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CONSTRUCTIVE SALE PRICE FOR EXCISE TAX ON CERTAIN TRUCKS, BUSES, TRACTORS, ET CETERA

AUGUST 21 (legislative day, AUGUST 16), 1978.—Ordered to be printed

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

REPORT

[To accompany H.R. 1337]

The Committee on Finance, to which was referred the bill (H.R. 1337) relating to constructive sale price for excise tax on certain trucks, buses, tractors, etc., having considered the same, reports favorably thereon with an amendment, and an amendment to the title, and recommends that the bill as amended do pass.

I. SUMMARY

1. Constructive sale price.—H.R. 1337 prohibits the use of a manufacturer's costs as the constructive sale price for purposes of the 10-percent manufacturers excise tax on trucks, buses, highway tractors, and trailers (sec. 4061(a)).

The section 4061(a) tax applies to the price at which the manufacturer sells a taxable product. Statutory rules provide for constructive sale prices in certain cases, including sales at retail by a manufacturer (sec. 4216). In the case of a manufacturer selling at retail, the Internal Revenue Service has developed constructive prices as a percentage of the manufacturer's retail selling price.

The Service also has ruled, however, that in cases of such retail sales, if the manufacturer's actual costs in making and selling the article exceed the percentage constructive price, the costs instead will be used as the base for computing the excise tax. The use of this administratively developed "cost floor" tax base causes differing level of excise tax among manufacturers of competing articles and also creates uncertainty as to the proper amount of the excise tax at the time of the sale.

The bill provides that percentage constructive prices are to be used in cases where a manufacturer sells articles taxable under section 406

(a) at retail, and prohibits the use of manufacturer's costs as an alternative tax base in such situations.

2. Home production of beer and wine.—The committee amendment allows any adult to produce wine and (if the individual registers with the Treasury Department) to produce beer for personal and family use up to certain quantities without incurring the wine or beer excise taxes or any penalties. The maximum amounts which may be produced free of tax are 200 gallons of wine and 200 gallons of beer per year in a household in which there are two or more adults. If there is only one adult in the household, the annual limit is 100 gallons of wine and 100 gallons of beer. In addition, the bill provides that the amount of such home-brewed beer on hand in any household at any one time (including beer in process) may not exceed 30 gallons. For purposes of the wine and beer production limitations, the term "adult" means an individual who has attained 18 years of age, or the minimum age (if any) established by law applicable in the locality in which the household is situated at which wine or beer (as the case may be) may be sold to individuals, whichever age determination is higher.

3. Aerial applicators.—Present law provides an exemption from the excise taxes imposed on gasoline and special fuels if such fuels are used for farming purposes. The committee amendment to the bill provides that a cropduster who uses tax-paid fuel for farming purposes is authorized to claim the applicable excise tax repayment or credit directly, in place of the farmer, if the farmer waives his right to the refund or credit.

4. Partial rollovers of lump-sum distributions.—Under present law, an individual who is eligible to make a tax-free rollover contribution of amounts distributed from a qualified retirement plan is required to contribute the entire amount of the distribution to an IRA or to another qualified plan. The committee amendment allows an individual to make a rollover contribution of any portion of the distribution. In addition, the amendment provides a special "makeup" rule for individuals who, prior to enactment of the bill, attempted to make a rollover contribution but failed to transfer the entire amount of the distribution. Such persons are allowed to make a rollover contribution of any portion of the distribution to an IRA or to a qualified retirement plan on or before December 31, 1978 or 60 days after enactment of the amendment, whichever is later.

II. GENERAL STATEMENT

A. Constructive Sale Price for Excise Tax on Certain Trucks, Buses, Tractors, Etc. (sec. 1 of the bill and sec. 4216 of the Code)

Present law

Under present law, a manufacturers excise tax of 10 percent is imposed on the sale by a manufacturer or importer of trucks, buses, highway tractors, and their related chassis, bodies, and trailers (sec. 4061(a)).[1] Generally, the tax is based on the price at which a taxable item is sold by the manufacturer to wholesale distributors.

