TREASURY DEPARTMENT

OFFICE OF TREASURER OF THE UNITED STATES

Emergency relief, 1941, administrative expenses: The Secretary of the Treasury may transfer, with the approval of the Director of the Bureau of the Budget, not to exceed $65,000 from the appropriation "Emergency relief, Treasury, Bureau of Accounts, administrative expenses, 1941" (referred to in section 5 (a) of the Emergency Relief Appropriation Act, fiscal year 1941, as "Office of Commissioner of Accounts and Deposits and Division of Bookkeeping and Warrants") to the appropriation "Emergency Relief, Treasury, Office of the Treasurer, administrative expenses, 1941", contained in the same section of such Act. Transfer of funds. 54 Stat. 617.

BUREAU OF CUSTOMS

Refunds and drawbacks, customs, 1941: For an additional amount for the refund or payment of customs collections or receipts, and for the payment of debentures or drawbacks, bounties, and allowances as authorized by law, fiscal year 1941, $11,800,000. 54 Stat. 60.

SEC. 2. This Act may be cited as the "Urgent Deficiency Appropriation Act, 1941". Short title.

Approved, March 1, 1941.

[CHAPTER 10]

AN ACT

To amend certain provisions of the Internal Revenue Code relating to the excess profits tax, and for other purposes.

March 7, 1941
[H. R. 3531]
[Public Law 10]

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That this Act may be cited as the "Excess Profits Tax Amendments of 1941". Excess Profits Tax Amendments of 1941.

SEC. 2. UNUSED EXCESS PROFITS CREDIT.

(a) Section 710 (b) (3) of the Internal Revenue Code is amended to read as follows: 54 Stat. 975. 26 U. S. C. § 710 (b) (3).

"(3) UNUSED EXCESS PROFITS CREDIT.—The amount of the excess profits credit carry-over for the taxable year, computed in accordance with subsection (c)."

(b) COMPUTATION OF EXCESS PROFITS CREDIT CARRY-OVER.—Section 710 of the Internal Revenue Code is amended by adding at the end thereof the following new subsection: 54 Stat. 975. 26 U. S. C. § 710.

"(c) EXCESS PROFITS CREDIT CARRY-OVER.—

"(1) DEFINITION OF UNUSED EXCESS PROFITS CREDIT.—The term 'unused excess profits credit' means the excess, if any, of the excess profits credit for any taxable year beginning after December 31, 1939, over the excess profits net income for such taxable year, computed on the basis of the excess profits credit applicable to such taxable year. *Post*, p. 701.

"(2) COMPUTATION OF EXCESS PROFITS CREDIT CARRY-OVER.—The excess profits credit carry-over for any taxable year shall be the sum of the following:

"(A) The unused excess profits credit for the first preceding taxable year; and

"(B) The unused excess profits credit for the second preceding taxable year reduced by the amount, if any, by which the excess profits net income for the first preceding taxable year exceeds the sum of—

"(i) the excess profits credit for such first preceding taxable year, plus

"(ii) the unused excess profits credit for the third preceding taxable year."

SEC. 3. ABNORMAL DEDUCTION IN BASE PERIOD.

54 Stat. 978, 979. 26 U. S. C. § 711 (b) (1).

Sections 711 (b) (1) (G), (H), and (I), of the Internal Revenue Code are amended to read as follows:

"(G) Dividends Received.—The credit for dividends received shall apply, without limitation, to dividends on stock of domestic corporations;

"(H) Payment of Judgments, and So Forth.—Deductions attributable to any claim, award, judgment, or decree against the taxpayer, or interest on any of the foregoing, if abnormal for the taxpayer, shall not be allowed, and if normal for the taxpayer, but in excess of 125 per centum of the average amount of such deductions in the four previous taxable years, shall be disallowed in an amount equal to such excess;

"(I) Intangible Drilling and Development Costs.—Deductions attributable to intangible drilling and development costs paid or incurred in or for the drilling of wells or the preparation of wells for the production of oil or gas, and for development costs in the case of mines, if abnormal for the taxpayer, shall not be allowed, and if normal for the taxpayer, but in excess of 125 per centum of the average amount of such deductions in the four previous taxable years, shall be disallowed in an amount equal to such excess; and

"(J) Abnormal Deductions.—Under regulations prescribed by the Commissioner, with the approval of the Secretary, for the determination, for the purposes of this subparagraph, of the classification of deductions—

"(i) Deductions of any class shall not be allowed if deductions of such class were abnormal for the taxpayer, and

"(ii) If the class of deductions was normal for the taxpayer, but the deductions of such class were in excess of 125 per centum of the average amount of deductions of such class for the four previous taxable years, they shall be disallowed in an amount equal to such excess.

"(K) Rules for Application of Subparagraphs (H), (I), and (J).—For the purposes of subparagraphs (H), (I), and (J)—

"(i) If the taxpayer was not in existence for four previous taxable years, then such average amount specified in such subparagraphs shall be determined for the previous taxable years it was in existence and the succeeding taxable years which begin before the beginning of the taxpayer's second taxable year under this subchapter. If the number of such succeeding years is greater than the number necessary to obtain an aggregate of four taxable years there shall be omitted so many of such succeeding years, beginning with the last, as are necessary to reduce the aggregate to four.

