumers.

Since its inception the excise tax on tires has been separately stated in each sale and paid by the ultimate consumer. Details of actual tire warranty adjustment procedures vary from manufacturer to manufacturer, with the nature of the retail outlet, and can be quite complex. Standard practice is uniform, however, in that the percentage of adjustment on a failed tire given to the ultimate consumer both as to the tire and the excise tax perviously paid has long been based on a performance measurement of the failed tire. In other words, if the tire is deemed to have given only 40% of the service warrantied, then the consumer would be allowed 60% off the price of a replacement tire, and also 60% off the federal excise tax on the replacement tire. Since the tire tax is based on weight, it is uniform as to tires of the same type, size, grade, and classification regardless of the sales price charged. This simple adjustment procedure

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1/ Total excise tax adjustments on tires in 1975 pursuant to warranties were $14 million or less. No increase or reduction in this amount is at stake, only whether internal business costs to manufacturers, dealers, etc., may be increased.

produces an excise tax credit which is correct to within a few pennies in all cases and in the aggregate produces a perfect adjustment figure. For more than 40 years, wherever the manufacturer's warranty has run to the ultimate consumer, variations in the chain of arrangements with dealers have not distorted the excise tax adjustment to the ultimate consumer, because the excise tax adjustment has been consistent with the practical result at the consumer level. The accompanying administrative procedures have been a convenience to consumers, stores and manufacturers, and have cause no significant tax gain or loss to anyone in the manufacturing-marketing chain.

Serious administrative problems would be caused on the other hand by an application of ad valorem tax concepts to the weight-based excise tax on tires. Under an ad valorem tax approach the price of the original article is critical because the tax by definition is based on value. Since tires are sold and driven all over the United States, they are rarely adjusted at the place where sold and original price information will simply not be available in most cases, either to the consumer or to the dealer where the tire is presented. This fact alone makes an ad valorem approach unworkable for our industry, and would make requesting original price documentation an annoyance to consumers. The more complicated paperwork involved would add to our industry's administrative costs in collecting the excise tax on tires — costs which are already heavy — with no advantages accruing to the federal government, or anyone else.

H.R. 2474, properly worded, would codify existing procedures so as to permit a correct and uniform tax adjustment for the benefit of consumers,without detriment to other parties in the tax collection process. By continuing the basic procedures used for more than 40 years, the bill would maintain continuity and avoid disruption and unnecessary costs to the tire industry.

In conclusion, our companies are keenly desirous of accomplishing the original purpose of section (d) of H.R. 2474, and we strongly hope that the Senate Committee on Finance will agree that our requested changes in the House bill are desirable.

STATEMENT OF SENATOR WILLIAM D. HATHAWAY ON BEHALF OF S. 1904, FINANCE COMMITTEE, AUGUST 24, 1976

Mr. Chairman, I very much appreciate this opportunity to testify on behalf of S. 1904, my bill designed to institute some measure of control over an abused loophole in the tariff schedules covering certain wool fabrics imported into the United States by way of one of our insular possessions.

Under present law, a substantial tariff is levied upon imported woven wool fabrics. However, such textiles which have been manufactured abroad and which have then received a simple "shower-proofing" treatment in the Virgin Islands are allowed to enter the United States duty free.

In particular, a heavy wool fabric, made in Romania and Italy, enters the United States by means of this procedure and escapes all duty. This results in an unfair competitive advantage to foreign manufacturers over American makers of this fabric.

Over the past few years, domestic consumption of wool textiles has suffered a dramatic decrease and both American production and Virgin Islands exports are well below their former amounts.

The harm in the present situation is that the mainland textile industry is threatened without corresponding benefit to the Virgin Islands. The "shower-proofing" process is accomplished with very few workers but its product competes with similar domestically produced textiles which represent the labor of thousands of workers in the United States.

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To allow this situation to continue unchanged means that we shall jeopardize further or eliminate those American jobs. And because that will not benefit the Virgin Islands in anywhere near equal measure, the only beneficiaries will be Italy and Romania who, if they were exploring these textiles directly to the United States, would be paying a heavy tariff.

But I do not wish to see the Virgin Islands suffer and that is why I do not in my bill propose applying normal duties on Virgin Islands textiles. Instead, S. 1904 sets a quota on such imports which are not arduous and which will give our shrinking textile industry the capacity to compete fairly with imports.

The bill has the support of the Administration and is endorsed as well by all relevant trade associations.

For the record, Mr. Chairman, I offer a copy of the letter of February 18, 1976 from the Treasury Department; a statement in support of H.R. 8124, a corresponding House measure; and a letter from the Northern Textile Association dated March 10, 1976, all of which are in support of S. 1904 and elaborate upon my brief remarks today.

NORTHERN TEXTILE ASSOCIATION

211 Congress Street, Boston, Massachusetts 02110 (617) 542-8220

March 10, 1976

The Honorable William J. Green, Chairman
Subcommittee on Trade
Committee on Ways and Means
1102 Longworth House Office Building
Washington, DC 20515

Dear Chairman:

Re: H.R. 8124

This is to further support my testimony of February 20, 1976 before your Committee in favor of H.R. 8124 and in response to the statements of the Delegate from the Virgin Islands, Honorable Ron deLugo and others on March 2 in opposition to the Bill.

As the Virgin Islands witnesses pointed out, there is now only one company in the Virgin Islands which processes imported wool fabrics. Even at the peak of activity in the Virgin Islands in 1973 when five companies were in operation, not more than 80 to 100 persons were employed on a part-time or seasonal basis. The witnesses asserted that the processing activities in the Virgin Islands has not resulted in the loss of jobs by textile workers on the mainland. This is not true.

A modern, efficient mainland mill will employ about 525 textile persons to manufacture the 3.5 million linear yards of the heavy weight woolens equal to the quota. In addition to the 525 textile jobs lost, there is an equal number of jobs in supporting industries such as chemicals, transportation, fuel and fibers.

A quota of 3.5 million linear yards of fabrics imported from Romania and Italy via the Virgin Islands costs the mainland industry and labor over 1,050 jobs. The benefit to the Virgin Islands is, at most, only 80 to 100 seasonal jobs. This is an expensive exchange. It benefits the foreign producers substantially; the Virgin Islands only marginally; and costs the United States (mainland and Islands) close to a thousand jobs.

Substantial tariffs were imposed by the United States on these fabrics in 1960 for which Italy and other exporters were paid compensation. Hence, these fabrics are not imported directly from such countries. The Virgin Islands shower proofing and processing is just another loophole to evade this tariff. Unemployment in mainland mills is increased thereby.

We are not proposing, however, the elimination of all processing of wool fabrics in the Virgin Islands. We propose a reduction to reflect the changed market for such products.

All the witnesses agree that there has been a drastic decline in the consumption of wool textiles in the United States. The quota should be reduced to reflect this. The decline in the market for wool textiles in the United States is a result of a long-term trend. While this has been going on, the Virgin Islands quota has actually been increasing. The quota was 2.5 million yards a few years ago. Although this was too high, our protests to the Virgin Islands Government and to the Governor, as well as our personal visits and pleas, were not only ignored but were not even acknowledged. Instead the quota was unilaterally and peremptorily increased by 40% to 3.5 million yards.

In 1975, Virgin Islands processors were not even able to fill the quota. Now is a propitious time to adopt this legislation as it will not involve a rollback in the level of imports of these foreign fabrics via the Virgin Islands.

The Virgin Islands witnesses suggested that the reduction of the quota to a half million yards at one time is excessive. H.R. 8124, which was filed last year, proposed reductions in two steps, namely, one million yards in 1975 and 500,000 yards in 1976. We would be willing to accept an amendment to the bill to make the quota for 1976 one million yards with a reduction to 500,000 yards in 1977 and thereafter.

The witnesses attempt to isolate Northern Textile Association as the only organization opposed to the high level of the quota and the only supporters of the Bill. It should be noted that the H.R. 8124 is supported by the American Textile Manufacturers Institute, the National Association of Wool Growers, as well as United States Government Agencies.

Consideration by you and members of the Subcommittee is appreciated, and we urge that the Bill be reported favorable.

Very truly yours,

R. Reed Grimwade, Treasurer
Charlton Woolen Company

William F. Sullivan, President
Northern Textile Association

Statement of R. Reed Grimwade, Treasurer
Charlton Woolen Mills
Charlton City, Massachusetts

Before the Subcommittee on Trade,
House Ways and Means Committee,
February 20, 1976, on H.R. 8124

Mr. Chairman, my name is R. Reed Grimwade. I am testifying on behalf of the Northern Textile Association, 211 Congress Street, Boston, Massachusetts 02110, of which I am a Director. The Association represents textile manufacturers which use all the principal fibers, including wool manufacturers. NTA's member firms are located primarily in the Northeast.

I am the principal officer, namely Treasurer, of the Charlton Woolen Company of Charlton City, Massachusetts. I am accompanied by Mr. Jack Crowder who is general counsel of the American Textile Manufacturers Institute.

I appreciate this opportunity to testify on H.R. 8124, the Bill now before this subcommittee. My statement on behalf of the Northern Textile Association is also supported by the American Textile Manufacturers Institute, the largest trade association in the textile industry, which is headquartered in Charlotte, North Carolina, and by the National Wool Growers Association of Salt Lake City, Utah. These three organizations together represent virtually the entire wool and textile industries in the United States.

We support H.R. 8124 which would reduce, but not eliminate, the quantity of woolen fabrics which are processed in the Virgin Islands and then re-exported to the U.S. on a duty free basis. Most of these imports are heavy weight woolen fabrics which compete with fabrics manufactured chiefly in the states of Massachusetts and Maine by firms which employ several thousand workers.

These imported fabrics are manufactured principally in Italy and Romania, sent to the Virgin Islands for a "shower proofing" process, and then re-exported to the U.S. duty free. If these woolen fabrics were imported directly from Italy or other countries where they are made, they would be subject to the standard rate of duty for similar woven fabrics of wool valued at not over $2 per pound -- namely, a tariff of $1.135 per pound.

