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*Taxation*

## COMMENTS ON THE TECHNICAL CHANGES ACT OF 1953

Congress contemplates a complete revision of the Internal Revenue Code in 1954. As is the situation with all technical laws, the present federal income and estate tax statutes cause many inequitable situations.<sup>1</sup> The Technical Changes Act of 1953<sup>2</sup> was passed in order to rectify the unjust applications of some sections of the Code immediately rather than allow the situation to continue an additional year or fifteen months.

The Act contains seventeen sections and applies, with one exception, to the estate and income tax.<sup>3</sup> Most of the provisions have a very limited scope, some sections being applicable probably to only one or two taxpayers. The purpose of this note is to explain briefly the change effected by each section of the Act and to show the probable reasons for the legislation.

*Income Tax*

Six of the seventeen changes brought about by this Act merely extend the time in which certain actions may be taken by a taxpayer. One of these six is Section 101, which extends Section 112(b)(7) of the Internal Revenue Code to the year 1953.

It has been the policy of Congress to encourage dissolution of personal holding companies through Section 112(b)(7).<sup>4</sup> For corporations which might be subject to the personal holding company<sup>5</sup> tax or to the tax on unreasonable accumulations of profits,<sup>6</sup> this provision can be used instead of the one which ordinarily would govern liquidations.<sup>7</sup> Under 112(b)(7) "qualified electing shareholders" (a technical term defined in the act)<sup>8</sup> can postpone present recognition of part of the gain resulting from the complete liquidation of any corporation according to a liquidation plan and a written election<sup>9</sup> within a single calendar month during 1951, 1952, 1953. In the liquidation, an individual's gain is taxed as an ordinary

<sup>1</sup> SEN. REP. NO. 685, 83d Cong., 1st Sess. 2 (1953).

<sup>2</sup> Pub. L. No. 287, 83d Cong., 1st Sess. (Aug. 15, 1953).

<sup>3</sup> Technical Changes Act of 1953, § 201, amends § 2 of an act to assist in the collection of cigarette taxes, 63 STAT. 884 (1949), 15 U.S.C. § 376 (Supp. 1952): "forward to" has been struck out and "file with" substituted.

<sup>4</sup> Jacob H. Wood, 3 T.C. 186, 188, n. 2 (1944); SEN. REP. NO. 2375, 81st Cong., 2d Sess. 63 (1950).

<sup>5</sup> INT. REV. CODE §§ 500-511.

<sup>6</sup> INT. REV. CODE § 102.

<sup>7</sup> INT. REV. CODE § 115(c).

<sup>8</sup> "Qualified electing shareholder" is further defined in U.S. Treas. Reg. 118, § 39.112(b)(7) (1953).

<sup>9</sup> Written election must be filed on Form 964 (revised) in duplicate within thirty days after the liquidation plan is adopted. U.S. Treas. Reg. 118, § 39.112(b)(7)-3 (1953).

dividend to the extent his share of the corporation's profits has accumulated after February 28, 1913. Capital gain, either long or short term, is recognized to the extent of the individual shareholder's portion of money, stock, or securities acquired by the corporation after August 15, 1950. Any excess is not recognized.<sup>10</sup>

In the case of a corporation which is not a qualified electing shareholder of the liquidating company, all gain is capital, either long or short term. It is recognized to the extent of the greater of either the stockholder's portion of cash, stock, or securities acquired by the company after August 15, 1950, or the stockholder's share of the company's profits accumulated since February 28, 1913.

With the excess profits tax threats, franchise, license, and dividend taxes in addition to those mentioned above on corporations, many small and medium sized companies have found that a partnership or proprietorship form of doing business would result in substantial tax savings. Liquidation, however, if not completed under Section 112(b)(7), might result in prohibitive taxes where gain is unrealized, as in the case of real estate, patents, trade-marks, and goodwill which have greatly increased in value.<sup>11</sup> It should be noted that this section does not eliminate the tax on gains, but merely postpones it.

An election under this section should not be made if the corporation has accumulated large earnings since 1913 since the shareholder would then incur a large dividend tax. Then too, the basis of property received will remain low for later depreciation or sale.

The application of this provision is not extensive, but it should not be overlooked in a proper case to effect postponement of substantial taxes to more advantageous periods.

. . . .

Section 113(d) of the Code was amended by the Technical Changes Act, Section 102. This amendment concerns the phrase "allowed, but not less than the amount allowable" formerly used in Section 113(b)(1)(B) in referring to depreciation of property. Its purpose in being introduced into the Code was to prevent double deductions resulting from excessive depreciation and later restoration of the correct basis after the running of the statute of limitations with subsequent additional deductions.<sup>12</sup>

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<sup>10</sup> INT. REV. CODE § 113(a)(18) provides that a qualified electing shareholder's basis is the same as the basis of the stock redeemed less the money received plus the recognized gain.

<sup>11</sup> N.Y. Times, Nov. 26, 1950, § 8, p. 4, col. 1. By dissolving corporations which own appreciated real estate, § 112(b)(7) indirectly boosts mortgage lending and sales.