"(ii) Deductions shall not be disallowed under such subparagraphs unless the taxpayer establishes that the abnormality or excess is not a consequence of an increase in the gross income of the taxpayer in its base period or a decrease in the amount of some other deduction in its base period, and is not a consequence of a change at any time in the type, manner of operation, size, or condition of the business engaged in by the taxpayer.

"(iii) The amount of deductions of any class to be disallowed under such subparagraphs with respect to

any taxable year shall not exceed the amount by which the deductions of such class for such taxable year exceed the deductions of such class for the taxable year for which the tax under this subchapter is being computed."

SEC. 4. COMPUTATION OF AVERAGE BASE PERIOD NET INCOME.

(a) Section 713 (a) (1) of the Internal Revenue Code is amended by striking out "subsection (b)" and inserting in lieu thereof "subsection (d)", and by striking out "subsection (c)" wherever occurring therein and inserting in lieu thereof "subsection (g)". 54 Stat. 980. 26 U. S. C. § 713 (a) (1).

(b) Section 713 (b) of the Internal Revenue Code is amended to read as follows: 54 Stat. 980. 26 U. S. C. § 713 (b).

"(b) BASE PERIOD.—

"(1) DEFINITION.—As used in this section the term 'base period'—

"(A) If the corporation was in existence during the whole of the forty-eight months preceding the beginning of its first taxable year under this subchapter, means the period commencing with the beginning of its first taxable year beginning after December 31, 1935, and ending with the close of its last taxable year beginning before January 1, 1940; and

"(B) In the case of a corporation which was in existence during only part of the forty-eight months preceding the beginning of its first taxable year under this subchapter, means the forty-eight months preceding the beginning of its first taxable year under this subchapter.

"(2) DIVISION INTO HALVES.—For the purposes of subsections (d) and (f) the base period of the taxpayer shall be divided into halves, the first half to be composed of one-half the entire number of months in the base period and to begin with the beginning of the base period.

"(c) DEFICIT IN EXCESS PROFITS NET INCOME.—For the purposes of this section the term 'deficit in excess profits net income' with respect to any taxable year means the amount by which the deductions plus the credit for dividends received exceeded the gross income. For the purposes of this subsection in determining whether there was such an excess and in determining the amount thereof, the adjustments provided in section 711 (b) (1) shall be made. 54 Stat. 977. 26 U. S. C. § 711 (b) (1). *Post*, p. 701.

"(d) AVERAGE BASE PERIOD NET INCOME—DETERMINATION.—

"(1) DEFINITION.—For the purposes of this section the average base period net income of the taxpayer shall be the amount determined under subsection (e), subject to the exception that if the aggregate excess profits net income for the last half of its base period, reduced by the aggregate of the deficits in excess profits net income for such half, is greater than such aggregate so reduced for the first half, then the average base period net income shall be the amount determined under subsection (f), if greater than the amount determined under subsection (e).

"(2) For the purposes of subsections (e) and (f), if the taxpayer was in existence during only part of the 48 months preceding the beginning of its first taxable year under this subchapter, its excess profits net income—

"(A) for each taxable year of twelve months (beginning with the beginning of its base period) during which it was not in existence, shall be an amount equal to 8 per centum of the excess of—

"(i) the daily invested capital for the first day of the taxpayer's first taxable year beginning after December 31, 1939, over

"(ii) an amount equal to the same percentage of such daily invested capital as is applicable under section 720 in reduction of the average invested capital of the preceding taxable year;

54 Stat. 985.
26 U. S. C. § 720.

"(B) for the taxable year of less than twelve months consisting of that part of the remainder of its base period during which it was not in existence, shall be the amount ascertained for a full year under subparagraph (A), multiplied by the number of days in such taxable year of less than twelve months and divided by the number of days in the twelve months ending with the close of such taxable year.

"(3) In no case shall the average base period net income be less than zero.

"(4) For the computation of average base period net income in the case of certain reorganizations, see section 742.

54 Stat. 992.
26 U. S. C. § 742.

"(e) AVERAGE BASE PERIOD NET INCOME—GENERAL AVERAGE.—The average base period net income determined under this subsection shall be determined as follows:

"(1) By computing the aggregate of the excess profits net income for each of the taxable years of the taxpayer in the base period, reduced, if for more than one of such taxable years there was a deficit in excess profits net income, by the sum of such deficits, excluding the greatest;

"(2) By dividing the amount ascertained under paragraph (1) by the total number of months in all such taxable years; and

"(3) By multiplying the amount ascertained under paragraph (2) by twelve.

"(f) AVERAGE BASE PERIOD NET INCOME—INCREASED EARNINGS IN LAST HALF OF BASE PERIOD.—The average base period net income determined under this subsection shall be determined as follows:

"(1) By computing, for each of the taxable years of the taxpayer in its base period, the excess profits net income for such year, or the deficit in excess profits net income for such year;

"(2) By computing for each half of the base period the aggregate of the excess profits net income for each of the taxable years in such half, reduced, if for one or more of such years there was a deficit in excess profits net income, by the sum of such deficits. For the purposes of such computation, if any taxable year is partly within each half of the base period there shall be allocated to the first half an amount of the excess profits net income or deficit in excess profits net income, as the case may be, for such taxable year, which bears the same ratio thereto as the number of months falling within such half bears to the entire number of months in such taxable year; and the remainder shall be allocated to the second half;

"(3) If the amount ascertained under paragraph (2) for the second half is greater than the amount ascertained for the first half, by dividing the difference by two;

"(4) By adding the amount ascertained under paragraph (3) to the amount ascertained under paragraph (2) for the second half of the base period;

"(5) By dividing the amount found under paragraph (4) by the number of months in the second half of the base period and by multiplying the result by twelve;

"(6) The amount ascertained under paragraph (5) shall be the average base period net income determined under this subsection, except that the average base period net income determined under this subsection shall in no case be greater than

the highest excess profits net income for any taxable year in the base period. For the purpose of such limitation if any taxable year is of less than twelve months, the excess profits net income for such taxable year shall be placed on an annual basis by multiplying by twelve and dividing by the number of months included in such taxable year.