The shower proofing process in the Virgin Islands is a simple and inexpensive operation requiring a small number of workers. It does not change the appearance or end use of the fabrics and has a minimal effect upon their value and utility. In fact, most U.S. textile mills sell shower proofed fabrics at no additional cost to the consumer.

When the shower proofed cloth is shipped to this country from the Virgin Islands, it is asserted that the foreign materials do not constitute more than 50 percent of the total value. The declared value for customs purposes is placed at twice the value of the cloth when it entered the Virgin Islands. This enables the goods to qualify for duty free treatment. Attachment A shows the U.S. Tariff Schedule provisions for tariff treatment of products of insular possessions.

Some time ago, the Virgin Islands government was persuaded that it should limit the quantity of fabrics undergoing the shower proofing process. In 1964, the Virgin Islands imposed a quota limitation of 2.8 million linear yards. The U.S. domestic industry in 1964 produced 247 million linear yards of wool fabrics. By 1974, the quota had risen to 3.5 million linear yards and U.S. production had dropped to 72.7 million linear yards. Based on the production rate during the first nine months of 1975, domestic production for calendar year 1975 will be even lower – about 68.1 million linear yards.

Nearly all the shower proofed fabrics from the Virgin Islands are heavy weight woolen fabrics which disrupt the market for similar fabrics in this country. The general decline of wool consumption, coupled with the impact of the recent national recession upon the industry, have made the situation even more critical.

As you will note in Attachment B, conditions in the U.S. market have deteriorated to the point where the Virgin Islands has been unable to sell the quota amounts. Although complete figures for 1975 are not yet available, imports are not expected to exceed one million linear yards.

Mr. Chairman, we believe that this is an appropriate time to reduce the quotas. Since the level of imports has declined, such a reduction in the quota would not require a rollback. Further, it would insure that a potential business recovery is not thwarted by a flood of imported goods of this type.

The value of this trade to the Virgin Islands is minimal since only a few workers are employed on a part-time basis in the shower proofing activity. The damage to U.S. mills which spin, weave and finish the cloth while providing several thousand jobs is disproportionate to any possible value to the Virgin Islands.

In closing, I would like to reemphasize that since these imported fabrics enter the U.S. duty free, a quota remains the only method by which their entry may be limited. Further, there is no compelling reason why the Virgin Islands should be exempted from both tariffs and quotas.

Mr. Chairman, the wool and textile industries of the United States believe that the serious market conditions which have developed in recent years require that the quota on these duty free imports be reduced. We urge this subcommittee to act favorably on H.R. 8124.

We will be pleased to answer any questions you may have.

Thank you.

ATTACHMENT A

TARIFF SCHEDULES OF THE UNITED STATES ANNOTATED (1978)

GENERAL HEADNOTES AND RULES OF INTERPRETATION

1. Tariff Treatment of Imported Articles. All articles imported into the customs territory of the United States from outside thereof are subject to duty or exempt therefrom as prescribed in general headnote 3.

2. Customs Territory of the United States. The term "customs territory of the United States", as used in the schedules, includes only the States, the District of Columbia, and Puerto Rico.

3. Rates of Duty. The rates of duty in the "Rates of Duty" columns numbered 1 and 2 of the schedules apply to articles imported into the customs territory of the United States as hereinafter provided in this headnote:

(a) Products of Insular Possessions.

(i) Except as provided in headnote 6 of schedule 7, part 2, subpart E, [and] except as provided in headnote 4 of schedule 7, part 7, subpart A, articles imported from insular possessions of the United States which are outside the customs territory of the United States are subject to the rates of duty set forth in column numbered 1 of the schedules, except that all such articles the growth or product of any such possession, or manufactured or produced in any such possession from materials the growth, product, or manufacture of any such possession or of the customs territory of the United States, or of both, which do not contain foreign materials to the value of more than 50 percent of their total value (or more than 70 percent of their total value with respect to watches and watch movements), coming to the customs territory of the United States directly from any such possession, and all articles previously imported into the customs territory of the United States with payment of all applicable duties and taxes imposed upon or by reason of importation which were shipped from the United States, without remission, refund, or drawback of such duties or taxes, directly to the possession from which they are being returned by direct shipment, are exempt from duty.

(ii) In determining whether an article produced or manufactured in any such insular possession contains foreign materials to the value of more than 50 percent, no material shall be considered foreign which, at the time such article is entered, may be imported into the customs territory from a foreign country, other than Cuba or the Philippine Republic, and entered free of duty.

(iii) Subject to the limitations imposed under section 503(b) and 504(c) of the Trade Act of 1974, articles designated eligible articles under section 503 of such Act which are imported from an insular possession of the United States shall receive duty treatment no less favorable than the treatment afforded such articles imported from a beneficiary developing country under title V of such Act.

(b) Products of Cuba. Products of Cuba imported into the customs territory of the United States, whether imported directly or indirectly, are subject to the rates of duty set forth in column numbered 1 of the schedules. Preferential rates of duty for such products apply only as shown in the said column 1. 1/

1/ By virtue of section 401 of the Tariff Classification Act of 1962, the application to products of Cuba of either suspended. See general headnote 3(e), infra.

(c) Products of Countries Designated Beneficiary Developing Countries for Purposes of the Generalized System of Preferences (GSP).

(i) The following countries and territories are designated beneficiary developing countries for purposes of the Generalized System of Preferences, provided for in Title V of the Trade Act of 1974 (88 Stat. 2066, 19 U.S.C. 2461 et seq.):

Independent Countries

Afghanistan	Malagasy Republic
Angola	Malawi
Argentina	Malaysia
Bahamas	Maldive Islands
Bahrain	Mali
Bangladesh	Malta
Barbados	Mauritania
Bhutan	Mauritius
Bolivia	Mexico
Botswana	Morocco
Brazil	Mozambique
Burma	Nauru
Burundi	Nepal
Cameroon	Nicaragua
Cape Verde	Niger
Central African Republic	Oman
Chad	Pakistan
Chile	Panama
Colombia	Papua New Guinea
Congo (Brazzaville)	Paraguay
Costa Rica	Peru
Cyprus	Philippines
Dahomey	Rumania
Dominican Republic	Rwanda
Egypt	Sao Tome and Principe
El Salvador	Senegal
Equatorial Guinea	Sierra Leone
Ethiopia	Singapore
Fiji	Somalia
Gambia	Sri Lanka
Ghana	Sudan
Grenada	Surinam
Guatemala	Swaziland
Guinea	Syria
Guinea Bissau	Taiwan
Guyana	Tanzania
Haiti	Thailand
Honduras	Togo
India	Tonga
Israel	Trinidad and Tobago
Ivory Coast	Tunisia
Jamaica	Turkey
Jordan	Upper Volta
Kenya	Uruguay
Korea, Republic of	Western Samoa
Laos	Yemen Arab Republic
Lebanon	Yugoslavia
Lesotho	Zaire
Liberia	Zambia

ATTACHMENT B

	Virgin Islands Production Quota	Shipments from V.I. to U.S.	U.S. Domestic Wool Apparel Fabric Production
		(In Thousands of Linear Yards)	
1975	3,500	453*	68,100 (est.)
1974	3,500	1,468	72,661
1973	3,500	2,368	99,674
1972	2,500	2,173	95,841
1971	2,500	2,841	108,851
1970	2,500	3,734	171,975

*Eleven months data.

(full year)

THE GENERAL COUNSEL OF THE TREASURY
WASHINGTON, D.C. 20220

FEB 18 1976

Dear Mr. Chairman:

Reference is made to your request for the views of this Department on S. 1904, a bill "To amend the Tariff Schedules of the United States in order to change the customs treatment of certain woven fabrics of wool if products of an insular possession of the United States but imported into such possession as fabric for further processing."

The proposed legislation would amend the Tariff Schedules of the United States (19 U.S.C. 1202) by imposing a quantitative limitation (1,000,000 linear yards in 1975 and 500,000 linear yards in subsequent years) on the duty-free entry under General Headnote 3(a) of the Tariff Schedules of certain foreign woolen fabrics which have undergone further processing in an insular possession of the United States located outside the United States customs territory. Beyond these limits, fabrics from the islands would be subject to the same U.S. tariff as woolens from any other most-favored-nation source. The woven woolen fabrics to which the proposed legislation relates are those described in items 336.50, 336.55, and 336.60 of the Tariff Schedules of the United States.

Presently, under General Headnote 3(a) of the Tariff Schedules, fabrics are entitled to duty-free entry if they are deemed to be a manufacture or product (not fabrics merely further processed) of the insular possessions and if they meet the value requirements set forth under that provision. In recent years a growing volume of trade in woolen fabrics has been entering through the Virgin Islands, where woolens frequently undergo further processing to meet the 50 per cent value-added criterion for duty-free entry into the United States. The increased value of such shipments from this insular possession -- $300,000 in 1968, $5.2 million in 1973, and $2.7 million in 1974 -- has given rise to protests from the U. S. textile industry against the discriminatory loophole in General Headnote 3(a) of the Tariff Schedules, as presently written, which, if continued, could bring about substantial unemployment in that industry.

Although the Treasury normally would oppose any measure which would create a new tariff or a nontariff barrier to trade, the instant situation would seem to warrant amendatory action. No unusual administrative difficulties are anticipated if the proposed legislation is enacted. Therefore, the Department would have no objection to enactment of S. 1904.

The Department has been advised by the Office of Management and Budget that there is no objection from the standpoint of the Administration's program to the submission of this report to your Committee.

Sincerely yours,

Richard R. Albrecht

General Counsel

The Honorable
Russell Long, Chairman
Committee on Finance
United States Senate
Washington, D. C. 20510

Departmental Comments Received as of Aug. 23, 1956 on the Various House Passed Revenue and Tariff Bills

75-946 O - 76 - 14

GENERAL COUNSEL OF THE
UNITED STATES DEPARTMENT OF COMMERCE
Washington, D.C. 20230

JUN 28 1976

Honorable Russell B. Long
Chairman, Committee on Finance
United States Senate
Washington, D. C. 20510

Dear Mr. Chairman:

This is in reply to your request for the views of this Department on H.R. 1386, an Act

"For the relief of Smith College Northampton, Massachusetts."

