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ELIMINATION OF DUTY ON METHANOL IMPORTED FOR CERTAIN USES

AUGUST 1, 1974.—Ordered to be printed

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

REPORT

[To accompany H.R. 11251]

The Committee on Finance, to which was referred the bill (H.R. 11251) to amend the Tariff Schedules of the United States to provide for the duty-free entry of methanol imported for use as fuel, having considered the same, reports favorably thereon with amendments and recommends that the bill as amended do pass.

I. SUMMARY

House bill.—The House bill would provide for the duty-free treatment of methanol when imported for use in producing synthetic natural gas or for direct use as a fuel. Duties on methanol imported for other than use as a fuel would remain unaffected. The committee bill does not substantially modify the House bill, but includes an amendment unrelated to the subject matter of the House bill.

Committee amendment.—The committee amendment makes a change in the DISC provisions relating to export transactions. This provision specifies that a financing corporation is not to be prevented from qualifying as a DISC if it holds accounts receivable or evidences of indebtedness which arise by reason of the export-related transactions of a related DISC. The present tax law requires that at least 95 percent of a corporation's assets be export-related in order to qualify as a DISC. These export-related assets include accounts receivable or evidences of indebtedness which arise in connection with the export transactions of the corporation. This corporation can retain these accounts receivable or evidences of indebtedness as its only assets and continue to qualify as a DISC. However, if these accounts receivable or evidences of indebtedness are transferred to another corporation, which retains these as its only assets, this transferee corporation can-not presently qualify as a DISC. The committee provision would allow the transferee financing corporation to hold these accounts receivable or evidences of indebtedness and qualify as a DISC if they arise by reason of the export-related transactions (whether as principal or agent) of a related DISC.

II. General Statement

A DUTY-FREE TREATMENT OF METHANOL

Methanol or methyl alcohol, the subject of H.R. 11251, is currently dutiable under item 427.96 of the Tariff Schedules of the United States (TSUS) at a rate column numbered 1 duty (applicable to countries accorded most-favored-nation treatment) of 7.6¢ per gallon and under rate column numbered 2 (applicable to Communist countries except Poland and Yugoslavia) at 18¢ per gallon. The bill would make entries of methanol duty free under rate column numbered 1 (there would be no change in rate column numbered 2) when imported for use in producing synthetic natural gas or for direct use as a fuel.

Imports of both natural gas and liquefied natural gas (LNG) are serve as a supplemental energy source to both natural gas and liquefied accorded duty-free treatment. As noted above, methanol, which could natural gas, is dutiable as a chemical intermediate, methyl alcohol, under item 427.96 of the TSUS. Until recently, widespread use of imported methanol has not been economically possible, although the development of liquefied natural gas facilities in the Caribbean and the Mediterranean areas have demonstrated the feasibility of processing and transporting long distances natural gas presently being flared-off in certain petroleum-producing countries due to the absence of nearby markets. With increasing energy shortages and technological developments, it now appears that it is economically feasible in such countries as Saudi Arabia and Iran to process into methanol the natural gas which is presently being flared-off. However, the existing rate of duty of 7.6¢ per gallon on imports of methanol precludes any further development of such additional sources of energy for the U.S. market.

During public hearings on H.R. 11251 on March 4, 1974, before the House Ways and Means Committee, witnesses called attention to the fact that in such petroleum-producing countries as Saudi Arabia, Iran and Indonesia, which are remote to major energy markets, large quantities of natural gas produced in association with petroleum production are simply being flared-off and wasted. Firms in energy-consuming countries, including the United States, have been working on proposals to acquire this wasted natural gas and transport it to their energy markets. Until recently, it was believed that the only practical method of transporting natural gas from these remote producing areas was to liquefy it by refrigeration.

The production and transport of liquefied natural gas (LNG) require elaborate and expensive liquid natural gas plants and special cryogenic tankers to transport it. While this method is considered best for moving gas from such relatively near source countries as Nigeria and Venezuela, more recent research shows that a more practical and less expensive method of transporting natural gas from the more remote overseas sources is to change the gas into liquid methanol by a relatively simple chemical process.

Methanol can be transported in any tanker or vessel suitable for transporting water or gasoline. Once it reaches the energy market, it may be used directly as fuel for gas burners modified to accommodate the liquid fuel, or it may be converted into synthetic natural gas (SNG) and used to supplement the domestic supply of gas in natural gas pipelines distribution systems.

The planned process, which would remove sulfur and hydrocarbons heavier than methane from the wet natural gas, would yield "crude" methyl alcohol. "Crude" methyl alcohol would be further refined abroad or after importation into the United States to bring it to the level of purity of domestically produced methanol. Crude methyl alcohol is not presently an article of trade in the United States. Refined methyl alcohol (also called methanol) is an important chemical intermediate. In 1972, United States production of refined methyl alcohol totaled 6 billion pounds valued at almost $120 million. About 85 to 90 percent of the production was consumed in the synthesis of other chemicals; less than 10 percent was used as a solvent; and virtually none was used as a fuel. There are 12 domestic producers, including several of the largest chemical companies.