"(7) For the purposes of this subsection, the excess profits net income for any taxable year ending after May 31, 1940, shall not be greater than an amount computed as follows:

"(A) By reducing the excess profits net income by an amount which bears the same ratio thereto as the number of months after May 31, 1940, bears to the total number of months in such taxable year; and

"(B) By adding to the amount ascertained under subparagraph (A) an amount which bears the same ratio to the excess profits net income for the last preceding taxable year as such number of months after May 31, 1940, bears to the number of months in such preceding year. The amount added under this subparagraph shall not exceed the amount of the excess profits net income for such last preceding taxable year.

"(C) If the number of months in such preceding taxable year is less than such number of months after May 31, 1940, by adding to the amount ascertained under subparagraph (B) an amount which bears the same ratio to the excess profits net income for the second preceding taxable year as the excess of such number of months after May 31, 1940, over the number of months in such preceding taxable year bears to the number of months in such second preceding taxable year."

(c) Section 713 (c) of the Internal Revenue Code is amended by striking out "(c)" and inserting in lieu thereof "(g)". 54 Stat. 981; 26 U. S. C. § 713 (c).

(d) Section 743 (a) of the Internal Revenue Code is amended by striking out "section 713 (c)" and inserting in lieu thereof "section 713 (g)". 54 Stat. 994. 26 U. S. C. § 743 (a).

SEC. 5. ABNORMALITIES IN INCOME IN TAXABLE PERIOD.

Section 721 of the Internal Revenue Code is amended to read as follows: 54 Stat. 986. 26 U. S. C. § 721.

"SEC. 721. ABNORMALITIES IN INCOME IN TAXABLE PERIOD.

"(a) DEFINITIONS.—For the purposes of this section—

"(1) ABNORMAL INCOME.—The term 'abnormal income' means income of any class includible in the gross income of the taxpayer for any taxable year under this subchapter if it is abnormal for the taxpayer to derive income of such class, or, if the taxpayer normally derives income of such class but the amount of such income of such class includible in the gross income of the taxable year is in excess of 125 per centum of the average amount of the gross income of the same class for the four previous taxable years, or, if the taxpayer was not in existence for four previous taxable years, the taxable years during which the taxpayer was in existence.

"(2) SEPARATE CLASSES OF INCOME.—Each of the following subparagraphs shall be held to describe a separate class of income:

"(A) Income arising out of a claim, award, judgment, or decree, or interest on any of the foregoing; or

"(B) Income constituting an amount payable under a contract the performance of which required more than 12 months; or

"(C) Income resulting from exploration, discovery, prospecting, research, or development of tangible property, patents, formulae, or processes, or any combination of the foregoing, extending over a period of more than 12 months; or

"(D) Income includible in gross income for the taxable year rather than for a different taxable year by reason of a change in the taxpayer's accounting period or method of accounting; or

"(E) In the case of a lessor of real property, income included in gross income for the taxable year by reason of the termination of the lease; or

"(F) Income consisting of dividends on stock of foreign corporations, except foreign personal holding companies.

All the income which is classifiable in more than one of such subparagraphs shall be classified under the one which the taxpayer irrevocably elects. The classification of income of any class not described in subparagraphs (A) to (F), inclusive, shall be subject to regulations prescribed by the Commissioner with the approval of the Secretary.

"(3) NET ABNORMAL INCOME.—The term 'net abnormal income' means the amount of the abnormal income less, under regulations prescribed by the Commissioner with the approval of the Secretary, (A) 125 per centum of the average amount of the gross income of the same class determined under paragraph (1), and (B) an amount which bears the same ratio to the amount of any direct costs or expenses, deductible in determining the normal-tax net income of the taxable year, through the expenditure of which such abnormal income was in whole or in part derived as the excess of the amount of such abnormal income over 125 per centum of such average amount bears to the amount of such abnormal income.

"(b) AMOUNT ATTRIBUTABLE TO OTHER YEARS.—The amount of the net abnormal income that is attributable to any previous or future taxable year or years shall be determined under regulations prescribed by the Commissioner with the approval of the Secretary. In the case of amounts otherwise attributable to future taxable years, if the taxpayer either transfers substantially all its properties or distributes any property in complete liquidation, then there shall be attributable to the first taxable year in which such transfer or distribution occurs (or if such year is previous to the taxable year in which the abnormal income is includible in gross income, to such latter taxable year) all amounts so attributable to future taxable years not included in the gross income of a previous taxable year.