H.R. 1386 would authorize the Secretary of the Treasury to admit free of duty thirty-three carillon bells (including all accompanying parts and accessories) manufactured in France for the use of Smith College, Northampton, Massachusetts. The bill further provides that, if the liquidation of the entry for any of the articles has become final, such entry shall be reliquidated and the appropriate refund of duty shall be made.

The bells which are the subject of the bill are tentatively valued at $36,400. Carillon bells are classified under item 725.36 of the Tariff Schedules of the United States (19 U.S.C. 1202), which provides that "Percussion musical instruments: Sets of tuned bells known as chimes, peals, or carillons:....Containing over 22 but not over 34 bells" are dutiable at 7 percent *ad valorem*. Duty would be approximately $2,550.

The Department of Commerce has no objection to the enactment of H.R. 1386.

When contacted in October 1974 concerning H.R. 16162, similar 93rd Congress legislation, the only known domestic producer of carillon bells indicated that he expected to stop casting bells and would concentrate entirely on importation and installation of bells.

Consequently, there appears to be no domestic producer of carillon bells that may be affected by the enactment of this bill.

In the event this legislation were enacted, it would have no impact on the revenues to, or the administrative cost of, this Department.

We have been advised by the Office of Management and Budget that there would be no objection to the submission of this report from the standpoint of the Administration's program.

Sincerely,

General Counsel

UNITED STATES
INTERNATIONAL TRADE COMMISSION
WASHINGTON, D.C. 20436

THE CHAIRMAN

August 18, 1976

Honorable Russell B. Long
Chairman, Committee on Finance
United States Senate
Washington, D.C. 20515

Dear Mr. Chairman:

H.R. 1386 has the effect of a private bill which, upon enactment, would direct the Secretary of the Treasury to admit free of duty a thirty-three bell carillon imported for the use of Smith College, Northampton, Massachusetts. In the case that the liquidation of the entry has become final, the bill authorizes reliquidation of the entry with appropriate refund of duties.

The most-favored-nation rates of duty applicable to carillons under items 725.34-.38 of the Tariff Schedules of the United States are currently as follows when--

Containing not over 22 bells-------------------	5% ad val.
Containing over 22 but not over 34 bells--------	7% ad val.
Containing over 34 bells-----------------------	3% ad val.

Information received by the Commission indicates that the sole producer of carillons in the United States has manufactured similar carillons containing as many or more bells in the last several months. However, this domestic manufacturer has scaled down its operation to the point where only 3 individuals are currently involved in the production of bells on a "to-order" basis and this manufacturer does not oppose the enactment of H.R. 1386.

Imports of carillons containing over 22 but not over 34 bells were valued at $8,325 in 1974, and increased to $53,013 in 1975.

Sincerely,

Will E. Leonard

Will E. Leonard
Chairman

206

GENERAL COUNSEL OF THE
UNITED STATES DEPARTMENT OF COMMERCE
Washington, D.C. 20230

AUG 9 1976

Honorable Russell B. Long
Chairman, Committee on Finance
United States Senate
Washington, D. C. 20510

Dear Mr. Chairman:

This is in response to your request for the views of this Department on H.R. 2177, an Act

"To exempt from duty certain aircraft components and materials installed in aircraft previously exported from the United States where the aircraft is returned without having been advanced in value or improved in condition while abroad."

If enacted, this legislation would provide duty exemption for components and materials of U.S. origin installed in aircraft in the United States when such aircraft are exported from the United States and reimported without having been advanced in value or improved in condition while abroad. The Act would apply only if the aircraft were entered for consumption before 1970 pursuant to an entry which is unliquidated as of the date of enactment of the Act.

This Act applies to a unique case in which a used aircraft with U.S. components was purchased abroad and imported into the United States. The Act would exempt from duty the U.S. components which had been installed in the plane following a previous importation.

The Department of Commerce does not object to enactment of H.R. 2177. It appears equitable to the Department in this case to exempt products of the United States from duty when such products are fabricated components of an article previously exported and reentered and when the components of U.S. origin have not been advanced in value or improved in condition while abroad. In the Department's view, there appears to be no reasonable purpose served in holding dutiable such components, as the U.S. Customs Service has so ruled them under present law. In our view, exemption from duty in this case would, moreover, be consistent with the duty-free treatment already provided under TSUS item 800.00 for products of the United States when returned after having been exported, without having been advanced in value or improved in condition while abroad.

In the event this legislation were enacted it would have no impact on the revenues to, or the administrative costs of, this Department.

We have been advised by the Office of Management and Budget that there would be no objection to the submission of this report to the Congress from the standpoint of the Administration's program.

Sincerely,

J.T. Smith

General Counsel

UNITED STATES INTERNATIONAL TRADE COMMISSION
Washington, D.C.

AUG 1^ 1976

MEMORANDUM TO THE SENATE COMMITTEE ON FINANCE ON H.R. 2177, AN ACT TO EXEMPT FROM DUTY CERTAIN AIRCRAFT COMPONENTS AND MATERIALS INSTALLED IN AIRCRAFT PREVIOUSLY EXPORTED FROM THE UNITED STATES WHERE THE AIRCRAFT IS RETURNED WITHOUT HAVING BEEN ADVANCED IN VALUE OR IMPROVED IN CONDITION WHILE ABROAD.

H.R. 2177 would exempt from duty components and materials of any aircraft which are products of the United States and which were installed (after the aircraft was operational) while the aircraft was within the United States when such aircraft is returned to the United States after having been exported without having been advanced in value or improved in condition by any process of manufacture or other means while abroad. This exemption is extremely limited, however, in that it only applies to aircraft which were entered for consumption before 1970 pursuant to an entry which is unliquidated as of the date of the enactment of H.R. 2177.

Although the Commission is not aware of the exact number of aircraft which would qualify for the duty exemption provided for in H.R. 2177, it is doubtful that there could be very many entries of such aircraft which were filed prior to 1970 and have not yet been liquidated. Therefore, the potential impact of this act on customs revenues would appear to be minimal.

The enactment of H.R. 2177 would not alter the present tariff treatment of aircraft in the Tariff Schedules of the United States.

75-946 O - 76 - 15

The act is apparently designed for a very limited purpose, and, so long as the U.S. Customs Service does not liquidate the subject entries prior to the enactment of H.R. 2177, it would appear that the act would accomplish that purpose. The Commission has found no technical deficiencies in the drafting of H.R. 2177.

THE GENERAL COUNSEL OF THE TREASURY
WASHINGTON, D.C. 20220

JUN 10 1976

Dear Mr. Chairman:

Reference is made to your request for the views of this Department on H.R. 2181, a bill "To amend the Tariff Schedules of the United States to provide duty-free treatment of any aircraft engine used as a temporary replacement for an aircraft engine being overhauled within the United States if duty was paid on such replacement engine during a previous importation."

H.R. 2181 would amend the Tariff Schedules of the United States (TSUS), (19 U.S.C. 1202) by the inclusion of a new item numbered 801.20, in subpart A of part 1 of schedule 8, TSUS. The new item would provide for the duty-free entry of any aircraft engine or propeller or any part or accessory of either, previously imported, with respect to which the duty was paid upon such previous importation, if (1) reimported without having been advanced in value or improved in condition by any process of manufacture or other means while abroad, after having been exported under loan, lease, or rent to an aircraft owner or operator as a temporary replacement for an aircraft engine being overhauled, repaired, rebuilt, or reconditioned in the United States, and (2) reimported by or for the account of the person who exported it from the United States.

Importations of the type described by the proposed bill are now subject to duty on full appraised value by reason of headnote 1, part 1, schedule 8, TSUS, which provides that in the absence of a specific provision to the contrary, the tariff status of an article is not affected by the fact that it was previously imported into the Customs territory of the United States and cleared through Customs whether or not duty was paid upon such previous importation. As there is no specific provision in the tariff schedules under which previously imported and duty-paid aircraft engines, propellers, or any part or accessory of either, could be exported and returned free of duty in the context of the type of transaction described in the bill, they would be subject to duty on each successive importation.

We are unable to reliably estimate the amount of duty now being collected on airplane engines and their parts which are imported under the circumstances in which the proposed bill would apply, because import statistics do not differentiate between articles imported for the first time and those which were previously imported. The principal importers under the proposed tariff provision would be firms that repair and overhaul engines and regularly loan engines to customers. Six such firms have been identified in the United States, and it is probable that the yearly loss of revenue from those importers alone would exceed $2.5 million if the bill is enacted. In addition to repair firms, some importations by commercial airlines would also be affected by the bill, resulting in additional loss of revenue.

The Department takes no position on the merits of the proposed legislation. No unusual administrative difficulties are anticipated should the bill be enacted.

The Department was advised by the Office of Management and Budget that there was no objection from the standpoint of the Administration's program to the submission of a similar report on this bill to the House Committee on Ways and Means.

Sincerely yours,

Richard R. Albrecht

General Counsel

The Honorable
Russell Long, Chairman
Committee on Finance
United States Senate
Washington, D.C. 20510

THE SPECIAL REPRESENTATIVE FOR
TRADE NEGOTIATIONS
WASHINGTON

28 JUN 1976

The Honorable Russell Long
Chairman, Committee on Finance
United States Senate
Washington, D. C. 20510

Dear Mr. Chairman:

Thank you for your letter of May 26, 1976 requesting a report from this Office on H.R. 2181, an Act "To amend the Tariff Schedules of the United States to provide duty-free treatment of any aircraft engine used as a temporary replacement for an aircraft engine being overhauled within the United States if duty was paid on such replacement engine during a previous importation."

We have reviewed the proposed legislation and have no objection to its enactment.

The Office of Management and Budget advises that there is no objection to the presentation of these views from the standpoint of the Administration's program.