[1] The tax is scheduled to be reduced to 5 percent on October 1, 1979. Revenues from this tax go to the Highway Trust Fund (through September 30, 1979).

However, present law also provides for a constructive sale price if taxable articles are sold by a manufacturer or importer to other than a wholesale distributor (sec. 4216). If a manufacturer or importer sells a taxable article at retail—i.e., directly to ultimate consumers—the constructive sale price is the lower of (1) the price for which the article was sold, or (2) the highest price at which such articles are sold to wholesale distributors, as determined by the Treasury Department (sec. 4216(b)(1)).

The Internal Revenue Service has ruled that if a manufacturer sells taxable trucks, etc. at retail, the price at which such items are sold to wholesale distributors is considered to be 75 percent of the established retail price (Rev. Rul. 54–61, 1954–1 CB 259). The "established retail price" is the highest price for which a manufacturer sells, or offers to sell, an item for use by an independent purchaser who ordinarily would not be expected to buy more than one item. If a taxable item actually is never sold at its list price, because of discounts or other price modifications, the "established retail price" is the price resulting from the minimum discount off the list price (Rev. Rul. 68–519, 1968–2 CB 513).

The Service also has ruled that if a manufacturer's actual cost of making and selling a taxable item is greater than the percentage constructive price referred to above, then its actual cost is used in lieu of the percentage constructive price for purposes of computing the applicable excise tax (Rev. Ruls. 54–61 and 68–519, as noted above). This administratively developed "cost floor" rule for determining the tax base has not been enacted into the Code.

Reasons for change

When the present system of manufacturers excise taxes was enacted, in 1932, the Congress recognized that two of the fundamental tests that such taxes should meet are: "Certainly, both as to liability and amount, must be attainable in advance of the sale" and "The tax must be imposed uniformly and without discrimination." [2]

The committee has concluded that the "cost floor" rule for determining the excise tax base discriminates against low-profit-margin manufacturers who sell at retail. These manufacturers pay a larger excise tax than do their competitors who sell similar articles at wholesale, or who sell at retail, but to whom the percentage constructive price rule is applied.

It also is noted that the "cost floor" rule often produces uncertainty at the time of the sale as to the amount of the manufacturer's tax liability. This uncertainty arises because both the application of the cost floor method and the amount of the tax base determined under this method depend upon which costs are allocable to a particular product, and there may be some questions as to which costs are properly allocable to a taxable product. Thus, a manufacturer which has paid the tax

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[2] H. Rept. 708, 72d Cong., 1st sess. 31 (1932). The report further stated, as to certainty, that "It is essential that the persons who will be called upon to make returns and pay the tax to the Government must know, in advance of the sale, whether the sale is taxable and the amount of the tax liability." (Id. at p. 32.) As to uniformity, the report stated that "Each member of a competitive group must pay upon substantially the same basis as all his competitors, even though his sales methods may differ." (*Ibid.*) See also H. Rept. 481, 85th Cong., 1st sess. 21 (1957) and S. Rept. 2090, 85th Cong., 2d sess. 21–22 (1958).

based upon a percentage constructive price may be assessed a deficiency at a date long after the sale has occurred, based upon an allocation by the Service of additional costs to a particular taxable product.

The committee therefore has decided to eliminate the use of the administratively developed "cost floor" rule for determining a constructive sale price in the case of items taxable under section 4061(a) which are sold at retail.

Explanation of provision

The bill prohibits the use of a constructive sale price based upon the manufacturer's costs in all cases where trucks, buses, highway tractors, and related articles taxable under section 4061(a) are sold at retail by a manufacturer. The bill provides that the excise tax in these situations is to be determined by using a percentage constructive sale price based on the highest price for which such articles are sold by manufacturers in the ordinary course of trade. The percentage constructive sale price is to apply in the case of any such retail sale by a manufacturer.

As under present law, the Internal Revenue Service may establish percentages to be used for determining the excise tax base. However, the bill provides that the percentage constructive price is not to exceed 100 percent of the actual sale price. Under the bill, the percentage so established by the Service will be applied to the actual selling price, and not to the so-called "established retail selling price."