"(c) COMPUTATION OF TAX FOR CURRENT TAXABLE YEAR.—The tax under this subchapter for the taxable year, in which the whole of such abnormal income would without regard to this section be includible, shall not exceed the sum of:

"(1) The tax under this subchapter for such taxable year computed without the inclusion in gross income of the portion of the net abnormal income which is attributable to any other taxable year, and

"(2) The aggregate of the increase in the tax under this subchapter which would have resulted for each previous taxable year to which any portion of such net abnormal income is attributable, computed as if an amount equal to such portion had been included in the gross income for such previous taxable year.

"(d) COMPUTATION OF TAX FOR FUTURE TAXABLE YEAR.—The amount of the net abnormal income attributable to any future taxable year shall, for the purposes of this subchapter, be included in the gross income for such taxable year. The tax under this subchapter for such future taxable year shall not exceed the sum of—

"(1) the tax under this subchapter for such future taxable year computed without the inclusion in excess profits net income of the portion of such net abnormal income which is attributable to such year, and

"(2) the decrease in the tax under this subchapter for the previous taxable year in which the whole of such abnormal income would without regard to this section be includible, which resulted by reason of the exclusion of the whole or a part of the abnormal income from the gross income for such previous taxable year; but the amount of such decrease shall be diminished by the aggregate of the increases in the tax under this subchapter which have resulted for the taxable years intervening between such previous taxable year and such future taxable year because of the inclusion in the gross income of the portions of such net abnormal income attributable to such intervening years."

SEC. 6. ABNORMAL BASE PERIOD EARNINGS.

Section 722 of the Internal Revenue Code is amended to read as follows: 54 Stat. 986. 26 U. S. C. § 722.

"SEC. 722. ADJUSTMENT OF ABNORMAL BASE PERIOD NET INCOME.

"(a) GENERAL RULE.—In the case of a taxpayer whose first taxable year under this subchapter begins in 1940, if the taxpayer establishes—

"(1) that the character of the business engaged in by the taxpayer as of January 1, 1940, is different from the character of the business engaged in during one or more of the taxable years in its base period (as defined in section 713 (b) (1)); or *Ante*, p. 19.

"(2) that in one or more of the taxable years in such base period normal production, output, or operation was interrupted or diminished because of the occurrence of events abnormal in the case of such taxpayer; and

"(3) the amount that would have been its average base period net income—

"(A) if the character of the business as of January 1, 1940, had been the same during each of the taxable years of such base period; and

"(B) if none of the abnormal events referred to in paragraph (2) had occurred; and

"(C) if in each of such taxable years none of the items of gross income had been abnormally large, and none of the items of deductions had been abnormally small; and

"(4) that the amount established under paragraph (3) is greater than the average base period net income computed under section 713 (d) or section 742, as the case may be, *Ante*, p. 19; *post*, p. 30.

then the amount established under paragraph (3) shall be considered as the average base period net income of the taxpayer for the purposes of this subchapter. 54 Stat. 992. 26 U. S. C. § 742.

"(b) RULES FOR APPLICATION OF SUBSECTION (a).—For the purposes of subsection (a)—

"(1) High prices of materials, labor, capital, or any other agent of production, low selling price of the product of the taxpayer, or low physical volume of sales owing to low demand for such product or for the output of the taxpayer, shall not be considered as abnormal.

"(2) The character of the business engaged in by the taxpayer as of January 1, 1940, shall be considered different from the character of the business engaged in during one or more of the taxable years in its base period only if—

"(A) there is a difference in the products or services furnished; or

"(B) there is a difference in the capacity for production or operation; or

"(C) there is a difference in the ratio of nonborrowed capital to total capital; or

"(D) the taxpayer was in existence during only part of its base period; or

"(E) the taxpayer acquired, before January 1, 1940, all or part of the assets of a competitor, with the result that the competition of such competitor was eliminated or diminished.

"(3) The average base period net income determined under subsection (a) (3) shall be computed in the same manner as provided in section 713 (d), except paragraphs (2) and (4), but for such purposes computing excess profits net income and deficit in excess profits net income on the basis of the assumptions made in subsection (a) (3).

Ante, p. 19

"(4) If subsection (a) (1), or both subsections (a) (1) and (a) (2) are applicable to any taxpayer, its average base period net income under subsection (a) (3) shall not exceed the excess profits net income (as computed for the purposes of subsection (a) (3)) for the last taxable year in such base period. For the purposes of this paragraph, if such last taxable year is of less than twelve months, the excess profits net income for such taxable year shall be placed on an annual basis by multiplying by twelve and dividing by the number of months included in such taxable year.

Post, p. 701.

"(c) LIMITATION ON APPLICATION OF GENERAL RULE.—This section shall not be applicable unless—

"(1) the tax under this subchapter for the taxable year computed without reference to this section, exceeds 6 per centum of the taxpayer's normal-tax net income for such year; and

"(2) the application of this section would result in a diminution of the tax otherwise payable under this subchapter for the taxable year by more than 10 per centum thereof.

"(d) EXTENT OF REDUCTION IN TAX UNDER THIS SECTION.—The application of this section shall not reduce the tax payable under this subchapter for the taxable year below 6 per centum of the taxpayer's normal-tax net income for such year. The tax under this subchapter computed with the application of subsection (a) shall be increased by an amount equal to 10 per centum of the tax computed without reference to this section.