Sincerely,

Frederick B. Dent

GENERAL COUNSEL OF THE
UNITED STATES DEPARTMENT OF COMMERCE
Washington, D.C. 20230

JUN 28 1976

Honorable Russel B. Long
Chairman, Committee on Finance
United States Senate
Washington, D. C. 20510

Dear Mr. Chairman:

This is in further reply to your request for the views of this Department with respect to H.R. 2181, an Act

"To amend the Tariff Schedules of the United States to provide duty-free treatment of any aircraft engine used as a temporary replacement for an aircraft engine being overhauled within the United States if duty was paid on such replacement engine during a previous importation."

If enacted, H.R. 2181 would amend the Tariff Schedules of the United States (TSUS) to add a new item 801.20 to allow duty-free entry of aircraft engines and parts which have been previously imported, with respect to which duty was paid on the previous importation, under the following conditions: (1) the engines or parts must be reimported without having been advanced in value or improved in condition while abroad, after having been exported under loan, lease, or rent to an aircraft owner or operator as a temporary replacement for an aircraft engine being overhauled, repaired, rebuilt, or reconditioned in the United States and, (2) must be reimported by or for the account of the person who exported them from the United States. Piston and jet aircraft engines and parts are dutiable at the respective rates of 4 percent ad valorem (TSUS item 660.44) and 5 percent ad valorem (TSUS item 660.46).

The Department of Commerce favors enactment of H.R. 2181.

Under item 801.00 of the TSUS articles previously imported are duty-free under conditions similar to those proposed in H.R. 2181, if reimported after having been exported under lease to a foreign manufacturer. However, in the case of aircraft owners or operators, rather than foreign manufacturers, such items do not qualify under item 801.00 and new tariff provisions appear to be necessary to obtain like treatment.

There are three major American firms engaged in the foreign aircraft engine repair business which supply replacement engines on loan. In order to service clients who own foreign-made aircraft engines, these firms purchase comparable aircraft engines and pay duty on them when they are originally imported. When an aircraft experiences engine trouble overseas, the American firm will loan an engine to the distressed aircraft and bring the original engine to the United States for repair. When the repair work is completed, the original engine is returned to the aircraft and the loaned engine is reimported by the American repair firm. With each reentry, duty must be paid. Between 100 and 150 reentries are made each year in the course of these firms' operations, resulting in an estimated $2 million in annual duty payments. As a result of these duty payments, the firms involved estimate a loss in business each year of several million dollars to their foreign competitors.

Enactment of H.R. 2181 would be consistent with the Administration's policy of promoting United States exports of goods and services. The duties payable on multiple entries of aircraft engines and parts in the normal course of the aircraft engine repair business represent a disincentive to the export of such services, as well as an unnecessary financial burden, which should and can be removed by the enactment of H.R. 2181.

In the event this legislation were enacted, it would have no impact on the revenues to, or administrative costs of, this Department.

We have been advised by the Office of Management and Budget that there would be no objection to the submission of this report from the standpoint of the Administration's program.

Sincerely,

General Counsel

UNITED STATES INTERNATIONAL TRADE COMMISSION
Washington, D.C. 20436

August 16, 1976

MEMORANDUM TO THE SENATE FINANCE COMMITTEE ON H.R. 2181, 94TH CONGRESS, AN ACT "TO AMEND THE TARIFF SCHEDULES OF THE UNITED STATES TO PROVIDE DUTY-FREE TREATMENT OF ANY AIRCRAFT ENGINE USED AS A TEMPORARY REPLACEMENT FOR AN AIRCRAFT ENGINE BEING OVERHAULED WITHIN THE UNITED STATES IF DUTY WAS PAID ON SUCH REPLACEMENT ENGINE DURING A PREVIOUS IMPORTATION."

H.R.2181 proposes to amend subpart A of part 1 of schedule 8 of the Tariff Schedules of the United States (TSUS) by inserting immediately after item 801.10, TSUS, a new item providing for the duty-free entry of:

> Any aircraft engine or propeller, or any part or accessory of either, previously imported, with respect to which the duty was paid upon such previous importation, if (1) reimported without having been advanced in value or improved in condition by any process of manufacture or other means while abroad, after having been exported under loan, lease, or rent to an aircraft owner or operator as a temporary replacement for an aircraft engine being overhauled, repaired, rebuilt, or reconditioned in the United States, and (2) reimported by or for the account of the person who exported it from the United States.

Section 2 of the act provides that the amendment shall be effective with respect to articles entered, or withdrawn from warehouse, for consumption on or after the date of the enactment of this Act.

The Commission has been advised that the act was occasioned by the inability of a firm engaged in the repair of aircraft engines to enter its "loaner" or replacement engines, propellers, parts and accessories (upon which duty had been paid on previous importations) free of duty. 1/ It is our understanding that the engines, propellers, parts and accessories to be repaired are entered into the United States without the payment of duty, under bond, for their exportation, pursuant to item 864.05,

---

1/ While some of its replacement engines, propellers, parts and accessories were originally imported by this firm, a significant percentage of its foreign engines and parts were purchased from others in the United States.

TSUS. Since it is often not economically feasible to ground an aircraft in the United States for a prolonged period of time pending engine repairs, it is the common practice to remove the defective engine or part while the aircraft is abroad and replace it with a "loaner" engine or part from the United States (subject to a rental fee). When the repair involves foreign engines, the replacement engines or parts are also invariably foreign made. When the repairs have been completed and the repaired articles are exported, the replacement engines or parts are returned to the United States where they are ordinarily subject to the payment of appropriate import duties. In this regard, headnote 1 to part 1 of schedule 8, TSUS, provides that:

> In the absence of a specific provision to the contrary, the tariff status of an article is not affected by the fact it was previously imported into the customs territory of the United States and cleared through customs whether or not duty was paid upon such previous importation.

In the case of the repair firm sponsoring this legislation, we have been informed that no duties have been paid on its replacement engines or parts since 1973. All of these engines and parts have been entered without the payment of duty, under bond, for their exportation, pursuant to item 864.05, TSUS, which provides for the temporary importation of articles to be repaired, altered, or processed. Under this provision of the TSUS, these engines and parts must be exported from the United States within 3 years (at the latest) of the date of importation. This requirement appears to be the reason for the retroactive provisions of the proposed legislation.

H.R. 2181, if enacted, would create a specific provision for the duty-free reimportation of "loaner" or replacement engines, propellers, parts and accessories. Similar duty-free provisions presently exist in part 1A of schedule 8, TSUS, to cover reimportations of articles exported under lease to a foreign manufacturer (item 801.00, TSUS), and reimportations of articles which do not conform to sample or specification (item 801.10, TSUS). The proposed legislation differs from these two existing provisions in that it only requires that the engine, propeller, part or accessory be reimported by or for the account of the person who exported it from the United States, while items 801.00 and 801.10, TSUS, require that the articles in question be reimported <u>by or for the account of the person who imported it into, and exported it from,</u> the United States. The rationale behind the existing provisions appears to be to prevent double liability for the payment of duty on imported articles under certain circumstances. The proposed legislation, as written could not only prevent double liability, it could preclude any liability for duty with respect to a person reimporting an article which he exported from the United States, but which he did not originally import and pay duties on.

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THE GENERAL COUNSEL OF THE TREASURY
WASHINGTON, D.C. 20220

JUN 22 1976

Dear Mr. Chairman:

Reference is made to your request for the views of this Department on H.R. 4047, "For the relief of Jack R. Misner."

Mr. Misner of North Tonawanda, New York, filed a temporary importation entry on September 25, 1972, under item 864.05, Tariff Schedules of the United States, for the renovation of the schooner Panda which was imported on September 19, 1972. This renovation has been delayed because of material shortages encountered by Mr. Misner.

Headnote 1, subpart 5C, schedule 8, Tariff Schedules of the United States, provides that the total period for which merchandise entered under a temporary importation bond may remain in the United States shall not exceed 3 years. H.R. 4047 would extend the 3-year period for the schooner Panda, which was due to expire September 18, 1975, for 2 additional years.

Although the bill would confer on Mr. Misner privileges not available generally to other importers, in view of the circumstances involved, this Department has no objection to the enactment of the proposed legislation. Further, the Department expects no unusual administrative difficulties in carrying out the provisions of the proposed legislation.

The Department has been advised by the Office of Management and Budget that there was no objection from the standpoint of the Administration's program to the submission of a similar report on this bill to the House Committee on Ways and Means.

Sincerely yours,

Acting General Counsel
[illegible] C. Stockell, Jr.

The Honorable
Russell Long, Chairman
Committee on Finance
United States Senate
Washington, D.C. 20510

GENERAL COUNSEL OF THE
DEPARTMENT OF COMMERCE
Washington, D.C. 20230

JUN 29 1976

Honorable Russell B. Long
Chairman, Committee on Finance
United States Senate
Washington, D.C. 20510

Dear Mr. Chairman:

This is in reply to your request for the views of this Department on H.R. 4047, an Act

"For the relief of Jack R. Misner."

H.R. 4047 would extend until September 18, 1977, the expiration date of the temporary importation bond covering the schooner Panda. Mr. Misner entered the Panda, which is under British registry, into the United States on September 25, 1972, for the purpose of carrying out certain repairs on the vessel. The Panda was entered under provisions of item 864.05 of the Tariff Schedules of the United States (TSUS), which provides that articles to be repaired, altered, or processed in the United States, when not imported for sale in the United States, may be admitted without the payment of duty, under bond for their exportation within one year of the date of importation. This period may be extended upon application, at the discretion of the Secretary of the Treasury, for a period not to exceed a total entry period of three years.

Upon entry of the vessel Mr. Misner paid the required temporary importation bond, which is double the duty that would be paid for regular importation of the vessel, and the schooner was granted duty-free entry under the bond for a period of one year following September 25, 1972. In 1973 Mr. Misner applied for and was granted a two-year extension of the bond until September 1975. However, repairs to the vessel have been hampered by continuing delays in delivery of certain parts, all of domestic origin, with the result that the repairs were not completed by September 1975, and Mr. Misner stands to forfeit the bond. Therefore, Mr. Misner is seeking legislative relief because the TSUS does not allow a temporary entry period of longer than three years, even if repairs are delayed because of parts shortages.

