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Comments

Internal Revenue Code Section 4061(b), Manufacturers' Excise Tax on Parts and Accessories of Motor Vehicles*

SUMMARY

"The present excise taxes, for the most part, were initially levied as emergency revenue-raising measures at the time of the Korean War, or World War II, or the depression of the 1930's. As a result, they were not developed on any systematic basis and are often discriminatory in their application to the taxed industries or to purchasers of the taxed products."¹

Born of crisis and nurtured by crises, Internal Revenue Code Section 4061(b), dealing with manufacturers excise tax on motor vehicle parts and accessories, together with its predecessors, from a modest and innocuous start in 1932 (Appendix A), developed by 1964 into an all-encompassing monster. This development, legislatively reflected in a mass of amendments over the years, adminis-

* *Editor's Note:* The author of the Comment which follows has recommended that Section 4061(b), and particularly 4061(b)(2), of the Internal Revenue Code be revised to exempt light truck parts and accessories from the imposition of the excise tax now prescribed by that section. Representative Alphonzo Bell from California, with whom the matter has been discussed, has volunteered to introduce legislation to that end.

1. H. Rep. No. 433, 89th Cong., 1st Sess., 1965 U.S. Code Cong. and Ad. News 1645.

tratively in regulations of the Internal Revenue Service, and judicially via the case law route, peaked in 1964.

In 1964 Congress took an important first step in attenuating the scope of the section. On October 13, 1964, it enacted Public Law Number 88-653 removing the tax on rebuilt parts and accessories. This was accomplished by adding Section 4063(c) to the Internal Revenue Code.²

From there it was all down hill. In 1965 Congress removed the tax on all auto parts and accessories,³ thereby, retaining it only on truck and bus parts and accessories. The statute has existed essentially in this truncated form until the present time.

It should be noted that the tax was removed from auto parts and accessories in 1964 and 1965, but the tax on the automobile itself continued in force until 1971. In 1971 the tax imposed on automobiles was removed.⁴ Hence, the sequence of events was that first auto parts were excluded from the tax imposition, and then the vehicle exclusion came into being. The Revenue Act of 1971, additionally, excluded light-duty trucks from imposition of the tax. Light-duty trucks were defined as those "having a gross vehicle weight of 10,000 pounds or less (as determined under regulations prescribed by the Secretary or his delegate)."⁵ Basically, this covered the popular one half and three quarter ton pickups.⁶

The legislative intent behind the exclusion of the light trucks was that such trucks really, to a substantial degree, fulfill the function of the passenger automobile in that they are used as a means of personal transportation.⁷

In light of the above, it would be both logical and sensible for the tax to be removed from the replacement parts and accessories associated with light trucks. Incongruously, however, as Section 4061(b) exists today, despite the fact that light trucks are not taxed (nor are the parts or accessories taxed when they are on the trucks

2. "Under regulations prescribed by the Secretary or his delegate, the tax imposed under section 4061(b) shall not apply in the case of rebuilt parts or accessories." Int. Rev. Code of 1954, § 4063(c).

3. Pub. L. No. 89-44, § 201(b)(2).

4. Pub. L. No. 92-178, § 401.

5. Int. Rev. Code of 1954, § 4061(a)(2).

6. H. Rep. No. 92-533, 92nd Cong., 1st Sess., 1971 U.S. Code Cong. and Ad. News 1966.

7. *Id.*, at 1826, 1831.

at the time of the original sale), light truck parts and accessories sold subsequently *are* excise taxed.

This is an anomalous situation in that automobiles and/or their parts and accessories are exempt from the manufacturers excise tax. Light trucks also have been excluded by the 1971 Act because they are used like automobiles. Therefore, they are treated like automobiles for excise tax purposes. The replacement parts and after-market accessories for light trucks, however, continue to be taxable.

This is especially puzzling when one recognizes that, historically, the tendency has always been to impose the tax on the vehicle first and then on the parts and accessories. On the removal side, the pattern has been to remove the tax on the parts and accessories sooner than on the vehicle. The truck situation is contra to that pattern.

At any rate, Section 4061(b) currently imposes the tax on the parts and accessories of light trucks and of heavy trucks and buses. Section 4061(a) imposes the tax only on heavy trucks and buses. Viewed in an historical light, it would be appropriate for the Congress to repeal Part I of Subchapter A of Chapter 32 of 26 United States Code. This would eliminate the manufacturers excise tax from all motor vehicles, their parts, and accessories. As a practical matter, Section 4063 of the Internal Revenue Code of 1954, an exemption section, has already exempted certain trucks and buses.⁸

At the very least, to correct the exclusion omission vis-a-vis light trucks, Section 4061(b) (2) should be amended to read as follows:

(2) No tax shall be imposed under this subsection upon any part or accessory which is suitable for use (and ordinarily is used) on or in connection with, or as a component part of, [any article enumerated in subsection (a) (2)], any chassis or body for a passenger automobile, any chassis or body for a trailer or semi-trailer suitable for use in connection with a passenger automobile, or a house trailer.

The bracketed portion inserted into the present section as shown would accomplish the purpose and would effect the suggested correction.

INTRODUCTION AND EARLY HISTORY

During the depression, by Acts of June 6, 1932 (Appendix A), Congress enacted Section 606 which provided an excise tax to be imposed upon "automobile truck chassis and automobile truck bodies (including in both cases parts or accessories therefor sold

8. See § 4063(a).

on or in connection therewith or with the sale thereof), 2 per centum." The tax was imposed upon those articles sold by "the manufacturer, producer, or importer" at two percent "of the price for which so sold." (Appendix A).