"(e) APPLICATION FOR RELIEF UNDER THIS SECTION.—The taxpayer shall compute its tax and file its return under this subchapter without the application of this section. The benefits of this section shall not be allowed unless the taxpayer, within six months from the date prescribed by law for the filing of its return, makes application therefor in accordance with regulations to be prescribed by the Commissioner with the approval of the Secretary, except that if the Commissioner in the case of any taxpayer with respect to the tax liability of any taxable year—

"(1) issues a preliminary notice stating a deficiency in the tax imposed by this subchapter such taxpayer may, within ninety days after the date of such notice, make such application, or

"(2) mails a notice of deficiency (A) without having previously issued a preliminary notice thereof or (B) within ninety days after the date of such preliminary notice, such taxpayer may claim the benefits of this section in its petition to the Board or in an amended petition in accordance with the rules of the Board.

If the application is not filed within six months after the date prescribed by law for the filing of the return, the application of this section shall not reduce the tax otherwise determined under this subchapter by an amount in excess of the amount of the deficiency finally determined under this subchapter without the application of this section. If the average base period net income has been determined under subsection (a) for any taxable year, the Commissioner may, by regulations approved by the Secretary, prescribe the extent to which the limitations prescribed by this subsection may be waived for the purpose of determining the tax under this subchapter for a subsequent taxable year."

SEC. 7. CONSOLIDATED RETURNS OF INSURANCE COMPANIES OTHER THAN LIFE OR MUTUAL.

Section 730 (e) (6) of the Internal Revenue Code is amended to read as follows: 54 Stat. 990. 26 U. S. C. § 730 (e) (6).

"(6) Insurance companies subject to taxation under section 201 or 207." 53 Stat. 71, 74. 26 U. S. C. §§ 201, 207.

SEC. 8. INCORPORATION OF PARTNERSHIP OR SOLE PROPRIETORSHIP.

(a) Section 740 (a) (1) (C) of the Internal Revenue Code is amended by striking out "owned by such other corporation." and inserting in lieu thereof: 54 Stat. 991. 26 U. S. C. § 740 (a) (1) (C).

"owned by such other corporation, or

"(D) Substantially all the properties of a partnership in an exchange to which section 112 (b) (5), or so much of section 112 (c) or (e) as refers to section 112 (b) (5), or to which a corresponding provision of a prior revenue law, is or was applicable." 53 Stat. 37, 39. 26 U. S. C. §§ 112 (b) (5), 112 (c) or (e).

(b) Section 740 (b) (4) of the Internal Revenue Code is amended by striking out the period at the end thereof and inserting in lieu thereof a semicolon and the following: 54 Stat. 991. 26 U. S. C. § 740 (b) (4).

"or

"(5) In the case of a transaction specified in subsection (a) (1) (D), the partnership whose properties were acquired."

(c) Section 740 of the Internal Revenue Code is amended by inserting at the end thereof the following new subsection: 54 Stat. 991. 26 U. S. C. § 740.

"(h) SOLE PROPRIETORSHIP.—For the purposes of sections 740 (a) (1) (D), 740 (b) (5), and 742 (g), a business owned by a sole proprietorship shall be considered a partnership."

(d) Section 742 of the Internal Revenue Code is amended by inserting at the end thereof the following new subsection: 54 Stat. 992. 26 U. S. C. § 742.

"(g) In the case of a partnership which is a component corporation by virtue of section 740 (b) (5), the computations required by this Supplement shall be made, under rules and regulations prescribed by the Commissioner with the approval of the Secretary, as if such partnership had been a corporation. For the purpose of such computations, in making the adjustment for income taxes required by section 711 (b) (1) (A), the partnership so regarded as a corporation shall be considered as having distributed all its net income as a dividend." *Supra.* 54 Stat. 977. 26 U. S. C. § 711 (b) (1) (A). *Post*, p. 701.

SEC. 9. PROCEDURAL PROVISIONS.

54 Stat. 975, 991.

Part 1 of subchapter E of chapter 2 of the Internal Revenue Code is amended by inserting at the end thereof the following new section:

"SEC. 732. REVIEW OF ABNORMALITIES BY BOARD OF TAX APPEALS.

"(a) PETITION TO THE BOARD.—If a claim for refund of tax under this subchapter for any taxable year is disallowed in whole or in part by the Commissioner, and the disallowance relates to the application of section 711 (b) (1) (H), (I), (J), or (K), section 721, or section 722, relating to abnormalities, the Commissioner shall send notice of such disallowance to the taxpayer by registered mail. Within ninety days after such notice is mailed (not counting Sunday or a legal holiday in the District of Columbia as the ninetieth day) the taxpayer may file a petition with the Board of Tax Appeals for a redetermination of the tax under this subchapter. If such petition is so filed, such notice of disallowance shall be deemed to be a notice of deficiency for all purposes relating to the assessment and collection of taxes or the refund or credit of overpayments.

Ante, pp. 18, 21, 23. 54 Stat. 986. 26 U. S. C. §§ 721, 722.

"(b) DEFICIENCY FOUND BY BOARD IN CASE OF CLAIM.—If the Board finds that there is no overpayment of tax in respect of any taxable year in respect of which the Commissioner has disallowed, in whole or in part, a claim for refund described in subsection (a) and the Board further finds that there is a deficiency for such year, the Board shall have jurisdiction to determine the amount of such deficiency and such amount shall, when the decision of the Board becomes final, be assessed and shall be paid upon notice and demand from the collector.

"(c) FINALITY OF DETERMINATION.—If in the determination of the tax liability under this subchapter the determination of any question is necessary solely by reason of section 711 (b) (1) (H), (I), (J), or (K), section 721, or section 722, the determination of such question shall not be reviewed or redetermined by any court or agency except the Board."

