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USE OF CERTAIN VOLATILE FRUIT-FLAVOR CONCENTRATES IN CELLAR TREATMENT OF WINE, EXCISE TAX ON REBUILT AUTO PARTS, AND DETERMINATION OF SALES PRICE OF REBUILT TELEVISION PICTURE TUBES.

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Mr. BYRD of Virginia, from the Committee on Finance, submitted the following

REPORT

[To accompany H.R. 4649]

The Committee on Finance, to whom was referred the bill (H.R. 4649) to amend the Internal Revenue Code of 1954 to authorize the use of certain volatile fruit-flavor concentrates in the cellar treatment of wine, having considered the same, report favorably thereon with amendments and recommend that the bill as amended do pass.

I. SUMMARY

Your committee has accepted the House provision without change but has added two amendments on other tax matters.

The House-passed provision amends present law so that it will be practical to produce wine by removing volatile fruit-flavor concentrate—which imparts flavor and aroma to fruits and which are normally lost in the fermentation process—from the juice before the fermentation process and then to add it back to the wine after this fermentation. This provision not only permits such a method of production, but in addition also makes it clear that this process will not be considered as making the wine an "imitation" wine. This provision is to be effective as of the beginning of the second month which starts more than 10 days after the date of enactment of this bill. The Treasury Department has indicated that it has no objection to the enactment of this provision.

One of the two amendments added by your committee repeals the 8-percent manufacturers' excise tax on rebuilt automotive parts. The other amendment your committee added makes the 10-percent manufacturers' excise tax on radio and television components inapplicable

to so much of the price of rebuilt television picture tubes as is represented by the fair market value of the used picture tube traded in. Both of these amendments are made effective as of the first calendar quarter beginning after the date of enactment of this bill.

VOLATILE FRUIT-FLAVOR CONCENTRATES

In the normal fermentation and production processes involved in the making of a wine, a large portion of the organic elements in the natural juice which impart flavor and aroma to the fruits is lost. It is possible, technically, to remove the elements giving rise to the flavor and aroma as "volatile fruit-flavor concentrates" from the fruit before the fermentation process and then to reincorporate them in the wine at, or near, the end of the production process. The resulting product in such a case tends to have a taste and bouquet more closely resembling the fresh fruit from which it is made than would otherwise be the case. The distillate process which enables producers to separate and collect the volatile highly flavored organic constituents of grapes and other fruits was developed by the Department of Agriculture and is used currently in the production of jellies and jam.

The separation and subsequent readdition of the volatile fruit-flavor concentrate has not proved feasible, however, in the case of wine, because of certain features of present law and the regulations under this law.

Present law (sec. 5381 of the code) states that natural wine is the product of the juice, or must, of sound, ripe grapes or other sound, ripe fruit. The law also permits the use of concentrated juice (sec. 5382(b)) in the production of wine although not specifically defining "concentrated juice." A ruling of the Internal Revenue Service [1] held that a concentrated juice from which the volatile fruit flavor has been removed in a volatile fruit-flavor concentrate plant could be used in the production of natural wine provided the volatile fruit-flavor concentrates are restored to the flashed or stripped juice before its removal from the volatile fruit-flavor plant. However, since the fermentation of the juice must occur in a winery, outside of the volatile fruit-flavor concentrate plant, this ruling, in effect, stops the use of flashed or stripped juice in the production of natural wine. At the same time the addition of volatile fruit-flavor concentrate after the fermentation, under the regulations under the Federal Alcohol Administration Act ordinarily results in the wine to which this was added being classified as an "imitation" wine.[2]

The use of volatile fruit-flavor concentrates to enhance the flavor and bouquet of wines will result in the development of products which vary somewhat from those which have customarily been available. However, your committee agrees with the House that there is no reason why winemakers should not be permitted to take advantage of a technological development of this type.

In view of the above considerations, this provision adds a paragraph to present law including among the specific processes permitted to be used in the production of natural wine the addition of volatile

[1] Rev. rule 57-477.

[2] Sec. 4.21(h)(1)(iii) of the Federal Alcohol Administration intoxicating liquor regulations requires wines to be designated as "imitation" if the taste, aroma, color, or other characteristics have been acquired in whole or in part by treatment with methods or materials of any kind, if the taste, aroma, color, or other characteristics of normal wine of such class or type are acquired without such treatment.

fruit-flavor concentrates. This volatile fruit-flavor concentrate must be produced from the same kind of fruit as that from which the wine was made, and, in addition, in the case of grape or berry wine, must be from the same variety of fruit. The proportion of the volatile fruit-flavor concentrate added under this provision may not exceed the proportion which the concentrate bears to the original juice from which it was extracted. The amendment does not limit the stage in the production process at which the concentrate may be added to the wine although, presumably, this usually will be added near the end of the fermentation processing. Under the amendment, volatile fruit-flavor concentrate may be added to wine made either from the whole juice or juice from which such a concentrate has been flashed or stripped. In the usual case, presumably, the wine to which the volatile fruit-flavor concentrate is added will be made from stripped or flashed juice. With the passage of this provision, it is also understood that the Treasury Department will revise the Federal Alcohol Administration intoxicating liquor regulations to remove the requirement that wine produced in the manner described above is to be labeled as "imitation" wine.