The committee wishes to emphasize that the methanol covered by this legislation and which is included in item 427.96 of the TSUS by H.R. 11251 is expressly limited to that which is imported for use in producing synthetic natural gas or for direct use as a fuel. It does not apply to methanol imported for other purposes, such as for chemical uses, which would be covered by new item 427.97 of the Tariff Schedules and would remain dutiable at the current rates of duty (7.6¢ per gallon). The committee calls attention to this because in the course of the public hearings, domestic producers of methanol for such other uses expressed some concern that the duty-free methanol imports for energy purposes be diverted to chemical use. In this regard, the committee cites general headnote 10(e) of the TSUS which will require that not only must the methanol imported duty free under item 427.96 be intended for the prescribed energy uses, but it must be actually so used and proof of such use furnished the U.S. Customs Service within three years after entry.

The committee believes that this provision and its careful administration by the Customs Service will serve to adequately prevent such diversion. In order to assure appropriate surveillance of imports under this legislation, however, your committee directs the Customs Service to notify it of the initial duty-free entry of methanol under this legislation. Such entry is not expected for several years because of plant construction and production lead times. Further, the committee directs the Customs Service to supply it specific information before January 1, 1978, relating to the volume of imports, and at that time, also to inform the committee of any difficulties or problems that may have arisen with respect to the administration and control of duty-free methanol under item 427.96.

The executive departments all support the enactment of H.R. 11251. For example, the Department of Commerce, in its report to the committee, stated as follows:

> The Department of Commerce strongly favors enactment of H.R. 11251. The proposed elimination of duty on imports

of methyl fuel will permit, in certain cases, an economically feasible and more practical alternative to the importation of LNG as a means of supplementing domestic energy supplies with fuels from producing countries which are remote to the U.S. energy market. The duty-free treatment would apply only to imports of methanol used in producing SNG or directly as fuel. There is no domestic production of methanol for use as fuel. The enactment of the proposed legislation would not change the tariff treatment presently applicable to methanol imported for use in producing chemical products which may be produced domestically and would not have an adverse effect on U.S. industry.

The committee approved two technical amendments relating to the changes in the Tariff Schedules of the United States effected by the House bill. The first amendment would indent the line item descriptions so as to bring the heading "Methyl" immediately below the other categories of alcohol subscribed by the general alcohol superior heading. The descriptions for items 427.96 and 427.97 would be indented below the Methyl heading. The second technical amendment would specify that the column 1 rates established by the House bill are to be considered rates proclaimed pursuant to trade agreement, in a manner consistent with the status of column 1 rates.

The committee received no unfavorable comments from any interested party, nor any unfavorable reports from any executive agency on the methanol provisions of the bill.

B. TRANSFERS OF ACCOUNTS RECEIVABLE TO RELATED DISC'S

Under present law, the profits of a Domestic International Sales Corporation (DISC) are not taxed to the DISC but instead are taxed to the shareholders when actually or constructively distributed to them. To qualify as a DISC, at least 95 percent of a domestic corporation's gross receipts must arise from export sale or lease transactions and other export-related investments or activities. In addition, at least 95 percent of the corporation's assets must be export-related. Included in export-related assets are accounts receivable and evidences of indebtedness held by the corporation which arose in connection with qualified export sale or lease transactions (including related and subsidiary services) of the corporation or the performance of managerial, engineering, or architectural services producing qualified export receipts by the corporation.

Accounts receivable and evidences of indebtedness can only be treated as qualified export assets if they arise by reason of transactions in which the corporation itself acted as principal or commission agent, and a corporation can qualify as a DISC even though these accounts receivable are the only assets of the corporation making the export sale. However, if these accounts receivable and evidences of indebtedness are transferred to another related corporation, they would not be treated as qualified export assets in the hands of that transferee corporation. Therefore, if these were the only assets held by the transferee corporation, it could not qualify as a DISC.

It has come to the attention of the committee that a corporation may want to have its sales operations in one DISC and its financing operations in another DISC. A corporation might adopt this corporate structure because it believes it eases its ability to receive outside financing. In view of this, the committee has adopted an amendment which enables a financing corporation to qualify as a DISC by allowing it to treat as qualified export assets the accounts receivable and evidences of indebtedness acquired as a result of the export related transactions (whether as principal or agent) of a related DISC.

This amendment applies with respect to taxable years beginning after 1973, and at the election of the taxpayer (if the election is made within 90 days after the date of the enactment of this amendment) to any taxable year beginning after 1971 and before 1974.

This amendment will have no direct effect on revenues.

III. Costs of Carrying Out the Bill and Effect on the Revenues of the Bill

In compliance with section 252(a) of the Legislative Reorganization Act of 1970, the following statement is made relative to the costs to be incurred in carrying out this bill and the effect on the revenues of the bill. The committee estimates that the temporary suspension of duties on methanol imported for use as fuel provided by the bill will not result in any additional revenue loss or administrative costs.

Similarly, the amendment permitting transfers of accounts receivable to related DISCs will have no direct effect on revenues.

IV. Vote of Committee on Reporting the Bill

In compliance with section 133 of the Legislative Reorganization Act, as amended, the following statement is made relative to the vote of the committee on reporting the bill. This bill was ordered favorably reported by the committee without a roll call vote and without objection.

V. Changes in Existing Law

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