Ante, pp. 18, 21, 23.

SEC. 10. CAPITALIZATION OF ADVERTISING, ETC., EXPENDITURES.

54 Stat. 975, 991.

(a) Part 1 of subchapter E of chapter 2 of the Internal Revenue Code is amended by inserting at the end thereof the following new section:

"SEC. 733. CAPITALIZATION OF ADVERTISING, ETC., EXPENDITURES.

"(a) ELECTION TO CHARGE TO CAPITAL ACCOUNT.—For the purpose of computing the excess profits credit, a taxpayer may elect, within six months after the date prescribed by law for filing its return for its first taxable year under this subchapter, to charge to capital account so much of the deductions for taxable years in its applicable base period on account of expenditures for advertising or the promotion of good will, as, under rules and regulations prescribed by the Commissioner with the approval of the Secretary, may be regarded as capital investments. Such election must be the same for all such taxable years, and must be for the total amount of such expenditures which may be so regarded as capital investments. In computing the excess profits credit, no amount on account of such expenditures shall be charged to capital account:

"(1) For taxable years in the base period unless the election authorized in subsection (a) is exercised, or

"(2) For any taxable year prior to the beginning of the base period.

"(b) EFFECT OF ELECTION.—If the taxpayer exercises the election authorized under subsection (a)—

"(1) The net income for each taxable year in the base period shall be considered to be the net income computed with such deductions disallowed, and such deductions shall not be considered as having diminished earnings and profits. This paragraph shall be retroactively applied as if it were a part of the law applicable to each taxable year in the base period; and

"(2) The treatment of such expenditures as deductions for a taxable year in the base period shall, for the purposes of section 734 (b) (2), be considered treatment which was not correct under the law applicable to such year."

Post, p. 28.

(b) AMENDMENT TO CHAPTER 1.—Section 23 (a) of the Internal Revenue Code is amended by adding at the end thereof a new paragraph, applicable to taxable years beginning after December 31, 1939, reading as follows:

53 Stat. 12.
26 U. S. C. § 23 (a).

"(3) EXPENDITURES FOR ADVERTISING AND GOOD WILL.—If a corporation has, for the purpose of computing its excess profits credit under chapter 2E, claimed the benefits of the election provided in section 733, no deduction shall be allowable under paragraph (1) to such corporation for expenditures for advertising or the promotion of good will which, under the rules and regulations prescribed under section 733 (a), may be regarded as capital investments."

54 Stat. 975.
Ante, p. 26.

SEC. 11. ADJUSTMENT IN CASE OF INCONSISTENT POSITION.

54 Stat. 975, 991.

Part 1 of subchapter E of chapter 2 of the Internal Revenue Code is amended by inserting at the end thereof the following new section:

"SEC. 734. ADJUSTMENT IN CASE OF POSITION INCONSISTENT WITH PRIOR INCOME TAX LIABILITY.

"(a) DEFINITIONS.—For the purposes of this section—

"(1) TAXPAYER.—The term 'taxpayer' means any person subject to a tax under the applicable revenue Act.

"(2) INCOME TAX.—The term 'income tax' means an income tax imposed by chapter 1 or chapter 2A of this title; Title I and Title IA of the Revenue Acts of 1938, 1936, and 1934; Title I of the Revenue Acts of 1932 and 1928; Title II of the Revenue Acts of 1926 and 1924; Title II of the Revenue Acts of 1921 and 1918; Title I of the Revenue Act of 1917; Title I of the Revenue Act of 1916; or section II of the Act of October 3, 1913; a war profits or excess profits tax imposed by Title III of the Revenue Acts of 1921 and 1918; or Title II of the Revenue Act of 1917; or an income, war profits, or excess profits tax imposed by any of the foregoing provisions, as amended or supplemented.

53 Stat. 4, 104.
26 U. S. C. §§ 1, 500.

"(3) PRIOR TAXABLE YEAR.—A taxable year beginning after December 31, 1939, shall not be considered a prior taxable year.

"(b) CIRCUMSTANCES OF ADJUSTMENT.—

"(1) If—

"(A) in determining at any time the tax of a taxpayer under this subchapter an item affecting the determination of the excess profits credit is treated in a manner inconsistent with the treatment accorded such item in the determination of the income-tax liability of such taxpayer or a predecessor for a prior taxable year or years, and

"(B) the treatment of such item in the prior taxable year or years consistently with the determination under this sub-

chapter would effect an increase or decrease in the amount of the income taxes previously determined for such taxable year or years, and

"(C) on the date of such determination of the tax under this subchapter correction of the effect of the inconsistent treatment in any one or more of the prior taxable years is prevented (except for the provisions of section 3801) by the operation of any law or rule of law (other than section 3761, relating to compromises),

53 Stat. 471, 462.
26 U. S. C. §§ 3801, 3761.

then the correction shall be made by an adjustment under this section. If in a subsequent determination of the tax under this subchapter for such taxable year such inconsistent treatment is not adopted, then the correction shall not be made in connection with such subsequent determination.

"(2) Such adjustment shall be made only if there is adopted in the determination a position maintained by the Commissioner (in case the net effect of the adjustment would be a decrease in the income taxes previously determined for such year or years) or by the taxpayer with respect to whom the determination is made (in case the net effect of the adjustment would be an increase in the income taxes previously determined for such year or years) which position is inconsistent with the treatment accorded such item in the prior taxable year or years which was not correct under the law applicable to such year.