The fermentation of juice from which the volatile fruit-flavor concentrate has been removed is qualified as a process for making natural wine by a second amendment (sec. 5382(b)). The second amendment achieves this result by providing that juice, concentrated juice, or must processed at a volatile fruit-flavor concentrate plant (of the type specified in sec. 5511), is to be considered as pure juice, concentrated juice, or must, even though the volatile fruit flavor has been removed, if there is added to it—or to wine made from this juice, etc.—the identical volatile flavor removed or an equivalent quantity of volatile fruit-flavor concentrate. As in the first amendment referred to above, any fruit-flavor concentrate added must be from the same kind of fruit and, in the case of berry or grape wine, from the same variety of fruit.

Present law provides that when a volatile fruit-flavor concentrate is removed from a volatile fruit-flavor concentrate plant, the concentrate must be rendered unfit for use as a beverage before removal from the place of manufacture (sec. 5511(2) of the code.) By regulation, it has been held that a concentrate containing not more than 6 percent alcohol is, for this purpose, considered as a concentrate not fit for use as a beverage. This provision permits the withdrawal from one of these plants of a concentrate with an alcoholic content of up to 24 percent by volume where the concentrate is transferred to a bonded wine cellar for use in the production of natural wine as provided in the provisions referred to above.

The amendments made by this provision are to take effect on the first day of the second month which begins more than 10 days after the date of enactment of this bill.

The Treasury Department has informed your committee that the revisions proposed in this bill should have no effect on revenues since in practice volatile fruit-flavor concentrates are not now taxed.

III. REPEAL OF TAX ON REBUILT AUTO PARTS

Present law imposes an excise tax of 8 percent (scheduled to revert to 5 percent as of July 1, 1965) on the sale of automobile parts and accessories by the manufacturer. Under longstanding regulations,

this tax has been held to apply to rebuilt automotive parts and accessories on the grounds that the rebuilding constitutes "manufacturing." This taxable status of rebuilt parts has been recognized by Congress in that it has provided that the sales price of rebuilt automobile parts or accessories is not to include the value of a like part traded in on the rebuilt part.

Although rebuilding of automotive parts is subjected to the manufacturers' excise tax on automotive parts and accessories, the regulations make it clear that reconditioning is not. Reconditioning, as contrasted to rebuilding, is the mere disassembling, cleaning, and reassembling (including any necessary replacement of worn parts). In practice it has frequently been difficult to distinguish between reconditioning and rebuilding. This has proved particularly difficult because reconditioning or rebuilding processes have not remained static but have continued to change. As a result, there has been a continuing dispute between the rebuilding industry and the Internal Revenue Service as to what constitutes taxable and nontaxable operations. The result has led to confusion and uncertainty as to the tax status of some processes, with some rebuilders paying tax on some processes and others not paying on substantially the same processes.

In addition to the troublesome administrative problems arising in defining what constitutes a taxable operation, the large number of small rebuilders scattered throughout the country are burdened in trying to comply with the tax.

This tax also is particularly objectionable in that its distribution among consumers is undoubtedly highly regressive. Certainly more than a proportionate part of the purchasers of automotive rebuilt parts (as distinct from new parts) are made by those with relatively low incomes; thus, the impact of the tax is believed to be heavily concentrated on the lower income groups. Moreover, the purchase of rebuilt auto parts such as generators, clutches, etc. cannot be viewed as the purchase of luxury-type items.

In view of the considerations set forth above, your committee has concluded that rebuilt automotive parts should be excluded from the tax on automobile parts and accessories. Moreover, since the revenue involved in this case amounts to only approximately $8 million a year, your committee does not believe that it is necessary to await consideration of all excise taxes before acting with respect to this small, but troublesome, problem.

Your committee's amendment exempts rebuilt auto parts from this tax as of the beginning of the first calendar quarter beginning after the date of enactment of this bill.

IV. SALE PRICE OF REBUILT TELEVISION PICTURE TUBES

Present law imposes a 10-percent manufacturers' tax on radio and television components. Included in the definition of "radio and television components" are tubes, including television picture tubes.

At the present time, there is a substantial volume of business in "rebuilding" television picture tubes. In this process, the old glass tube is used but new electronic components are placed in the tube with the result that a picture tube substantially the same as the original tube can be obtained from the process. This process comes

within the definition of "manufacturing" in the same manner as does the rebuilding of automotive parts and accessories. However, the exclusion from the taxable sales price of the value of the old part traded in on the rebuilt part, which is available in the case of rebuilt auto parts, is not available in the case of television picture tubes. For that reason, the taxable price for a rebuilt tube at the present time is the charge made to the purchaser for the rebuilt tube plus the fair market value of the old tube traded in.

This gives rise to difficult administrative problems in determining the fair market value of the old tube traded in. In addition, a tax has already been paid on the value of the old tube. Only the price, over and above the value of the old tube, represents the value of new manufacturing. This was recognized in the case of rebuilt automotive parts when in 1951 the special rule was provided by Congress excluding from the taxable price of a rebuilt automotive part the fair market value of the part traded in.

In view of these considerations, your committee has amended the House bill to provide an exclusion from the taxable price in the case of rebuilt television picture tubes of the fair market value of the tubes traded in.

This exclusion is to be available with respect to articles sold on or after the beginning of the calendar quarter commencing after the date of enactment of this bill.

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