The committee intends that elimination of the cost floor rule in cases of the retail sales described above will not apply to situations where articles taxable under section 4061(a) are not sold, but are instead used by the manufacturer or importer. In such cases, where the use by the manufacturer is considered a taxable sale (sec. 4218), it is intended that the cost floor rule may be used as an alternative tax base.

It is also intended that no inference be drawn from this legislative action with regard to controversies between taxpayers and the Service concerning either the validity of the cost floor rule or determinations of cost for taxable transactions which occurred before the effective date of this legislation.

Effective date

This provision applies to articles sold by the manufacturer or producer on or after the first day of the first calendar quarter which begins 30 days or more after the date of enactment.

Revenue effect

The provision is estimated to reduce budget receipts by $1 million in fiscal year 1979 and by $500,000 annually thereafter. These revenues would otherwise go into the Highway Trust Fund (through September 30, 1979).

B. Excise Tax Treatment of Home Production of Beer or Wine (sec. 2 of the bill and secs. 5042 and 5053 of the Code)

Present law

Present law (sec. 5042 of the code) permits the "head of any family," after registering with the Treasury Department, to produce up to 200 gallons of wine a year for family use without payment of tax. However, a single individual who is not the head of a family is not

covered by this exemption (see Treas. Regs. 27 CFR secs. 240.540 et seq.).

The Bureau of Alcohol, Tobacco, and Firearms interprets present law (sec. 5054(a)(3)) as providing that it is illegal to brew beer in one's home for home consumption. As a result, the tax of $9 per barrel (31 gallons or less), which is imposed on the production of beer (sec. 5051(a)), is due and payable immediately upon production. In addition, the Bureau takes the position that home brewers are subject to the criminal penalties imposed by the code (sec. 5687) for liquor tax offenses that are not otherwise specifically covered.

Reasons for change

The committee believes it is appropriate to grant a limited exemption from the beer tax for the production of beer for personal and family use. The committee also believes that it is consistent with the present wine tax exemption for heads of families to provide a comparable exemption for adult individuals not now covered by this exemption.

Accordingly, the bill provides a limited exemption from the wine and beer taxes for wine and beer produced, for personal or family use (and not for sale), by adults.

Explanation of provision

Wine

The bill modifies the provisions of existing law that permit heads of families to produce wine tax-free for family use. Under the bill, the present limitation of 200 gallons of tax-free production in a calendar year is to apply if there are two or more adults in the household. If there is only one adult in the household, then 100 gallons of wine may be produced by that adult tax-free in a calendar year. The present law's requirement that any producer of wine under the family-use exemption must be a "head of any family" is repealed.

For purposes of the wine production limitations, the term "adult" means an individual who has attained 18 years of age, or the minimum age (if any) established by law applicable in the locality in which the household is situated at which wine may be sold to individuals, whichever age determination is higher.

In addition, the bill eliminates the present-law requirement that the person producing the wine must have registered with the Treasury Department.

Beer

The bill provides essentially the same rules in the case of household production of beer by adults, with the added requirement that, in order not to be subject to the beer tax, the amount of beer on hand at any one time (including beer in process) is not to exceed 30 gallons. Also, the bill requires that the producers of beer register with the Treasury Department in order to qualify under the home brewing exception.

For purposes of the beer production limitations, the term "adult" means an individual who has attained 18 years of age, or the minimum age (if any) established by law applicable in the locality in which the household is situated at which beer may be sold to individuals, whichever age determination is higher.

The bill also makes it clear that criminal penalties imposed under Federal law in connection with illegally produced beer do not apply to home production which qualifies for the exemption provided in this bill. The provisions dealing with illegally produced beer are amended to make it clear that home production of beer that does not qualify for the new exemption is illegal.

Effective date

The provision would take effect on the first day of the first calendar month which begins more than 90 days after the date of the bill's enactment.

Revenue effect

The provision is estimated to reduce budget receipts by less than $1.5 million annually, beginning with fiscal year 1979.