<sup>12</sup> SEN. REP. No. 665, 72d Cong., 1st Sess. 20 (1932).

In *Helvering v. Virginian Hotel Corp.*<sup>13</sup> the taxpayer was allowed excessive depreciation for ten years on hotel carpets and furnishings. Later the Commissioner reduced the rates of depreciation and applied them to the depreciated basis. In several of the years in which excessive deductions had been allowed, they resulted in no tax benefit because the hotel corporation had sustained a net loss in excess of its allowed appreciation. The court applied the above phrase literally in deciding that the basis of property must be reduced by excessive depreciation allowed whether or not it produced any tax benefit.<sup>14</sup> The court admitted the harshness of its rule, but stated that "the remedy is with Congress and not the courts or the executive."<sup>15</sup>

Because of this decision Congress amended Section 113(b)(1)(B) and added Section 113(d).<sup>16</sup> The new provisions gave an election to the taxpayer until December 31, 1952, to increase the basis of property by the amount of excessive depreciation taken since February 28, 1913, which had not produced a tax benefit.<sup>17</sup> Election was to be made by rules prescribed by the Secretary, but these rules were not released until December 30, 1952, leaving one day in which to make an election.

An election, if made, applies to all property held by the taxpayer after February 28, 1913. Carryovers of net operating losses and excess profits credits are also considered in determining the tax benefit of the deduction. This amendment extended the time for making an election under the former provision until December 31, 1954, and permitted revocation of an election made before January 1, 1953, at any time prior to January 1, 1955.

The provisions benefit most those who had excessive depreciation coupled with losses in the 1930's. The high rates in recent years have made this section an important one to consider for possible tax reduction.

. . . .

Section 103 of the 1953 Act is another instance where the time limitation has been extended an additional year. An election for special treatment of certain war loss recoveries may now be made until December 31, 1953, instead of 1952.<sup>18</sup> However, if property is recovered during a tax-

<sup>13</sup> 132 F.2d 909 (4th Cir.), *aff'd*, 319 U.S. 523 (1943).

<sup>14</sup> The affirmance of the decision in effect overruled *Pittsburg Brewing Co. v. Commissioner*, 107 F.2d 155 (3d Cir. 1939), a squarely opposite holding.

<sup>15</sup> *Helvering v. Virginian Hotel Corp.*, 132 F.2d 909, 913 (4th Cir.), *aff'd*, 319 U.S. 523 (1943).

<sup>16</sup> 66 STAT. 629 (1952), 26 U.S.C. § 113(b)(1)(B) (Supp. 1952). See [1953] U.S.C. Cong. & Adm. News 4098.

<sup>17</sup> See SEN. REP. NO. 1160, 82d Cong., 2d Sess. 1 (1952). The question which the taxpayer must ask in determining his new basis is: Would the tax for the year in question have been greater but for such deduction?

<sup>18</sup> INT. REV. CODE § 127(c)(5).

able year ending after October 20, 1951, there is no present time limit. The election provided for under this section is irrevocable when made, and it applies to all years beginning after December 31, 1941.

Section 127 of the Code provides for deduction of war losses from income of the taxpayer. Because of previous litigation concerning the time when a loss actually occurs,<sup>19</sup> Congress created statutory presumptions as to the time of loss; namely, property in enemy countries is declared to be lost at the date war is declared, and property in other countries is considered lost when the enemy comes into control.<sup>20</sup> Formerly, the amount of recovery was measured by the fair market value of the property on the date of recovery. That part of the war loss deduction which did not give a tax benefit could be recovered tax free. The part that did result in a tax benefit was considered ordinary income. That part was a gain on involuntary conversion which was greater than the allowable deductions in previous years. The recognition of this latter portion of the gain depends on disposition of the proceeds of the conversion and whether they are reinvested in similar property.<sup>21</sup>

If the taxpayer had deducted his total loss on only one specific piece of property, the rules stated above work very well. However, if loss on several properties has resulted, an inequitable result may occur. Since the excess of the fair market value on the date of recovery over the adjusted basis at the date of the loss is ordinary income *to the extent of the deduction allowable in the loss year*, where two properties were lost and only one recovered, the appreciated value of the latter was balanced against the two lost properties in determining the amount of income tax benefits received from the war loss.<sup>22</sup> In other words, part of the appreciated value in property recovered was subject to ordinary tax merely because a deduction had been taken on property not recovered.

Section 341 of the Revenue Act of 1951<sup>23</sup> amended Section 127(c) of the Code to provide that the taxpayer could elect to take the recovered property at the adjusted basis on the date of loss or its fair market value on the date of recovery. This provision prevents the unjust situation described above. Section 341 also provided that if no war loss deduction was claimed or allowed on particular property, its recovery could not be taxed against other loss property on which a deduction was allowed.

Section 127 still presents some problems for future legislation.<sup>24</sup> The taxpayer must prove his cost or other basis, and in some cases the event

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<sup>19</sup> United States v. White Dental Mfg. Co., 274 U.S. 398 (1927).