"(c) METHOD AND EFFECT OF ADJUSTMENT.—(1) The adjustment authorized by subsection (b), in the amount ascertained as provided in subsection (d), if a net increase shall be added to, and if a net decrease shall be subtracted from, the tax otherwise computed under this subchapter for the taxable year with respect to which such inconsistent position is adopted.

"(2) If more than one adjustment under this section is made because more than one inconsistent position is adopted with respect to one taxable year under this subchapter, the separate adjustments, each an amount ascertained as provided in subsection (d), shall be aggregated, and the aggregate net increase or decrease shall be added to or subtracted from the tax otherwise computed under this subchapter for the taxable year with respect to which such inconsistent positions are adopted.

"(3) If all the adjustments under this section, made on account of the adoption of an inconsistent position or positions with respect to one taxable year under this subchapter, result in an aggregate net increase, the tax imposed by this subchapter shall in no case be less than the amount of such aggregate net increase.

"(d) ASCERTAINMENT OF AMOUNT OF ADJUSTMENT.—In computing the amount of an adjustment under this section there shall first be ascertained the amount of the income taxes previously determined for each of the prior taxable years for which correction is prevented. The amount of each such tax previously determined for each such taxable year shall be (1) the tax shown by the taxpayer, or by the predecessor, upon the return for such prior taxable year, increased by the amounts previously assessed (or collected without assessment) as deficiencies, and decreased by the amounts previously abated, credited, refunded, or otherwise repaid in respect of such tax; or (2) if no amount was shown as the tax by such taxpayer or such predecessor upon the return, or if no return was made by such taxpayer or such predecessor, then the amounts previously assessed (or collected without assessment) as deficiencies, but such amounts previously assessed, or collected without assessment, shall be decreased by the amounts previously abated, credited, refunded, or otherwise

repaid in respect of such tax. There shall then be ascertained the increase or decrease in each such tax previously determined for each such year which results solely from the treatment of the item consistently with the treatment accorded such item in the determination of the tax liability under this subchapter. To the increase or decrease so ascertained for each such tax for each such year there shall be added interest thereon computed as if the increase or decrease constituted a deficiency or an overpayment, as the case may be, for such prior taxable year. There shall be ascertained the difference between the aggregate of such increases, plus the interest attributable to each, and the aggregate of such decreases, plus the interest attributable to each, and the net increase or decrease so ascertained shall be the amount of the adjustment under this section with respect to the inconsistent treatment of such item."

SEC. 12. ADMISSIBLE ASSETS OF DEALERS IN SECURITIES.

(a) Section 720 (a) (1) (A) of the Internal Revenue Code is amended to read as follows: 54 Stat. 985. 26 U. S. C. § 720 (a) (1) (A).

"(A) Stock in corporations except stock in a foreign personal-holding company, and except stock which is not a capital asset; and"

(b) Section 711 (a) (2) (A) is amended by inserting after "companies" a period and the following: "This subparagraph shall not apply to dividends on stock which is not a capital asset". 54 Stat. 976. 26 U. S. C. § 711 (a) (2) (A).

SEC. 13. ALLOWANCE OF EXCESS PROFITS CREDIT.

Section 712 of the Internal Revenue Code is amended to read as follows: 54 Stat. 979. 26 U. S. C. § 712.

"SEC. 712. EXCESS PROFITS CREDIT—ALLOWANCE.

"(a) DOMESTIC CORPORATIONS.—In the case of a domestic corporation which was in existence before January 1, 1940, the excess profits credit for any taxable year shall be an amount computed under section 713 or section 714, whichever amount results in the lesser tax under this subchapter for the taxable year for which the tax under this subchapter is being computed. In the case of all other domestic corporations the excess profits credit for any taxable year shall be an amount computed under section 714. (For allowance of excess profits credit in case of certain reorganizations of corporations, see section 741.) 54 Stat. 980, 981. 26 U. S. C. §§ 713, 714. *Ante*, p. 19. *Post*, p. 30.

"(b) FOREIGN CORPORATIONS.—In the case of a foreign corporation engaged in trade or business within the United States or having an office or place of business therein, the first taxable year of which under this subchapter begins on any date in 1940, which was in existence on the day forty-eight months prior to such date and which at any time during each of the taxable years in such forty-eight months was engaged in trade or business within the United States or had an office or place of business therein, the excess profits credit for any taxable year shall be an amount computed under section 713 or section 714, whichever amount results in the lesser tax under this subchapter for the taxable year for which the tax under this subchapter is being computed. In the case of all other foreign corporations the excess profits credit for any taxable year shall be an amount computed under section 714.

"(c) EFFECT OF DISCLAIMER OF CREDIT.—If the taxpayer states in its return for the taxable year under this subchapter that it disclaims the use of the credit computed under section 713 or the use of the

credit computed under section 714, the credit so disclaimed shall not, for the purposes of the internal revenue laws, be applicable to the computation of the tax under this subchapter for such taxable year."

SEC. 14. EXCESS PROFITS CREDIT OF ACQUIRING CORPORATIONS.

54 Stat. 992. 26 U. S. C. § 741.

Section 741 of the Internal Revenue Code is amended to read as follows:

"SEC. 741. ALLOWANCE OF EXCESS PROFITS CREDIT.