The Department of Commerce does not object to H.R. 4047. The Department believes that this Act does not affect U.S. international economic policy and that it does not adversely affect U.S. producers as the repairs are being made with goods produced by U.S. manufacturers.

In the event this legislation were enacted, it would have no impact on the revenues to, or administrative costs of, this Department.

We have been advised by the Office of Management and Budget that there would be no objection to the submission of this report to the Congress from the standpoint of the Administration's program.

Sincerely,

General Counsel

August 16, 1976

UNITED STATES INTERNATIONAL TRADE COMMISSION
Washington, D.C.

MEMORANDUM TO THE SENATE FINANCE COMMITTEE ON H.R. 4047, 94TH CONGRESS, AN ACT FOR THE RELIEF OF JACK R. MISNER

H.R. 4047 has the effect of a private bill which, upon enactment, would direct the Secretary of the Treasury to extend the expiration date of the temporary importation bond covering the schooner Panda until the close of September 18, 1977, notwithstanding the provisions of subpart 5C of schedule 8 of the Tariff Schedules of the United States (TSUS) (19 U.S.C. 1202).

Mr. Jack R. Misner of North Tonawanda, New York, filed a temporary importation entry on September 25, 1972, under item 864.05, TSUS, 1/ for the renovation of the schooner Panda which was imported on September 19, 1972. This renovation has been delayed because of shortages of material encountered by Mr. Misner. Headnote 1, subpart 5C, schedule 8, TSUS, provides that the total period for which merchandise entered under a temporary importation bond may remain in the United States shall not exceed 3 years. The 3-year period for the schooner Panda is to expire September 18, 1975. H.R. 4047 would extend this period for two additional years.

Although the Secretary of the Treasury is currently empowered under section 318, Tariff Act of 1930, as amended (19 U.S.C. 1318), to extend the time period prescribed therein for the performance of any act during the continuance of an emergency proclaimed by the President, this authority does not provide any basis for relief to Mr. Misner.

1/ Item 864.05 provides for the temporary importation under bond of --"Articles to be repaired, altered or processed (including processes which result in articles manufactured or produced in the United States)."

This bill would, in effect, confer upon Mr. Misner privileges which are not available to other importers. From an equitable or hardship point of view, the circumstances in this case may very well warrant the extension of the temporary importation bond period. However, it may be that there are other similar hardship cases or there may be such cases in the future, therefore, the Committee may wish to give consideration to giving to the Secretary of the Treasury the authority to grant extensions in any instance where he deems the circumstances warrant.

If the 3-year temporary importation bond period is to be extended for hardship cases the most appropriate remedy would be an amendment of headnote 1, subpart 5C, schedule 8, TSUS to give the Secretary of the Treasury the authority to extend the period in cases of hardship. It is suggested that such an amendment might be as follows (new language underscored):

> 1. (a) The articles described in the provisions of this subpart, when not imported for sale or for sale on approval, may be admitted into the United States without the payment of duty, under bond for their exportation within 1 year from the date of importation, which period, in the discretion of the Secretary of the Treasury, may be extended, upon application, for one or more further periods which, when added to the inital 1 year, shall not exceed a total of 3 years, except that (1) with respect to articles imported under item 864.05 the period may be extended beyond 3 years in cases of hardship, at the discretion of the Secretary of the Treasury, (2) articles imported under item 864.75 shall be admitted under bond for their exportation within 6 months from the date of importation and such 6-months period shall not be extended, and (3) in the case of professional equipment and tools of trade admitted into the United States under item 864.50 which have been seized (other than by seizure made at the suit of private persons), the requirement of reexportation shall be suspended for the duration of the

seizure. For purposes of this headnote, an aircraft engine or propeller, or any part or accessory of either, imported under item 864.05, which is removed physically from the United States as part of an aircraft departing from the United States in international traffic shall be treated as exported.

(b) For articles admitted into the United States under item 864.50, entry shall be made by the nonresident importing the articles or by an organization represented by the nonresident which is established under the laws of a foreign country or has its principal place of business in a foreign country.

THE GENERAL COUNSEL OF THE TREASURY
WASHINGTON, D.C. 20220

AUG 3 - 1976

Dear Mr. Chairman:

This is in response to your request for the views of the Treasury Department on H.R. 7228, 94th Congress, 2d Session, a House passed bill. H.R. 7228 would amend section 5205(h) of title 26 of the United States Code to permit the authorization of means other than stamps on containers of distilled spirits as evidence of tax payment.

Under existing law the payment of the Federal excise tax on distilled spirits is required to be evidenced by the attachment of what is commonly known as a strip stamp to the containers.

The technological advances in the closure industry indicate that it may become preferable to evidence the tax payment on containers of distilled spirits by devices other than the stamps that are now used. The proposed amendment to section 5205(h) of the words "or other device" to the current description of form of stamp will allow the authorization of other forms of evidence of tax payment under the regulatory controls now in existence.

In addition, H.R. 7228 would amend section 6801(b) which currently restricts the preparation and distribution of stamps to the Secretary or his delegate.

The restriction has no undesirable features in relation to the preparation and distribution of paper stamps since the Bureau of Engraving and Printing is geared to the printing of paper materials. However, the restriction does exclude consideration of most other methods and materials because the Government is not generally equipped to prepare them in the desired form from other materials.

The Department recognizes that the stamp used on distilled spirits containers to evidence tax payment represents large amounts of taxes and that the preparation and distribution of this evidence of tax payment outside of the Government should be made only under circumstances which will ensure that no revenue is lost because a different method is used to evidence tax payment. The amendment to section 6801(b) provides that the Secretary is to prescribe whatever controls are necessary for the protection of the revenue when authorizing persons outside of the Government to prepare and distribute stamps or other devices for evidence of tax payment on containers of distilled spirits. This amendment will provide the Secretary with the flexibility to consider and approve new materials and methods of preparing and distributing the product while retaining the control believed essential to the protection of the revenue.

Enactment of H.R. 7228 would have no effect on the revenues.

Accordingly, the Treasury Department favors enactment of H.R. 7228.

The Department has been advised by the Office of Management and Budget that there is no objection from the standpoint of the Administration's program to the submission of this report to your Committee.

Sincerely yours,

Richard R. Albrecht

General Counsel
Richard R. Albrecht

The Honorable
Russell B. Long, Chairman
Committee on Finance
United States Senate
Washington, D.C. 20510

THE GENERAL COUNSEL OF THE TREASURY
WASHINGTON, D.C. 20220

JUL 22 1976

Dear Mr. Chairman:

This is in response to your request for the views of the Treasury Department on H.R. 8283, 94th Congress, 2d Session, a House passed bill. H.R. 8283 would amend section 5386(a) of title 26 of the United States Code with respect to the type of flavors which may be used on bonded wine cellar premises in the production of special natural wines.

Under existing law (26 U.S.C. § 5386), special natural wines are generally the products made, pursuant to an approved formula, from a base of natural wine exclusively, with the addition, before, during or after fermentation, of natural herbs, spices, fruit juices, aromatics, essences, and other natural flavorings. Flavors other than natural are not presently permitted to be used in the production of special natural wines.

The Department recognizes that in the processing of natural flavors, particularly those of a delicate nature, percolation, distillation, extraction, and other processes often destroy desirable characteristics. Therefore, the need becomes apparent to restore some of the original character of such flavors which is lost by the addition of small amounts of flavor other than natural. However, such additions are currently precluded under the law.

H.R. 8283 would amend section 5386(a) to permit flavors, other than natural, to be used in the production of special natural wines. It is based on the present need to allow the use of small amounts of flavors other than natural in the production of special natural wines, and vests in the Secretary or his delegate the authority to approve the use of such flavors. H.R. 8283 would not affect the circumstances under which natural herbs, spices, fruit juices, aromatics, and other natural flavorings may be used in producing special natural wines.

Enactment of H.R. 8283 would have no affect on the revenues. Furthermore, the additional costs incurred by the Government as a result of an enactment of the proposed bill would be negligible.

Accordingly, the Treasury Department has no objection to the enactment of H.R. 8283.

The Department has been advised by the Office of Management and Budget that there is no objection from the standpoint of the Administration's program to the submission of this report to your Committee.

Sincerely yours,

(Signed) Richard R. Albrecht

General Counsel

The Honorable
Russell B. Long, Chairman
Committee on Finance
United States Senate
Washington, D.C. 20510

THE SPECIAL REPRESENTATIVE FOR
TRADE NEGOTIATIONS
WASHINGTON

29 JUL 1976

Dear Mr. Chairman:

Thank you for your letter of June 11, 1976 requesting a report from this Office on H.R. 8656, an Act "To amend the Tariff Schedules of the United States in order to provide for the duty-free importation of loose glass prisms used in chandeliers and wall brackets."

The prisms covered by the bill are not produced in the United States. Since domestic users are dependent on foreign supplies, elimination of the duty would help U.S. producers of chandeliers to compete more effectively with imports of such articles, with potential benefits in the form of increased production and employment.

It is usually preferable to reduce or eliminate duties in the context of a trade agreement, which enables the United States to secure reciprocal advantages for our exports. However, under the circumstances noted above, we believe that the negotiating value of loose prisms would not be large. Moreover, the present duty could be reduced only 60 percent rather than eliminated. For these reasons, the benefits of unilateral duty elimination in this case appear to offset the costs, and this Office accordingly has no objection to enactment of H.R. 8656.

The Office of Management and Budget advises that there is no objection to the presentation of these views from the standpoint of the Administration's program.

Sincerely,
(signed) Frederick B. Dent

Frederick B. Dent

The Honorable Russell Long
Chairman, Committee on Finance
United States Senate
Washington, D.C. 20510

THE GENERAL COUNSEL OF THE TREASURY
WASHINGTON, D.C. 20220

JUN 10 1976

Dear Mr. Chairman:

Reference is made to your request for the views of this Department on H.R. 11259, "To lower the duty on levulose until the close of June 30, 1978."