<sup>20</sup> INT. REV. CODE § 127(a)(1).

<sup>21</sup> INT. REV. CODE § 112(f).

<sup>22</sup> This example is given in SEN. REP. No. 781, 82d Cong., 1st Sess. 54 (1951).

<sup>23</sup> 65 STAT. 511, 513 (1951).

<sup>24</sup> Kramer, *War Losses, Their Continuing Effect Under Section 127*, 10 N.Y.U. INST. 613, 620 (1952).

which produced the loss also destroyed the records.<sup>25</sup> The courts have had difficulty determining what constitutes a "recovery" under Section 127(d).<sup>26</sup>

. . . .

During World War II there were various provisions in the Code for tax exemption for members of the armed forces.<sup>27</sup> Several acts since the beginning of the "police action" in Korea have extended those provisions. Section 104 of the Technical Changes Act of 1953 extends the application of Section 154 of the Code from January 1, 1954, to January 1, 1955.

Section 154 of the Code, added in 1951,<sup>28</sup> provided that any member of the armed forces who dies while serving in a combat zone<sup>29</sup> need pay no tax imposed by Chapter 1 of the Code during the taxable year of his death or for any other year ending after June 24, 1950, during which decedent served at any time in a combat zone. If taxes, interest, or penalties for the period covered are due at decedent's death they need not be paid, and if paid they will be refunded. Because of the uncertainty of the duration of hostilities in the combat zone, the present Act extended the exemption until the beginning of 1955.

Also amended by this Act was a parallel provision in the estate tax law. Section 939(b) of the Code exempts from the additional estate tax which would otherwise be due, estates of decedents dying under conditions listed above. The application of that subsection is extended from January 1, 1954, to January 1, 1955. It should be noted that the exemption does not apply to the basic estate tax.

It has been ruled that in case of a member of the air force killed in action in 1952 cancellation of the income tax by reason of Section 154 does not eliminate the income on which the tax is based and thus does not require correction of the records of the Social Security Administration with regard to decedent's income.<sup>30</sup>

Under present law compensation of members of the United States armed forces which is received for service in a combat zone is excluded,<sup>31</sup>

<sup>25</sup> Benjamin Abraham, 9 T.C. 222 (1947); Ernest Adler, 8 T.C. 726 (1947).

<sup>26</sup> *Kenmore v. Commissioner*, 205 F.2d 90 (2d Cir. 1953). A house in Vienna was captured in 1941 and allowed as a loss in that year. Though achieving no actual repossession, taxpayer claimed "recovery" when the allies occupied the city on April 13, 1945. The house burned on April 30, 1945. A deduction for fire loss was disallowed because the taxpayer had not proved "recovery."

<sup>27</sup> SEN. REP. NO. 781, 82d Cong., 1st Sess. 52 (1951).

<sup>28</sup> Revenue Act of 1951, § 334, 65 STAT. 507 (1951).

<sup>29</sup> "Combat zone" is defined in INT. REV. CODE § 22(b)(13)(c) as any area which the President designates as such both by location and time

<sup>30</sup> Rev. Rul. 55, 1953-1 CUM. BULL. 259.

<sup>31</sup> INT. REV. CODE § 22(b)(13) was amended by Pub. L. No. 213, 83d Cong., 1st Sess. (Aug. 7, 1953). See [1953] U.S.C. Cong. & Adm. News 3400.

certain tax due at death is abated under Section 154; and the additional estate tax is not applied under Section 939(b). Section 345 of the Revenue Act of 1951,<sup>32</sup> which abates the income tax on certain trusts for members of the armed forces dying in the service, differs from the other provisions in that its application has been limited to decedents dying before January 1, 1948. Its scope, however, includes not only military and naval forces of the United States, but also of any member of the other United Nations. It is submitted that in the interest of simplicity all provisions dealing with this subject should be uniform in their application, both as to time and subject.

. . . .

The sixth of the one year extension provisions concerns taxation of life insurance companies under Sections 201, 203A, and 433(a)(1)(H) of the Code. Section 105 of the new Act has amended these sections, which applied in 1951 and 1952, to keep them in force during 1953.

Life insurance companies, because of the nature of their business and investments and the various legal restrictions imposed on them, are subject to special federal tax rules. In 1947 and 1948, because of the tax formula applied to them, life insurance companies generally paid no income tax. Changes in the yield of investments and in interest rates paid on reserves have modified that status somewhat.<sup>33</sup>

Section 202 of the Code<sup>34</sup> determines net taxable income for 1949 and 1950 by deducting a certain per cent of net investment income and adding to that amount  $3\frac{1}{4}\%$  of unearned premiums and unpaid losses accruing from its health and accident business. Adjustments were made for tax exempt interest and dividends received. Normal corporation tax and surtax rates applied. The percentage to be deducted was proclaimed each year by the Secretary and was the same for all companies.<sup>35</sup> This was intended to be a stopgap provision only.