"(a) ALLOWANCE.—In the case of a taxpayer which is an acquiring corporation which was in existence on the date of the beginning of its base period, the excess profits credit for any taxable year shall be an amount computed under section 713 or section 714, whichever amount results in the lesser tax under this subchapter for the taxable year for which the tax under this subchapter is being computed.

54 Stat. 980, 981. 26 U. S. C. §§ 713, 714. *Ante*, p. 19.

"(b) EFFECT OF DISCLAIMER OF CREDIT.—If the taxpayer states in its return for the taxable year under this subchapter that it disclaims the use of the credit computed under section 713 or the use of the credit computed under section 714, the credit so disclaimed shall not, for the purposes of the internal revenue laws, be applicable to the computation of the tax under this subchapter for such taxable year."

SEC. 15. AVERAGE BASE PERIOD NET INCOME OF ACQUIRING CORPORATIONS.

54 Stat. 992. 26 U. S. C. § 742.

So much of section 742 of the Internal Revenue Code as follows the section heading and precedes the beginning of subsection (a) is amended to read as follows:

"In the case of a taxpayer which is an acquiring corporation the excess profits credit of which is allowed under section 741, its average base period net income (for the purpose of the credit computed under section 713) if the taxpayer was actually in existence before January 1, 1940, shall, at the election of the taxpayer made in its return for the taxable year, be computed as follows, and if the taxpayer was not actually in existence before such date, shall be computed as follows, in lieu of the method provided in section 713:".

Supra.

54 Stat. 980. 26 U. S. C. § 713. *Ante*, p. 19.

SEC. 16. COMPUTATION OF CREDITS ON RETURNS.

54 Stat. 989. 26 U. S. C. § 729 (b).

Section 729 (b) of the Internal Revenue Code is amended by striking out "(b) RETURNS.—" and inserting in lieu thereof the following:

"(b) RETURNS.—

"(1) COMPUTATION OF EXCESS PROFITS CREDITS.—In the case of a taxpayer which under section 712 or section 741 is entitled to have the excess profits credit computed under section 713 or section 714, whichever results in the lesser tax under this subchapter, the return under this subchapter for any taxable year shall contain computations of two tentative taxes, one with the credit computed under section 713 and one with the credit computed under section 714; and the return shall contain all information which the Commissioner, by regulations prescribed by him with the approval of the Secretary, may prescribe as necessary for such computations. If the taxpayer states in such return that it disclaims the use of one of such credits in the computation of the tax under this subchapter for the taxable

Ante, p. 29; *supra*.

54 Stat. 980, 981. 26 U. S. C. §§ 713, 714. *Ante*, p. 19.

year, the computation and information based on such credit may be omitted from the return.

"(2) NO RETURN REQUIRED.—".

SEC. 17. EFFECTIVE DATE.

The amendments made by this Act shall be effective as of the date of enactment of the Excess Profits Tax Act of 1940.

54 Stat. 975, 1018. 26 U. S. C. §§ 710-752.

Approved, March 7, 1941.

[CHAPTER 11]

AN ACT

Further to promote the defense of the United States, and for other purposes.

March 11, 1941
[H. R. 1776]
[Public Law 11]

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That this Act may be cited as "An Act to Promote the Defense of the United States".

An Act to Promote the Defense of the United States.
Post, p. 236.

SEC. 2. As used in this Act—

"Defense article."

(a) The term "defense article" means—

(1) Any weapon, munition, aircraft, vessel, or boat;

(2) Any machinery, facility, tool, material, or supply necessary for the manufacture, production, processing, repair, servicing, or operation of any article described in this subsection;

(3) Any component material or part of or equipment for any article described in this subsection;

(4) Any agricultural, industrial or other commodity or article for defense.

Such term "defense article" includes any article described in this subsection: Manufactured or procured pursuant to section 3, or to which the United States or any foreign government has or hereafter acquires title, possession, or control.

"Defense information."

(b) The term "defense information" means any plan, specification, design, prototype, or information pertaining to any defense article.

Powers of the President.

SEC. 3. (a) Notwithstanding the provisions of any other law, the President may, from time to time, when he deems it in the interest of national defense, authorize the Secretary of War, the Secretary of the Navy, or the head of any other department or agency of the Government—

Manufacture, etc., of defense articles for designated governments.

(1) To manufacture in arsenals, factories, and shipyards under their jurisdiction, or otherwise procure, to the extent to which funds are made available therefor, or contracts are authorized from time to time by the Congress, or both, any defense article for the government of any country whose defense the President deems vital to the defense of the United States.

Disposal.

(2) To sell, transfer title to, exchange, lease, lend, or otherwise dispose of, to any such government any defense article, but no defense article not manufactured or procured under paragraph (1) shall in any way be disposed of under this paragraph, except after consultation with the Chief of Staff of the Army or the Chief of Naval Operations of the Navy, or both. The value of defense articles disposed of in any way under authority of this paragraph, and procured from funds heretofore appropriated, shall not exceed $1,300,000,000. The value of such defense articles shall be determined by the head of the department or agency concerned or such other department, agency or officer as shall be designated in the manner provided in the rules and regulations issued hereunder. Defense articles procured from funds hereafter appropriated to any department or agency of the Government,

Limitation on value.
Post, p. 813.

Defense articles procured from future appropriations.