C. Credit or Refund of Excise Tax on Fuels Used by Aerial Applicators for Farming Purposes (section 3 of the bill and sections 6420 and 6427 of the Code)

Present law

Under present law, gasoline and special fuels used by noncommercial aviation are subject to excise taxes totaling 7 cents per gallon (secs. 4041(c) and 4081 of the Internal Revenue Code).[1] Present law provides an exemption from these taxes if the fuel is used for farming purposes (sec. 4041(f)).

The farming-use exemption applies if gasoline or special fuel is sold for use, or used, on a farm in the United States for farming purposes by the owner, tenant, or operator of the farm (sec. 4041(f), 6420(c), and 6427(c)). If the taxes have been paid, the owner, tenant, or operator may obtain a "refund" of the excise taxes, either by a payment under the excise tax system (secs. 6420 and 6427) or by a refundable income tax credit (sec. 39). The repayment and credit provsions also apply if the gasoline or other fuel is used on the farm by someone other than the owner, tenant, or operator (such as a cropduster). In the latter situations, the owner, tenant, or operator reports the number of gallons of fuel consumed on or over the farm and claims the repayment or credit (see Treas. Regs. sec. 48.6420(a)-1(c)).

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[1] Section 4081(a) imposes a manufacturers excise tax of 4 cents a gallon on gasoline. Section 4041(c)(2) imposes a retailers excise tax of 3 cents a gallon on gasoline taxable under section 4081 which is sold for use, or used, as a fuel in aircraft in noncomercial aviation. Section 4041(c)(1) imposes a retailers excise tax of 7 cents a gallon on liquids (other than gasoline) sold for use, or used, as a fuel in aircraft in noncommercial aviation. Thus, excise taxes totalling 7 cents a gallon are imposed on all fuels used by aircraft in noncommercial aviation, regardless of whether the aircraft uses only gasoline, only another liquid fuel, or some combination of liquid fuels.

The excise tax on gasoline imposed by section 4081 is scheduled to be reduced to 1½ cents a gallon on Oct. 1, 1979 (sec. 4081(b)). At that time, the excise taxes imposed by section 441(c) are scheduled to be 5½ cents a gallon (to total 7 cents a gallon on aviation fuel); the section 4041(c) taxes are then scheduled to expire on July 1, 1980 (sec. 4041(c)(5)). The revenues from these taxes on fuel used by noncomercial aviation go to the Airport and Airway Trust Fund.

Reasons for change

The present system under which farmers may obtain a refund or credit of excise taxes paid with respect to gasoline or special fuels used during agricultural spraying and cropdusting has proved, in some cases, to be burdensome for both the aircraft operator and the farmer. The aircraft operator must supply each farmowner, tenant, or operator with sufficient information concerning the number of gallons of fuel consumed by the aircraft on or over a particular farm so that the farmer may then claim the excise tax credit or repayment (sec. 6420(c)(3)(B)). In cases where the amount of crop spraying or dusting done for a particular farmer is small, the cost of making these individual determinations and of supplying the farmer with information adequate to obtain a credit or repayment of taxes by the aircraft operator frequently exceeds the applicable refund.

Accordingly, the committee has decided to modify the present procedure applicable to the farm use exemption. Under the bill, an agricultural aircraft operator, if the farmer consents, will be able to claim the excise tax repayment or credit in place of the farmer.

Explanation of provision

The bill permits aerial applicators, such as cropdusters, to claim the credit or refund of aircraft fuel taxes for fuel used on farms for farming purposes if the farmer waives his right to the credit or refund. However, the bill does not change the uses which qualify a taxpayer to claim the credit or payment; it simply permits a change in the category of persons who are entitled to claim the credit or payment. For example, fuel used in going to and from the farm is not to be considered to be used "on" the farm, and therefore the tax paid with respect to such fuel would not be eligible for the credit or payment (see Treas. Regs. § 48.6420(a)–1(c)(2)). The change made by the bill applies only to the extent that gasoline or special fuels are used for farming purposes by the aerial applicator as determined in accordance with Treasury regulations (secs. 4041(f)(1), 6420(f), and 6427(h)).