A different temporary formula appeared in Section 336 of the Revenue Act of 1951.<sup>36</sup> The income tax rate is fixed at  $3\frac{3}{4}\%$  of net investment income up to \$200,000 and  $6\frac{1}{2}\%$  on the excess. Adjustments are made with respect to exempt interest, dividends received, and health and accident policy transactions.<sup>37</sup> Graduated percentages of income are taxed by this Act depending on the proportion of net investment income to the particular policy requirements.<sup>38</sup>

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<sup>32</sup> 65 STAT. 517 (1951). See note INT. REV. CODE § 162.

<sup>33</sup> SEN. REP. No. 781, 82d Cong., 1st Sess. 30 (1951).

<sup>34</sup> See 1951-2 CUM. BULL. 316.

<sup>35</sup> U.S. Treas. Reg. 118, §§ 39.202-1, 202-2 (1953).

<sup>36</sup> 65 STAT. 507 (1951).

<sup>37</sup> U.S. Treas. Reg. 118, § 39.202-2 (1953).

<sup>38</sup> INT. REV. CODE § 203A.

It must be remembered that the present tax is only temporary. It is complicated and uncertain, and there are administrative difficulties. Probably the principal advantage of the new provisions is that they were estimated to increase revenues in each year by about \$58 million over those derived under the wartime formula.<sup>39</sup> At the present time Congress is formulating a new method of taxing the life insurance industry.

. . . .

The principal effect of Section 24(c) of the Code has been to prevent the taxpayer from deciding in which year certain income is to be included by him. It provides that no deduction will be permitted for expenses or interest accrued if all three of the following conditions are present:<sup>40</sup> (1) The expenses were not paid within two and one-half months after the close of the taxable year.<sup>41</sup> (2) The payor and payee use the same accounting methods so the amount is not includible in the payee's income for that year.<sup>42</sup> (3) The payor and payee were related taxpayers within the meaning of Section 24(b).<sup>43</sup>

There is a conflict on the question whether constructive payment fulfills the first requirement. *Musselmann Hub-Brake Co. v. Commissioner*<sup>44</sup> held that there was constructive payment when a demand note was given within the required time, and thus the expense was deductible. *P. G. Lake, Inc. v. Commissioner*<sup>45</sup> stated that payment must ordinarily be made in cash. Financial ability to pay is an important factor to consider and includes credit balance as well as cash balance on the payor's books.<sup>46</sup>

Section 202 of the 1953 Act amends Section 24(c) (1) by providing that the section does not apply if the expenses are paid to or constructively received by the payee. This presents the situation where payment to the related taxpayer is taxed to him as constructively received, yet not deductible by the payor because not actually paid during the payor's taxable year or within two and one-half months thereafter.

This amendment affects taxable years beginning after December 31, 1950. However, an election may be made by the taxpayer to include any

<sup>39</sup> SEN. REP. No. 781, 82 Cong., 1st Sess. 30-32 (1951).

<sup>40</sup> *Fincher Motors, Inc.*, 43 B.T.A. 673, 676 (1941).

<sup>41</sup> *P. G. Lake, Inc. v. Commissioner*, 148 F.2d 898 (5th Cir.), *cert. denied*, 326 U.S. 732 (1945); *Cheltenham & Abington Sewerage Co.*, P-H 1942 TC MEM. DEC. ¶ 42,182, *aff'd*, 131 F.2d 863 (3d Cir. 1942).

<sup>42</sup> In *Ace Heater Mfg. Co.*, P-H 1951 TC MEM. DEC. ¶ 51,364 (1951), § 24(c) was not applicable where the accounting methods were the same.

<sup>43</sup> *Gilbert Herndon*, P-H 1948 TC MEM. DEC. ¶ 48,030 (1948), *aff'd*, 175 F.2d 55 (5th Cir. 1949) (payee was the son of the payor); *Akron Welding & Spring Co.*, 10 T.C. 715 (1948) (payee was principal stockholder of the payor corporation).

<sup>44</sup> 139 F.2d 65 (6th Cir. 1943).

<sup>45</sup> 148 F.2d 898, 900 (5th Cir.), *cert. denied*, 326 U.S. 732 (1945).

<sup>46</sup> *Nock Fire Brick Co.*, P-H 1945 TC MEM. DEC. ¶ 45,144 (1945) (ample funds available to pay officers salary held payment under statute).



year beginning after December 31, 1945, if certain conditions are met: (1) Payment must have been taken as constructively received gross income in the proper taxable year; or (2) if this was not done, written assent to collection of any deficiency for failure to include may be filed. In such case the statute of limitations is extended for one year after consent is filed. When, because of the consent the same income is included for more than one year, double taxation will be prevented by application of Section 3801 which provides for the correction of the effect of such errors in the tax law.<sup>47</sup>

. . . .