The bill would amend subpart B of part 1 of the Appendix to the Tariff Schedules of the United States (19 U.S.C. 1202) by inserting a new item 907.90 to reduce the rate of duty on levulose to .6625 cent per pound (column 1) and 1.9875 cents per pound (column 2) until June 30, 1978. This would effectively reduce the column 1 tariff on levulose from 20 percent to approximately 1 percent ad valorem.

Levulose is a sugar complex used in special dietetic foods and medicinal products (e.g. for diabetes). Domestic consumption of this item is supplied wholly by imports. This bill should lower costs to consumers without injury to domestic industry. Furthermore, a temporary duty reduction ending on June 30, 1978, would not hinder negotiations in the MTN or conflict with any tariff reductions agreed therein.

The Customs Service anticipates no unusual administrative difficulties if the proposed legislation is enacted.

In light of the foregoing, the Department would have no objection to the enactment of the proposed legislation.

The Department was advised by the Office of Management and Budget that there was no objection from the standpoint of the Administration's program to the submission of a similar report on this bill to the House Committee on Ways and Means.

Sincerely yours,

Richard R. Albrecht

General Counsel

The Honorable
Russell Long, Chairman
Committee on Finance
United States Senate
Washington, D.C. 20510

THE SPECIAL REPRESENTATIVE FOR
TRADE NEGOTIATIONS
WASHINGTON

17 JUN 1976

The Honorable Russell B. Long
Chairman, Committee on Finance
United States Senate
Washington, D. C. 20510

Dear Mr. Chairman:

This is in response to your request of May 24, 1976, for the views of this Office on an Act, H.R. 11259, "To lower the duty on levulose until the close of June 30, 1978.

We have no objections to the above mentioned bill.

The Office of Management and Budget advises that it has no objection to the presentation of these views from the standpoint of the Administration's program.

Sincerely,

Frederick B. Dent

Frederick B. Dent

GENERAL COUNSEL OF THE
UNITED STATES DEPARTMENT OF COMMERCE
Washington, D.C. 20230

JUN 18 1976

Honorable Russell B. Long
Chairman, Committee on Finance
United States Senate
Washington, D. C. 20510

Dear Mr. Chairman:

This is in response to your request for the views of the Department of Commerce on H.R. 11259, an Act

> "To lower the duty on levulose until the close of June 30, 1978."

If enacted H.R. 11259 would amend the Tariff Schedules of the United States (TSUS) to provide for the importation of levulose at a reduced duty rate through June 30, 1978. The bill accomplishes this by adding the following new item to the TSUS:

		Column 1	Column 2
907.90	Levulose	0.6625¢ per lb.	1.9875¢ per lb.

The ad valorem equivalent of the proposed column-1 specific duty, based on 1975 import prices, is 1.0 percent. There have been no imports of levulose from column-2 countries in recent years. Levulose is currently dutiable under TSUS item 493.66 at a column-1 rate of 20 percent ad valorem and a column-2 rate of 50 percent ad valorem.

The Department of Commerce does not oppose enactment of H.R. 11259.

Levulose is a purified saccharide that is not produced commercially in the United States. Current use of levulose is for special dietetic foods and medicinal products. Imports amounted to about 274,000 pounds in

1975, valued at $175,000. Because of its high price and specialized uses, levulose is not directly competitive with other commercial sweeteners of the type produced in the United States. For this reason there should be no significant effect on U.S. industry if the duty on levulose is lowered.

The U.S. firm currently accounting for the bulk of levulose imports believes the temporary duty reduction will enable it to expand the U.S. market for levulose and justify its plans to establish a U.S. plant to produce the product domestically by 1978.

The Department believes that duty reductions should normally be accomplished through trade negotiations to obtain reciprocal concessions of value to U.S. exporters. In this case, however, we believe that the economic benefits of an immediate unilateral reduction outweigh the benefits of such potential reciprocal concessions that might be negotiated. In any case, since the duty reduction is temporary, the President could still negotiate a permanent reduction during the Multilateral Trade Negotiations.

Enactment of this legislation would not involve the expenditure of funds by this Department.

We have been advised by the Office of Management and Budget that there would be no objection to the submission of this report from the standpoint of the Administration's program.

Sincerely,

J. T. Smith

General Counsel

EXECUTIVE OFFICE OF THE PRESIDENT
OFFICE OF MANAGEMENT AND BUDGET
WASHINGTON, D.C. 20503

June 22, 1976

Honorable Russell Long
Chairman, Committee on Finance
United States Senate
2227 New Senate Office Building
Washington, D.C. 20510

Dear Mr. Chairman:

This is in reply to your letter of May 24, 1976, requesting the views of the Office of Management and Budget on H.R. 11259, a bill "To lower the duty on levulose, until the close of June 30, 1978."

For reasons set forth in the reports to your Committee from the Department of Commerce and the Department of the Treasury, the Office of Management and Budget would have no objection to enactment of this legislation.

Sincerely yours,

James M. Frey

James M. Frey
Assistant Director for
Legislative Reference

GENERAL COUNSEL OF THE
UNITED STATES DEPARTMENT OF COMMERCE
Washington, D.C. 20230

AUG 11 1976

Honorable Russell B. Long
Chairman, Committee on Finance
United States Senate
Washington, D. C. 20515

Dear Mr. Chairman:

This is in response to your request for the views of this Department on H.R. 11321, a bill

> "To suspend until July 1, 1978, the duty on certain elbow prostheses if imported for charitable therapeutic use, or for free distribution, by certain public or private non-profit institutions."

H.R. 11321 would suspend for the period beginning on the date of enactment and ending on July 1, 1978, the column-1 duties applicable to imports from countries afforded most-favored-nation tariff treatment of externally-powered electric elbow prosthetic devices for juvenile amputees, and parts thereof, if imported solely for charitable therapeutic use, or distribution free of charge, by any public or private nonprofit institution established for educational, scientific or therapeutic purposes. H.R. 11321 would amend subpart B of part 1 of the Appendix to the Tariff Schedules of the United States (19 U.S.C. 1202) by inserting after item 912.05 the new item 912.07 providing for the above suspension of duty. The column-2 duties applicable to imports of electric elbow prosthetic devices from other countries would not be affected.

The Department's interest in the proposed legislation arises principally in connection with its administration of the Educational, Scientific, and Cultural Materials

Importation Act of 1966 (Public Law 89-651; 80 Stat. 897), which permits the duty-free entry of certain instruments and apparatus when entered for the scientific or educational use of nonprofit institutions established for scientific or educational purposes. We provided comments on H.R. 11321 to the House Ways and Means Committee earlier this year, and on a predecessor Bill (H.R. 6893) last year; copies of our previous comments are enclosed for your information. In summary, the Department recommended on the most recent occasion that favorable consideration be given to H.R. 11321 after H.R. 6893 was revised to avoid an undesirable overlapping with the statutory scope of P.L. 89-651, and in accordance with our opinion that the Bill would have no adverse impact since there was no domestic production of such devices for juvenile amputees and none was anticipated for at least two or three years.

During our review of the circumstances as of June 1976, we learned that development in this area has occurred earlier than previously estimated. We understand that a prototype of a child-size electric elbow has reportedly been perfected by staff members of a university in New York and the developers have contracted for production of the device by a domestic manufacturer. We are advised, however, that even though the foreign and the new domestic devices have similar production costs, the developers of the U.S. device are convinced of its clear technical superiority over the foreign article, so that the proposal to suspend the duty on the foreign device is consequently of little or no concern to them. We also understand that the groups in the United States heretofore most interested in importing the foreign article free of duty scheduled testing of the new domestic device to begin in June 1976, and that the U.S. developers are confident the tests will result in their definite preference for the domestic device irrespective of whether or not duty must be paid on the foreign imports.

In view of these circumstances, the Department of Commerce has no objection to the enactment of H.R. 11321.

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We have been advised by the Office of Management and Budget that there would be no objection to the submission of our report to the Congress from the standpoint of the Administration's program.

Sincerely,

General Counsel

Enclosure

THE GENERAL COUNSEL OF THE TREASURY
WASHINGTON, D.C. 20220

JUN 11 1976

Dear Mr. Chairman:

Reference is made to your request for the views of this Department on H.R. 11605, "To suspend for a temporary period the rate of duty on mattress blanks of rubber latex."

The bill would amend subpart B of part 1 of the Appendix to the Tariff Schedules of the United States (TSUS) (19 U.S.C. 1202) by inserting a new item 912.08. H.R. 11605 would reclassify natural foam rubber used for bed mattresses from TSUS Item 727.86 to TSUS Item 912.08, until June 30, 1978. The effect of the reclassification is to permit natural foam rubber used in mattresses to enter the United States duty free until June 30, 1978. After June 30, 1978, the item would revert to its present TSUS classification. Currently this is a 15 percent rate of duty.

The bill was introduced because the only United States manufacturing plant of natural foam rubber burned down in March 1975. Consequently, the manufacturers of mattresses using natural foam rubber must now import foam rubber, mainly from Canada.

The Customs Service anticipates no unusual administrative difficulties if the proposed legislation is enacted.

In view of the fact that the only United States manufacturing plant of the product is out of production, the Department would have no objection to the enactment of the proposed legislation.

The Department was advised by the Office of Management and Budget that there was no objection from the standpoint of the Administration's program to the submission of a similar report on this bill to the Committee on Ways and Means.

Sincerely yours,

Richard R. Albrecht

General Counsel

The Honorable
Russell Long, Chairman
Committee on Finance
United States Senate
Washington, D.C. 20510

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EXECUTIVE OFFICE OF THE PRESIDENT
OFFICE OF MANAGEMENT AND BUDGET
WASHINGTON, D.C. 20503

June 28, 1976

Honorable Russell Long
Chairman, Committee on Finance
United States Senate
2227 New Senate Office Building
Washington, D. C. 20510

Dear Mr. Chairman:

This is in reply to your letter of May 26, 1976, requesting the views of the Office of Management and Budget on H.R. 11605, an Act "To suspend for a temporary period the rate of duty on mattress blanks of rubber latex."