Under the bill, the Treasury Department is authorized to issue regulations as to the time, form, and manner of waivers by farmers of rights to the fuel excise tax credit or refund. The committee intends that these regulations be developed with the objective of simplifying and minimizing any burdens imposed on farmers with respect to signing waivers, and that the waiver shall not be required to include a specific computation of excise tax or the refund or credit.

Effective date

The provision applies to fuels used on or after the first calendar quarter which begins more than 90 days after the date of enactment, even if the tax was paid before the effective date. However, if the fuel was used before the effective date, the farmer (and not the aerial applicator) is entitled to the credit or refund, even if the tax is not paid by the effective date of the bill.

Revenue effect

The provision is estimated to reduce budget receipts by less than $1 million annually, beginning with fiscal year 1979. These revenues

would otherwise go into the Airport and Airway Trust Fund (through June 30, 1980).

D. Partial Rollovers of Lump Sum Distributions (sec. 4 of the bill and sec. 402 of the Code)

Present law

Under present law, a lump-sum distribution from a qualified retirement plan or a complete distribution upon termination of such plan is not includible in a plan participant's gross income if he or she makes a rollover contribution to an IRA (an individual retirement account, an individual retirement annuity, or a retirement bond) or to another qualified retirement plan within 60 days of the date of the distribution (sec. 402(a) of the code). For a contribution to qualify as a rollover contribution, the individual must contribute to the IRA or to the other qualified plan the amount of money plus all of the assets received from the qualified plan, except for an amount allocable to previous employee contributions to the qualified plan.

An employee who fails to contribute the required amount is taxed on the entire distribution from the qualified plan in the year received. (If the distribution qualifies as a lump-sum distribution, the individual may elect special 10-year income averaging.) Also under present law, assets contributed to an IRA in a nonqualified rollover constitute an excess contribution to the IRA. Accordingly, (1) a 6-percent excise tax is imposed for each year for which the excess remains (sec. 4973), (2) the excess contribution and the earnings thereon are included in gross income when distributed from the IRA (sec. 408(d)), and (3) the excess contribution and earnings thereon generally are subject to a 10-percent penalty tax if distributed before age 59½ (sec. 408(f)).

Reasons for change

The committee understands that the requirement that a rollover contribution must contain the entire amount of money and other property distributed has caused problems for plan participants who receive lump-sum distributions from qualified retirement plans. If the recipient or his or her employer makes an error in determining the amount of the rollover contribution, the rollover is disqualified, and the recipient is subject to severe tax penalties. In addition, the committee understands that persons receiving distributions of property other than money frequently have trouble finding an IRA trustee to accept the property as part of a rollover. As a result, such individuals are unable under present law to save any portion of the distribution for retirement needs on a tax-deferred basis.

Explanation of provision

The provision permits a plan participant who receives a lump-sum distribution from a qualified retirement plan or a complete distribution upon termination of a qualified retirement plan to make a rollover contribution of all or a portion of the distribution (less the amount allocable to employee contributions) to an IRA or to another qualified plan. If the individual makes a rollover contribution of less than the full distribution eligible for rollover treatment, the amount retained

will be taxed in the year of receipt as ordinary personal service income and will not be eligible for special 10-year income averaging.

In addition, the provision permits special "makeup" rollovers for individuals who, prior to enactment of the bill, received a lump-sum distribution and attempted to comply with the present-law rule which requires a rollover contribution to contain all the property distributed. Such individuals would have until the later of December 31, 1978 or the 60th day after the date of enactment of the bill to make a qualified rollover contribution of all or a portion of the property received in a lump-sum distribution. For purposes of this special makeup rollover only, an individual may contribute money in lieu of property received in the distribution to the extent the money transferred does not exceed the fair market value of the retained property on the date of distribution (or at any time within 60 days thereafter).

Effective date

The amendments made by this provision would apply with respect to taxable years beginning after December 31, 1974 (the effective date for establishment of IRA's pursuant to the Pension Reform Act of 1974).