Before the enactment of the Technical Changes Act of 1953, Section 113(a)(5) of the Code, relating to the basis of property transmitted at death, provided that in the case of property transferred in trust with income and power of revocation retained the basis to the grantee would be the same as if the property had passed by will on the grantor's death. In other words, the basis would be the fair market value at the date of the grantor's death, instead of the adjusted basis in the hands of the grantor.<sup>48</sup> This provision is important in cases where the market value of the property at his death greatly exceeds the grantor's basis. Subsequent sale by the grantee where property is held with the grantor's basis might result in large taxable gains. If the basis was increased to the fair market value at grantor's death, as in this section, little or no gain might be realized.

The word "revoke" has been held to mean something different than "terminate." In *Commonwealth Trust Co. v. United States*,<sup>49</sup> the inter vivos trust was terminable but not revocable, and thus in determining the basis the value of the trust property at the date of death was held to be immaterial. The court also stated that the fact that the property was included under Internal Revenue Code Section 811(d) for estate tax purposes was immaterial since the estate tax does not need to be consistent with provisions of the income tax.<sup>50</sup>

Section 203 of the present Act amends Section 113(a)(5) to include in its scope not only a power to revoke, but power retained by the grantor to make any change in enjoyment through a power to amend, alter, or terminate a trust. Since there is no difference for estate tax purposes in a power to revoke, terminate, amend, or alter there should be none for income tax purposes.

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<sup>47</sup> See discussion of this section *infra*.

<sup>48</sup> INT. REV. CODE § 113(a)(3).

<sup>49</sup> 96 F. Supp. 712 (W.D. Pa. 1951).

<sup>50</sup> *Contra* is *Edith Hilles Dewess*, 1 T.C. 791, 796 (1943), where the court stated that Congress intended to treat as testamentary dispositions all transfers over which grantor retained control. "There is nothing to indicate that the term 'right . . . to revoke' was used in any technical sense. . . ."

This amendment reduces the "basis" conflicts between the estate and income tax laws. It is submitted that Congress in the interests of uniformity might well go further by providing that all property included in a decedent's estate for tax purposes should be given a basis of the fair market value at the date of death. Since the estate tax is paid on that valuation the new owner should have the benefit of that basis. The rule should be extended to transfers in contemplation of death<sup>51</sup> and transfers of property held in joint tenancy or in tenancy by the entirety.<sup>52</sup>

. . . .

Income of American citizens abroad is excluded from taxation generally for the purpose of stimulating foreign trade and commerce.<sup>53</sup> Before enactment of the Revenue Act of 1951 in order for the exclusion to operate a citizen had to be a bona fide resident of a foreign country for at least an entire taxable year.<sup>54</sup> The 1951 Act modified this rule by providing that any individual citizen of the United States may exclude from gross income amounts earned from personal services attributable to that period if he is present in a foreign country for 510 days in 18 consecutive months regardless of bona fide residence, and the income is not received from the United States or its agency.<sup>55</sup> Section 116(a)(2) was designed to promote in connection with the Point Four program the work in foreign countries of men with technical skills, such as engineers and managers.<sup>56</sup> This section thus allowed workers who could not establish bona fide residence under Section 116(a)(1) to benefit from the exclusions.

The provision has been abused, however. The case of *David E. Rose*<sup>57</sup> illustrates the possibilities of tax savings. In five years during the war the taxpayer while employed as an executive in Great Britain for an American motion picture company saved \$230,000 in income taxes. His salary was exempt from United States tax because of bona fide residence in Great Britain and was exempt from British tax because it was paid to him in New York. Under the 1951 Act it was not even necessary to establish bona fide residence.

The popular radio show "Duffy's Tavern" has for years been written in Puerto Rico, probably motivated in part, at least, by consequent tax

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<sup>51</sup> See *Wurlitzer v. Helvering*, 81 F.2d 928 (6th Cir. 1936).

<sup>52</sup> See *Lang v. Commissioner*, 289 U.S. 109 (1933).

<sup>53</sup> *Price v. United States*, 87 F. Supp. 901, 903 (N.D. Ill. 1949).

<sup>54</sup> Revenue Act of 1942, § 148, 56 STAT. 841 (1942).

<sup>55</sup> Revenue Act of 1951, § 321, 26 U.S.C. § 116(a)(2) (Supp. 1952).

<sup>56</sup> SEN. REP. No. 685, 83d Cong., 1st Sess. 5 (1953).

<sup>57</sup> 16 T.C. 232 (1951). Note that though the question in this case was whether there was a bona fide residence, the tax avoidance principle is equally applicable to § 116(a)(2). See Levin and Mitosky, *Tax Saving Practices of Artists and Entertainers*, 31 *Taxes* 21, 27 (1953).

savings.<sup>58</sup> The current practice of producing motion pictures in all parts of the world has been encouraged greatly by this provision.

Section 204 of the present Act plugs this loophole by limiting the exemption of Section 116(a)(2) to \$20,000 per year for the 18 month period. If that period does not include an entire taxable year in the 18 months, the exemption is reduced proportionately. The amendment applies only to amounts received on or after January 1, 1953. This \$20,000 limitation, however, applies only to Section 116(a)(2), and if the taxpayer can establish bona fide residence in a foreign country under Section 116(a)(1) there is still opportunity for tax avoidance if that country has a low income tax or none at all.