For reasons set forth in the reports to your Committee from the Department of Commerce and the Department of the Treasury, the Office of Management and Budget would have no objection to enactment of this legislation.

Sincerely yours,

James M. Frey

James M. Frey
Assistant Director for
Legislative Reference

GENERAL COUNSEL OF THE
DEPARTMENT OF COMMERCE
Washington, D.C. 20230

JUN 29 1976

Honorable Russell B. Long
Chairman, Committee on Finance
United States Senate
Washington, D.C. 20510

Dear Mr. Chairman:

This is in response to your request for the views of this Department on H.R. 11605, an Act

"To suspend for a temporary period the rate of duty on mattress blanks of rubber latex."

If enacted, H.R. 11605 would amend the Tariff Schedules of the United States (TSUS) to suspend the duty on mattress blanks of rubber latex from countries afforded column-1, most-favored-nation treatment from April 1, 1975 until the close of June 30, 1978. Imports of mattress blanks of rubber latex are currently dutiable under TSUS item 727.86 at the column-1 rate of 15 percent ad valorem. The column-2 rate of duty, applicable to imports from communist countries except Poland, Yugoslavia, and Romania, would not be affected by the Act.

The Department of Commerce does not oppose enactment of H.R. 11605 since there is currently no domestic source of latex mattress blanks, and duty-free entry would help to control the production costs of those mattress manufacturers using this material.

Mattress blanks of rubber latex are used in the manufacture of a small percentage of the foam-core mattresses produced in the United States. The majority of the foam-core mattress industry utilizes synthetic materials. A fire on March 1, 1975, destroyed the last U.S. plant producing natural foam rubber latex, forcing the small sector of the foam-core mattress industry using latex blanks to import its needs. Import data are not available since mattress blanks of rubber latex are classified in the TSUS under a broader category.

Foam-core mattresses of rubber latex are not directly competitive with the synthetic variety produced in the United States because they are generally higher priced and supply a specialized market which demands the latex product. For this reason there should be no significant effect on the U.S. mattress industry if the duty on mattress blanks of rubber latex is temporarily suspended.

The Department normally believes that duty reductions should be accomplished through trade negotiations to obtain reciprocal concessions of value to U.S. exporters. In this case, however, it believes the economic benefits of an immediate unilateral reduction outweigh the potential reciprocal concessions that might be negotiated. It notes furthermore that reducing the rate temporarily would retain some negotiating value since the President could negotiate a permanent reduction during the multilateral trade negotiations.

Enactment of this legislation would not involve the expenditure of funds by this Department.

We have been advised by the Office of Management and Budget that there would be no objection to the submission of this report to the Congress from the standpoint of the Administration's program.

Sincerely,

J. V. Smith

General Counsel

THE SPECIAL REPRESENTATIVE FOR
TRADE NEGOTIATIONS
WASHINGTON

JUL 1 1976

The Honorable Russell Long
Chairman, Committee on Finance
United States Senate
Washington, D. C. 20510

Dear Mr. Chairman:

Thank you for your letter of May 26, 1976 requesting a report from this Office on H.R. 11605, an Act "To suspend for a temporary period the rate of duty on mattress blanks of rubber latex".

We have reviewed the proposed legislation and have no objection to its enactment.

The Office of Management and Budget advises that there is no objection to the presentation of these views from the standpoint of the Administration's program.

Sincerely,

Frederick B. Dent

UNITED STATES INTERNATIONAL TRADE COMMISSION

August 16, 1976

MEMORANDUM TO THE SENATE FINANCE COMMITTEE ON H.R. 11605, A BILL TO SUSPEND FOR A 3-YEAR PERIOD THE RATE OF DUTY ON MATTRESS BLANKS OF RUBBER LATEX

Purpose of bill

H.R. 11605, if enacted, would amend the Appendix to the Tariff Schedules of the United States (TSUS) to provide for the suspension until March 31, 1978, of the column 1 rate of duty on mattress blanks of rubber latex (provided for in item 727.86, part 4A, schedule 7). The column 2 rate of duty, which applies to most Communist-dominated countries (except Yugoslavia, Poland, and Romania) would not be affected.

Section 2(a) provides that the duty suspension will take effect on the date of enactment of H.R. 11605. Section 2(b) of the bill provides for the retroactive application of the duty suspension to entries made after March 31, 1975, upon the request filed therefor with the customs officer concerned on or before the ninetieth day after the date of enactment of the proposed legislation.

Description and uses

Imported mattress blanks of rubber latex are a blend of synthetic latex and natural rubber. The latex compound is mechanically whipped and metered into a mold. The rubber in the mold is vulcanized, then the blank is stripped from the mold, washed, dried, and tested for degree of firmness. Latex rubber mattress blanks have a density of approximately 4.5 pounds per cubic foot. Pin holes of up to one-fourth inch in diameter extend through the blank and make it breathable. Frequently tapes or fabric strips are put on the edges of the blank with adhesive prior to shipping. When the mattress blank is received by the importing firm in the United States, a quilted cover is sewn to the tapes on the edges of the blank, thus making a complete mattress which is then inspected, boxed, and shipped to a customer.

The domestically produced, high-density, high-resiliency polyurethane mattress competes directly with the latex foam mattress in the market place. 1/ Polyurethane blanks used in domestically produced mattresses vary in quality. Densities of polyurethane foam range from 1.2 pounds per cubic foot to 4 pounds per cubic foot, according to the domestic industry. The high-density, high-resiliency, polyurethane foam mattress has a density ranging from 3 to 4 pounds per cubic foot. Rubber latex and polyurethane mattress blanks are generally used in mattresses for regular and modular beds. There is some disagreement between importers of rubber latex mattress blanks and domestic producers of high-density, high-resiliency, polyurethane mattress blanks as to the relative overall quality of the two blanks. A study by Consumer Reports (January 1976) indicates that a latex foam mattress reverts to its original shape faster than a polyurethane mattress once the surface pressure on the mattress is removed. It is believed

1/ Innerspring mattresses account for approximately 85 percent of the mattresses sold in the United States; foam mattresses, for 15 percent. A customer desiring a foam mattress, however, would have to choose either the polyurethane foam type or the latex foam type.

however, that the high-density, high-resiliency, polyurethane foam mattress reverts to its original shape about as quickly as a latex foam mattress when the occupant of the bed moves or turns. Although some objective observers feel that the rubber latex mattresses are slightly superior to the high-density, high-resiliency, polyurethane mattresses, we have not been able to determine the relative consumer preferences for these products.

Tariff treatment

Mattress blanks, including those of rubber and of polyurethane, are currently being classified in item 727.86 of the TSUS with a column 1 duty rate of 15 percent ad valorem and a column 2 rate of 40 percent ad valorem. It should be noted that this item is included on the list of eligible articles under the Generalized System of Preferences (GSP) and is admissible duty free from those countries which are Designated Beneficiary Developing Countries for purposes of the GSP. 1/

U.S. producers and productions

At the present time there are no producers of latex mattress blanks in the United States. The single facility that produced blanks of rubber latex foam, the Sponge Rubber Products Company, situated in Shelton, Connecticut, was destroyed by fire in March 1975. A new company, Latex Foam Products, Inc., is negotiating to buy the equipment of the destroyed facility and reestablish operations in the Shelton

1/ See Executive Order 11888, Nov. 24, 1975, effective date Jan. 1, 1976.

area. The Economic Development Commission of the State of Connecticut has authorized a loan of $900,000 to Latex Foam Products, Inc.; however, this firm probably will not go into production for some months, if in fact it does start to produce.

With respect to polyurethane producers, 10 domestic chemical companies produce polyurethane compound, which is sold to some 40 large and small firms that pour the foam. Only 15 of these concerns actually ship high-density polyurethane buns (or cut pieces) to domestic mattress manufacturers. Although the domestic industry estimates that 700 million pounds of polyurethane foam will be produced in the United States in 1976, only about 49 million pounds will be of the high-density, slab-stock type that will be used for high-resiliency mattress blanks. Some 35 firms produce mattresses of polyurethane in the United States, only 6 or 8 of these produce mattresses of the high-density polyurethane type.

U.S. imports

Mattress blanks of rubber latex are not reported separately in the official statistics of the United States. TSUS item 727.8620 (formerly item 727.8080) covers several imported noncotton articles of bedding. Included under item 727.862 are mattresses, mattress blanks, and baby lounge pads. Imports, by value, of all items falling under 727.8620 were as follows:

Year	Value (1,000 dollars)
1970	181
1971	332
1972	372
1973	289
1974	269
1975	267

Information from the Customs Service indicates that rubber latex mattress blanks are being imported from Canada. It is reported that Great Britain is also a potential source.

Price comparison

Information available to the United States International Trade Commission indicates that twin-size latex foam mattress blanks (5-1/2 x 39-1/2 x 75-1 inches) are being imported with an f.o.b. foreign port value of approximately $30 to $31 per unit, whereas a competing domestically produced, high-density, high-resiliency, polyurethane mattress blank of the same dimensions has a domestic ex-factory price of about $23 per unit.

Potential impact of H.R. 11605

Should H.R. 11605 be enacted, importers of latex foam mattress blanks would realize a saving in duty of approximately $4.50 per unit on each blank imported. Such a saving would permit the latex foam mattress manufacturer that imported the blank to come nearer to meeting the prices of manufacturers of high-density polyurethane and consequently could slightly depress the demand for the domestically produced high-density polyurethane blanks and mattresses. Furthermore, suspension of the duty for 3 years might discourage U.S. manufacturers from reestablishing production of foam rubber latex in the United States.

Potential loss of revenue

Based on estimated imports of rubber latex mattress blanks in 1975, the potential loss of tariff revenues resulting from the enactment of H.R. 11605 would be approximately $10,000 annually.