Revenue effect

The provision is estimated to have a negligible impact on budget receipts.

III. COSTS OF CARRYING OUT THE BILL AND VOTE OF THE COMMITTEE IN REPORTING H.R. 1337, AS AMENDED

Revenue cost

In compliance with section 252(a) of the Legislative Reorganization Act of 1970, the following statement is made relative to the costs incurred in carrying out H.R. 1337, as reported by the committee. The committee estimates that this bill will result in a decrease in budget receipts of $3.5 million in fiscal year 1979 and $3 million per year thereafter.

The Treasury Department agrees with this statement.

Vote of the committee

In compliance with section 133 of the Legislative Reorganization Act of 1946, the following statement is made relative to the vote by the committee on the motion to report the bill, H.R. 1337, as amended by the committee, was ordered reported by a voice vote.

IV. REGULATORY IMPACT OF THE BILL AS REPORTED AND OTHER MATTERS TO BE DISCUSSED UNDER SENATE RULES

Regulatory impact

Pursuant to rule XXIX of the Standing Rules of the Senate, as amended by S. Res. 4 (February 4, 1977), the committee makes the following statement concerning the regulatory impact that might be incurred in carrying out the provisions of H.R. 1337, as reported by the committee.

A. Numbers of individuals and businesses who would be regulated.—The provisions of this bill affect manufacturers of trucks, buses, highway tractors, and trailers with respect to retail sales of such items; home producers of beer and wine; aerial agricultural applicators and farmers for whom such cropdusters perform services; and individuals eligible to make tax-free rollover contributions of certain lump-sum distributions from qualified retirement plans to IRAs or other qualified plans.

B. Economic impact of regulation on individuals, consumers, and businesses affected.—The provisions of the bill will eliminate certain inequities and uncertainties involved in administration of the manufacturers excise tax on trucks, buses, highway tractors, and trailers; will assist individuals who desire to produce beer or wine at home for personal or family use; will alleviate certain burdens on farmers with respect to obtaining the benefit of the excise tax exemption for fuels used during agricultural spraying and cropdusting; and will alleviate certain severe tax penalties otherwise imposed under present law on individuals who attempted to make tax-free rollover contributions of certain lump-sum distributions from qualified retirement plans but inadvertently failed to satisfy present-law requirements.

C. Impact on personal privacy.—The bill makes no changes in those provisions of Federal law relating to the personal privacy of taxpayers.

D. Determination of the amount of paperwork.—The bill will not involve significant additional paperwork for taxpayers. Section 2 of the bill eliminates the present-law requirement that home producers of tax-free wine must register with the Treasury Department. A registration requirement is imposed under the bill for home producers of tax-free beer; under present law (as interpreted by the Bureau of Alcohol, Tobacco, and Firearms), any home production of beer is subject to tax and criminal penalties. Under section 3 of the bill, a farmer will have to execute a waiver of his right to the refund or credit for tax-paid fuels used by an aerial applicator over his farm in order for the applicator to claim the excise tax repayment or credit. The committee intends that Treasury regulations as to the time, form, and manner of such waivers be developed with the objective of simplifying and minimizing any burdens imposed on farmers with respect to signing waivers.

Consultation with Congressional Budget Office on budget estimates

In accordance with section 403 of the Budget Act, the committee advises that the Director of the Congressional Budget Office has examined the committee's budget estimates (as shown in part III of this report) and agrees with the methodology used and the resulting dollar estimates for those items.

Tax expenditures

In compliance with section 308(a)(2) of the Budget Act with respect to tax expenditures, and after consultation with the Director of the Congressional Budget Office, the committee makes the following statement. The provisions contained in sections 1, 2, and 3 of the bill involve no new or increased tax expenditures. The provision of the bill relating

to partial IRA rollovers will involve a negligible change in the amount of tax expenditures for fiscal year 1979 and each fiscal year thereafter.

V. CHANGES IN EXISTING LAW MADE BY THE BILL, AS REPORTED

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

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