. . . .

In referring to provisions for accelerated amortization of emergency defense facilities (Section 124A of the Code) it has been stated:<sup>59</sup>

Accelerated amortization operates to encourage expansion by permitting concentration of depreciation allowances in the first few years after construction or acquisition of the facility. It is designed also to help the taxpayer finance expansion by telescoping much of the process of capital adjustment into the years immediately ahead when the chances for high income and full use of the new facilities seem good.

The policy of permitting amortization of emergency facilities has been carried over to the agriculture industry in the new Internal Revenue Code Section 124B to encourage the building or repair of corn cribs, grain bins, elevators, and public grain warehouses. Bumper grain crops in previous years have filled the nation's grain bins. To save the expense of government owned bins, farmers are encouraged to build their own storage facilities by the allowance of a write-off of their cost in a 60-month period instead of during the life of the structure. The structure may be amortized to the extent of the amount expended after December 31, 1952, and before January 1, 1957, but only the facility itself may be amortized, not the land as in Section 124A.

This section, added by Section 206 of the new Technical Changes Act, does not permit amortization by anyone except those who operate public grain warehouses or who build the facility with the intention, at the time of election to amortize, of storing grain raised by them. A subsequent purchaser may continue the amortization for the remainder of the sixty-month period.

Election to amortize may be made to begin with the month following the month of completion or with the beginning of the succeeding taxable year, and the taxpayer may terminate the amortization as of the beginning of any month by written notice to the Secretary. If the election to terminate is exercised any remaining balance may be depreciated under

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<sup>58</sup> Levin and Mitosky, *supra* note 57, at 27.

<sup>59</sup> SEN. REP. NO. 1107, 82d Cong., 2d Sess. 45 (1952).

Section 23(1) of the Code. Note that ordinary depreciation may be taken on any part of the facility which cannot be amortized. For example, only part of a structure might be used for storing grain, or only part of the expenditures might be made within the permitted time.

There has been much political controversy and some administrative difficulties with Section 124A.<sup>60</sup> Though there is an acute shortage of grain storage structures, the same political arguments might be applied to this new Section 124B. Critics might say that the purpose of this Section is to give farmers an added tax advantage or to gain their support for other legislation. Because the wording of this section is much broader than that of 124A, few administrative problems should develop.

. . . .

Tax carry-overs were introduced into the law in 1942 to permit industry to offset wartime and reconversion losses against wartime profits. Modifications of the wartime provisions have been continued to encourage new businesses.<sup>61</sup>

The Revenue Act of 1950<sup>62</sup> substituted in Section 122 of the Code for years beginning after December 31, 1949, a one year carry-back and a five year carry-forward instead of the existing two year carry-back and two year carry-forward. This afforded averaging over a longer period of time, aided new businesses which cannot use carry-backs, and reduced administrative problems involved in carry-backs.<sup>63</sup> Congress recognized an inequity in this section<sup>64</sup> and provided in the 1951 Revenue Act<sup>65</sup> that corporations formed after December 31, 1945 could carry-over in taxable years beginning in 1947 an operating loss to three succeeding taxable years instead of two, thus putting them in a competitive position with corporations formed in 1950 or later. But inequities still remained in Section 122(b).

Section 205(a) of the new Technical Changes Act applies only to corporations on a fiscal year basis which were at a tax disadvantage under the former acts. If a corporation which began business before 1945 sustained a loss for a year beginning in 1947 and ending in 1948, it may carry-forward to a third taxable year that proportion of the loss which is equal to the proportionate number of days of the taxable year falling after December 31, 1947. Similarly, if a corporation's first taxable year began in 1949 it can carry forward to a fourth and fifth succeeding year the part of the loss proportionate to the number of days in the loss year

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<sup>60</sup> Green, *How to Treat Amortization of Emergency Facilities*, 10 N.Y.U. INST. 599 (1952).

<sup>61</sup> Bate, *A Critique of Section 122*, 26 TAXES 297 (1948).

<sup>62</sup> Revenue Act of 1950, § 215(b)(2)(B), 64 STAT. 938 (1950).

<sup>63</sup> SEN. REP. NO. 2375, 81st Cong., 2d Sess. 62 (1950).

<sup>64</sup> SEN. REP. NO. 781, 82d Cong., 1st Sess. 57 (1951).

<sup>65</sup> Revenue Act of 1951, § 330(b), 65 STAT. 505 (1951).

falling after December 31, 1949. This amendment puts fiscal year corporations on the same terms as calendar year companies with respect to carry-overs.

A short taxable year is treated the same way as a full taxable year under Section 122.<sup>66</sup> Thus Section 205(b) of this Act provides that in the case of the reorganization of a railroad corporation, if the taxable year of the predecessor ended within the taxable year of the successor corporation, an extra year for the carry-forward is allowed.