July 1, 1976

UNITED STATES INTERNATIONAL
TRADE COMMISSION

MEMORANDUM TO THE COMMITTEE ON FINANCE OF THE UNITED STATES SENATE ON H.R. 12254, AN ACT TO SUSPEND THE DUTIES ON CERTAIN BICYCLE PARTS AND ACCESSORIES UNTIL THE CLOSE OF JUNE 30, 1978.

Purpose of the bill

H.R. 12254, if enacted, would amend the article description for items 912.05 and 912.10 of the appendix to the Tariff Schedules of the United States (TSUS) to read as follows (underscored words are added by the proposed legislation):

912.05	Generator lighting sets for bicycles <u>and parts thereof</u> (provided for in item 653.39, part 3F, schedule 6) . . .
912.10	Derailleurs, caliper brakes, drum brakes, three-speed hubs incorporating coaster brakes, three-speed hubs not incorporating coaster brakes, click-twist grips, click stick levers, multiple freewheel sprockets, <u>coaster brakes, alloy butted frame tubing, frame lugs, alloy cotterless crank sets, alloy rims and parts of all the foregoing</u> (provided for in item 732.36, part 5C, schedule 7) . . . .

This would have the effect of temporarily suspending the duty on the above-underscored items. Section 1(c) would change the expiration date for items 912.05 and 912.10 from 12/31/76 to 6/30/78.

Description and uses

Parts of generator lighting sets for bicycles include a number of items, such as headlamps with mounting brackets, taillights, lens and reflector units, and set screws. Except for coaster brakes, which are used principally on less expensive bicycles, the other products covered by H.R. 12254 (alloy butted frame tubing, frame lugs, alloy cotterless crank sets, alloy rims, and parts of all the foregoing) are all bicycle parts used on high-priced multispeed bicycles.

Tariff treatment

Imported parts of generator lighting sets for bicycles are currently provided for under TSUS item 653.39 at a column 1 rate of duty of 19 percent ad valorem and a column 2 rate of 45 percent ad valorem. This item is included on the list of eligible articles for purposes of the Generalized System of Preferences (GSP) 1/, and imports thereunder are duty free from those countries which are Designated Beneficiary Developing Countries. Coaster brakes, alloy butted frame tubing, frame lugs, alloy cotterless crank sets, alloy rims, and most parts of all the foregoing, are currently provided for under TSUS item 732.36 at a column 1 rate of 15 percent ad valorem and a column 2 rate of 30 percent ad valorem. Imports under item 732.36 are not included on the list of eligible articles for purposes of the GSP.

U.S. production

Trade sources indicate that there is currently no domestic production of parts of generator lighting sets for bicycles, or of coaster brakes, alloy butted frame tubing, frame lugs, alloy cotterless crank sets, alloy rims, and parts of all the foregoing. As to those products currently included under TSUS items 912.05 and 912.10, the rates of duty for which have been suspended since January 13, 1971, there continues to be no domestic production, except for derailleurs. In June 1974, a domestic firm began production of derailleurs at its Illinois facility. An official of that company stated that in 1975 the firm produced 140,000 derailleurs, and projected that the firm would produce 2 million derailleurs in 1976. However, while this official indicated that his company's derailleurs were of good quality and would improve

1/ See Executive Order 11888, November 24, 1975, effective date January 1, 1976.

in quality in the future, there is some question as to whether the domestically produced derailleurs are presently of sufficient quality to satisfy all domestic users.

U.S. imports

Imports of parts of generator lighting sets for bicycles, coaster brakes, alloy butted frame tubing, alloy cotterless crank sets, alloy rims, and parts of all the foregoing are not separately reported in the official statistics of the United States. Imports of generator lighting sets for bicycles are provided for under a "basket" provision (653.3950) covering parts of illuminating articles of base metal, other than brass. Similarly, imports of coaster brakes, alloy butted frame tubing, frame lugs, alloy cotterless crank sets, alloy rims, and parts of all the foregoing, are provided for under a "basket" provision (732.3670) covering certain parts of bicycles, not provided for elsewhere in the tariff schedules. The following tabulation shows the value of imports entered under TSUSA items 653.3950 and 732.3670 for 1971-75.

	Item 653.3950 Imports ($1,000)	Item 732.3670 Imports ($1,000)
1971-----------	4,275	12,275
1972-----------	7,245	23,833
1973-----------	7,220	29,831
1974-----------	6,634	48,076
1975-----------	5,669	18,861

West Germany, France, and Japan, which in the aggregate accounted for about one-fifth of the total imports under item 653.3950 in 1975, are the principal suppliers of parts for generator lighting sets for bicycles; however, probably only a small part of the total imports from these countries consisted of such parts. Japan, Mexico, West Germany, France, and Italy have been the principal sources of imports under item 732.3670, accounting for about 80 percent of the total value imported in 1975. Imports under this classification consist of a wide range of bicycle parts, including those parts listed in H.R. 12254. It is believed that imports of coaster brakes, alloy butted frame tubing, frame lugs, alloy cotterless crank sets, alloy rims, and parts of all the foregoing, accounted for an appreciable portion of the total value of imports under item 732.3670.

The following tabulation shows the value of duty-free imports from 1971 through 1975 under item 912.0500, generator lighting sets for bicycles; 912.1010, three-speed hubs whether or not incorporating coaster brakes; and 912.1020, derailleurs, caliper brakes, drum brakes, click twist grips, click stick levers, and multiple free wheel sprockets for 1971-75.

	Item 912.0500 Imports($1,000)	Item 912.1010 Imports($1,000)	Item 912.1020 Imports($1,000)
1971---------	1,068	2,638	11,784
1972---------	4,954	8,358	36,159
1973---------	5,263	12,378	58,997
1974---------	2,962	9,137	73,040
1975---------	1,535	2,111	17,766

In 1975, Japan and Hong Kong were the principal suppliers of imports under item 912.0500, accounting for about 61 percent; Japan was the principal source of imports under item 912.1010, accounting for 88 percent of the total; and Japan, again, was the leading supplier of imports under item 912.1020, accounting for 78 percent of the total.

France was the second most important supplier under the latter classification, accounting for 10 percent of total imports in 1975.

Potential loss of revenue

Based on imports in 1975, it is estimated that the potential loss of revenue resulting from enactment of H.R. 12254 would be approximately $1.25 million annually.

GENERAL COUNSEL OF THE
DEPARTMENT OF COMMERCE
Washington, D.C. 20230

AUG 16 1976

Honorable Russell B. Long
Chairman, Committee on Finance
United States Senate
Washington, D. C. 20510

Dear Mr. Chairman:

This is in reply to your request for the views of this Department on H.R. 12254, an Act

"To suspend the duties on certain bicycle parts and accessories until the close of June 30, 1978."

If enacted H.R. 12254 would extend from the close of December 31, 1976 until the close of June 30, 1978 existing suspension of the column-1 duties, which are accorded imports from countries receiving most-favored-nation tariff treatment, on generator lighting sets and certain specified parts for bicycles. The Act would also add parts of generator lighting sets and coaster brakes, alloy butted frame tubing, frame lugs, alloy cotterless crank sets, alloy rims, and parts of the foregoing to the specified parts presently covered by the temporary duty-free treatment.

The Department of Commerce favors the enactment of H.R. 12254. The continued duty-free importation of the parts and accessories covered in the proposed legislation is important to U.S. producers of finished bicycles in preserving their competitiveness against imported bicycles because, but for a small quantity of derailleur components, none of the parts and accessories covered in the proposed legislation is manufactured in the United States.

In the absence of the duty suspensions, imports of generator lighting sets would be subject to a duty of 19 percent *ad valorem* and the parts to a duty of 15 percent *ad valorem*. The duty suspensions were first introduced in 1971 in order to help domestic bicycle manufacturers compete with growing imports of complete foreign-made bicycles. Domestic manufacturers have taken a number of steps to increase their production and to improve their competitive position, including investments in new machinery. U.S. bicycle production, which relies heavily on the importation of duty-free parts, rose from 6.5 million units in 1971 to 10.0 million units in 1973 and 10.1 million units in 1974, but decreased sharply to 5.6 million units in 1975. Production is expected to increase to 7.4 million units in 1976.

During this period, with boom conditions in the domestic bicycle market, imports of bicycles as a share of the U.S. market rose from 26 percent (2.3 million units) in 1971 to 37 percent (5.2 million units) in 1972. However, from this high level the imports-to-consumption ratio dropped steadily to less than 24 percent (1.7 million units) in 1975 and is expected to decline to less than 20 percent in 1976.

Further, in connection with maintaining the competitiveness of domestic bicycle manufacturers, it should be noted that the great bulk of imported bicycles is subject to rates substantially lower than those of the parts covered by the duty suspensions. The two most popular import categories, accounting for 75 and 20 percent of the total quantity of bicycle imports, are currently dutiable at 5.5 percent *ad valorem* (TSUS item 732.18) and 11 percent *ad valorem* (TSUS item 732.12), respectively.

With the exception of derailleurs, the Department is unaware of any domestic production of generator lighting sets and the specified parts for bicycles. According to information obtained by the Department, there is a U.S. manufacturer of four of the normally seven parts of derailleurs used by domestic bicycle manufacturers. The production of this manufacturer, which was started in 1975, supplies parts for about 4 percent of the requirements for derailleur components in domestically produced bicycles. Until 1975, U.S. bicycle manufacturers historically depended on imports for virtually 100 percent of their derailleur component requirements. Major U.S. manufacturers state that reestablishing the 15 percent ad valorem duty on derailleurs would increase by 5 or 6 percent the consumer price of bicycles with derailleurs. It is our opinion that such an increase at this time would cause U.S. manufacturers to lose a major portion of the domestic market to import competition.

Until such time as domestic sources can produce adequate supplies of complete derailleurs to more nearly replace those historically imported, we feel that it is in the overall interest of the U.S. industry for the duty suspension on derailleurs to be continued for the short period provided in the Act.

In the event this legislation were enacted, it would have no impact on the revenues to, or the administrative costs of, this Department.

We have been advised by the Office of Management and Budget that there would be no objection to the submission of this report from the standpoint of the Administration's program.

Sincerely,

J. K. Smith

General Counsel

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