### *Estate Tax*

Section 811 of the Internal Revenue Code determines the inclusions in the estate of a decedent for estate tax purposes.

The effect of Section 207 of the new 1953 Act is to free from any possibility of estate tax under Section 811(c) all transfers made prior to March 4, 1931, in which the transferor reserved the right to receive income for life.

The situation first became important in *May v. Heiner*,<sup>67</sup> where the court held such a transfer not to be within the estate tax. The next year Congress by joint resolution declared the property includible.<sup>68</sup> It was held in *Hasset v. Welch*<sup>69</sup> that the provision was not intended to be retroactive. *May v. Heiner* was overruled in 1949 by *Commissioner v. Estate of Church*,<sup>70</sup> which held that a transfer of property in 1924 with income reserved for life was taxable to the estate of the grantor who died in 1939. A dissent in that case stated:<sup>71</sup>

In reliance upon a long-settled course of legislative and judicial construction, donors have made property arrangements that should not now be upset summarily with no stronger reasons for doing so than that former courts and the Congress did not interpret the legislation in the same way as this Court now does.

Congress agreed with that dissent, and the Technical Changes Act of 1949<sup>72</sup> superseded the *Church* case, providing that such transfer would not be includible if decedent died after February 10, 1939,<sup>73</sup> and before January 1, 1951. (Church died on December 11, 1939.) Since the *Church* case had in effect overruled *Hasset v. Welch*, and the 1949 Act was applicable only to this limited period, all other estates not within that

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<sup>66</sup> *Young v. United States*, 103 F. Supp. 12 (W.D. Ark. 1952), *aff'd*, 203 F.2d 686 (8th Cir. 1953).

<sup>67</sup> 281 U.S. 238 (1940).

<sup>68</sup> 46 STAT. 1516 (1931); see SEN. REP. NO. 685, 83d Cong., 1st Sess. 8 (1953).

<sup>69</sup> 303 U.S. 303, 307 (1938); SEN. REP. NO. 831, 81st Cong., 1st Sess. 7 (1949).

<sup>70</sup> 335 U.S. 632 (1949).

<sup>71</sup> *Id.* at 652-53.

<sup>72</sup> Technical Changes Act of 1949, § 7b, 63 STAT. 895-6 (1949).

<sup>73</sup> This is the date of the approval of the Internal Revenue Code. See 53 STAT. iii (1939).

period were subject to the rule in the *Church* case — clearly an unintended, unjust result. The provisions of the 1953 Act thus eliminate completely the effect of the *Church* decision.

Congress did not provide for extension of the statute of limitations in pre-1939 estates, stating that no hardship is involved except in cases being litigated at the time of the *Church* decision,<sup>74</sup> for which it has provided that refund will be given if application is made by August 15, 1954.

. . . .

Another Section 811 amendment is effected by Section 208 of this Act. In 1939 the Supreme Court in *Estate of Sanford v. Commissioner*<sup>75</sup> and in its companion case of *Rasquin v. Humphreys*<sup>76</sup> held that where a trust settlor created an irrevocable trust retaining power to change the beneficiaries, an incomplete gift was made, and no gift tax would apply until the power to change beneficiaries was released. Section 811(d) includes the corpus of such trusts in the grantor's estate. Release of the power at the time of those decisions meant a gift tax on the current value of the trust, thus creating a hardship in some cases.

To remove this hardship Section 1000(e) of the Code was added by the Revenue Act of 1943.<sup>77</sup> As amended<sup>78</sup> it provides for the tax free release of such powers after January 1, 1940, and before January 1, 1948, thereby excluding the corpus of the trust from estate tax under Section 811(d). If the power was not released in accordance with the 1943 provision the full value was includible in the grantor's estate.

The present Act, applicable to decedents dying after December 31, 1950, provides that property transferred with the reserved power shall not be included in estates of decedents who were under a mental disability to release such power from September 30, 1947, until the date of death. This amendment prevents certain decedents from being penalized because of this disability. The decedent must be mentally disabled in fact during the whole period, and a legal declaration of incompetence is not necessarily controlling.<sup>79</sup>

. . . .

The scope of Section 209 of the 1953 Act is extremely limited in its effect on Section 811(g) of the Internal Revenue Code. It applies only to the estates of decedents who died after January 10, 1941, and before October 22, 1942, leaving life insurance payable to irrevocable beneficiaries under which decedent had a reversionary interest not exceeding five per cent of the policy value and which did not arise by the express

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<sup>74</sup> SEN. REP. No. 685, 83d Cong., 1st Sess. 8 (1953).

<sup>75</sup> 308 U.S. 39 (1939).

<sup>76</sup> 308 U.S. 54 (1939).

<sup>77</sup> Revenue Act of 1943, § 502(a), 58 STAT. 71 (1944).

<sup>78</sup> Pub. L. No. 112, 80th Cong., 1st Sess. § 2(a), 61 STAT. 178 (1947).

<sup>79</sup> SEN. REP. No. 685, 83d Cong., 1st Sess. 9 (1953).

terms of the policy. Nor does the new section apply if all of decedent's policies did not total more than \$40,000, and if decedent possessed any "legal incidents of ownership" after January 10, 1941.<sup>80</sup>

The inclusion of life insurance in an estate has long been a troublesome problem. The government on January 10, 1941, issued new definite rules intended to clarify the tests for includibility of insurance proceeds.<sup>81</sup> Insurance payable to other beneficiaries in excess of \$40,000 was taxable, (1) to the extent taken out by decedent on his own life after January 10, 1941; and (2) to the extent taken out by decedent on his own life on or before January 10, 1941, *and* with respect to which he possessed any legal incidents of ownership after such date.

The Revenue Act of 1942, Section 404,<sup>82</sup> specifically applying only to decedents dying after October 21, 1942, excluded insurance paid to beneficiaries if (1) decedent paid no premiums, and (2) had no incidents of ownership. Premiums paid before January 11, 1941, on insurance in which decedent had no incidents of ownership were not treated as paid by decedent. However, there was no provision which excluded a reversion as an incident of ownership. For example, if the insured named his wife irrevocable beneficiary on a policy paid up before 1941 and named his estate to receive the proceeds if she predeceased him, the proceeds would be includible in his estate.

In the case of *Estate of Speigel v. Commissioner*,<sup>83</sup> under state law the decedent had a right of reverter in an inter vivos trust. The chances of the property reverting were less than 1½ out of 100, but the entire trust corpus was included in decedent's estate, increasing the tax by \$450,000. As a result of this decision Congress in 1950<sup>84</sup> modified Section 404 of the 1942 Act to include in the gross estate a reversionary interest (1) if it exceeded five percent of the value of the policy, and (2) arose by the express terms of the policy or other instrument. This amendment was an equitable adjustment to the problem except in one respect: It was limited by the 1942 Act, which applied only to decedents dying after October 21, 1942. The present Technical Changes Act merely extends the 1950 amendment to the period from January 10, 1941, to October 21, 1942.

. . . .

An already complex provision of the estate tax law, Section 812(e), is complicated even more by Section 210 of the Technical Changes Act of 1953.

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<sup>80</sup> See U.S. Treas. Reg. 105, § 81.27(c) (1943).

<sup>81</sup> T.D. 5032, 1941-1 CUM. BULL. 427.

<sup>82</sup> Revenue Act of 1942, § 404, 56 STAT. 944 (1942).

<sup>83</sup> 335 U.S. 701 (1949).

<sup>84</sup> Revenue Act of 1950, § 503, 64 STAT. 962 (1950).

The Revenue Act of 1948<sup>85</sup> added the marital deduction provision to the Code. It affected estates of decedents dying after December 31, 1947 by allowing, among other things, a tax free transfer in trust to the surviving spouse of a general power of appointment. To qualify, the power must include the right of unrestricted disposition either during life or by will.<sup>86</sup>

It came to the attention of Congress that certain decedents who died after December 31, 1947, and on or before April 2, 1948, the enactment date, had substantially fulfilled the requirements for the power of appointment to qualify for the marital deduction except that the transfer was not *in trust*.<sup>87</sup> The new amendment provides that in those cases the requirement of a transfer in trust should be waived, the reason being that estates should not be penalized for failure to meet a merely technical requirement. Then too, the decedent would surely have qualified had he not died before the enactment date, April 2, 1948.<sup>88</sup> An election to take advantage of this amendment may be made within one year of the date of its enactment, *i.e.*, until August 15, 1954.

. . . .

Section 211 of the new Act added paragraphs (6) and (7) to Section 3801 of the Code. The latter section provides in certain described instances for corrections of an erroneous tax result which otherwise would be barred by the statute of limitations in instances where an inconsistent position is maintained by the taxpayer or the Commissioner.

Paragraphs (6) and (7) apply where there has been *no* inconsistent position taken. Paragraph (6) provides that if a determination under the law disallows to the taxpayer a deduction which should have been allowed either in a different year or to a related taxpayer, then an adjustment will be made. Two criteria are necessary: (1) The determination must have become final on or after June 1, 1952. (2) The claim for credit must not have been barred at the time the taxpayer first claimed in writing that he was entitled to the deduction for the year in which it was disallowed.

Under paragraph (7) if a determination under the tax law excludes from gross income in one year an item which is includible either in another taxable year or by a related taxpayer, then an adjustment will be made. Two requirements must be met: (1) The determination must have become final on or after June 1, 1952. (2) Assessment of a deficiency for the other taxable year must not have been barred at the time the Secretary first maintained in a deficiency notice that the item should have been included in the income of that other taxable year.

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<sup>85</sup> Revenue Act of 1948, § 361, 62 STAT. 117 (1948).

<sup>86</sup> INT. REV. CODE, § 812(e)(1)(F).

<sup>87</sup> SEN. REP. NO. 685, 83d Cong., 1st Sess. 10 (1953).

<sup>88</sup> *Ibid.*