Even in this essentially simple form, the statute portended some of the problems that were to arise later. The tax was a "manufacturer's" tax. What and who is a "manufacturer," for example, and what is "the price for which so sold?" Subsequent Code sections and cases have dealt extensively, and eventually not entirely satisfactorily, with these questions.

The Revenue Act of 1938, expanded Section 606 by amendment, differentiated between trucks and passenger automobiles as to rate of tax (two percent on the former, and three percent on the latter), and, more importantly, added subsection (c) which imposed the tax (two percent) on automobile and truck parts and accessories sold separately from the vehicles themselves. (Appendix A). The addition of subsection (c) further complicated the problems that were to arise. In addition to the two questions referred to above, i.e., the one pertaining to the identity and nature of the manufacturer and the one relating to the selling or taxable price, subsection (c) introduced other questions that were not only in addition to, but, at the same time, also were interwoven with the original two questions. What is an automobile truck part or accessory? What is the status of a part or accessory that has been rebuilt, reconditioned, or repaired? What, if anything, shall the tax be on a rebuilt part that employs tax-paid components in the rebuilding process? These are examples of the kinds of knotty questions that were generated by the appearance of the tax on automobile and truck parts and accessories.

It is foreseeable that the practical difficulties in resolving these questions would be enormous. The Treasury Department would encounter troublesome administrative problems in defining what constitutes a taxable operation, and the prospective taxpayers, on the whole, were small companies scattered throughout the country. Generally, the latter were not sufficiently sophisticated to know how to comply with the tax or cope with the Treasury regulations and definitions on an administrative or legal level.⁹

9. Note statements to this effect made in S. Rep. No. 1251, 88th Cong., 2nd Sess., 1964-2 Cum. Bull. 870, 872, reproduced in Appendix C.

The statute contained in the Acts of 1932, as amended, became part of the Internal Revenue Code of 1939, identified therein as 26 United States Code Section 3403 (c) of Chapter 29, Subchapter A, i.e., Section 3403, subsection (c) became the successor to subsection (c) of the 1932 Acts as amended. (Appendix A). Reference to Appendix A will demonstrate how elaborate the subsection had become by the last quarter of 1955. The concept of the taxability of rebuilt parts had become incorporated within the statute by that time. Section 3403 (c) was the forerunner of and became Section 4061 (b) of the Internal Revenue Code of 1954. (Appendix A).

On the whole, the nodal points in the development of the statute were historical points of crisis in the country. As a result, the taxes were not developed on any systematic basis, and they were often discriminatory in their application to the taxed industries or to purchasers of the taxed products.¹⁰

UNITED STATES V. ARMATURE EXCHANGE, INC.¹¹

This important 1941 case set the tone for many of the judicial, administrative, and, to some extent, even legislative attitudes in subsequent years regarding the definition of a manufacturer or producer, and also regarding the taxable status of rebuilt parts.

The plaintiff taxpayer brought an action against the United States of America to recover \$1,452.30 assessed and paid as manufacturer's excise taxes on the sale of armatures. The taxes were assessed against the taxpayer by virtue of Section 606(c) of the Revenue Act of 1932 as amended. (Appendix A).

The taxpayer acquired burned and worn-out armatures, stripped them to the core, and by various machine and hand operations, through the use of the old core and new material, turned out and sold what it called "rebuilt armatures." These armatures were sold outright to the trade with the taxpayer sometimes taking burned and worn-out armatures in exchange and sometimes not.

The taxpayer contended that it was in the business simply of reconstructing and restoring armatures as opposed to manufacturing or producing armatures. The trial court supported the taxpayer's contention and rendered judgment in its favor. The government appealed.

The appellate court reversed in a unanimous decision.

10. See first paragraph under "Summary" in this COMMENT.

11. 116 F.2d 969 (9th Cir. 1941), *rehearing denied*, *cert. denied*, 313 U.S. 573.

The lower court decided that the rebuilt articles were not "manufactured or produced" asserting that to be "manufactured or produced" there must be a "new and different" article at the completion of the taxpayer's operations.

The appellate court rejected this criterion holding that the operations involved constituted "manufacture or production" within the meaning of the statute. The significant segments of its opinion were:¹²

1) There was no justification for reading into the statute involved the qualification that the articles "manufactured or produced" had to have been so manufactured or produced entirely from new or virgin raw materials.

2) The discarded armatures having lost their function as useful articles as well as their commercial value as such, when acquired for use in the manufacturing and production of articles of commerce, bear the same relationship to the completed armatures as the purchase of unused materials would bear to the completed articles. The article resulting from the use of the discarded core with new materials through the employment of skill, labor, and machinery is a manufactured and produced article of commerce.

3) Treasury Regulations (Reg. 46, Art. 4) of 1932, under Section 606 of the Revenue Act of 1932, had defined "producer" as including a person who produces a taxable article by combining or assembling two or more articles. Subsequent to the appearance of the definition Congress had reenacted the statute several times. "Under the established rule Congress must be taken to have approved the administrative construction and thereby to have given it the force of law."¹³

4) Certainly if new parts had been purchased and combined to make the armatures, that would have constituted "manufacturing or producing." There can be no difference just because the parts utilized were used or discarded parts.

This case did two things at the same time. It defined the scope of the term "manufacturer or producer" and also established the concept that rebuilding is "manufacturing or producing." It is in

12. *Id.*, at 971.

13. *Helvering v. Reynolds Tobacco Co.*, 306 U.S. 110, 115 (1938).

this latter area that the most confusing and greatest bulk of the problems associated with Section 4061(b) have appeared.

MANUFACTURER, PRODUCER, OR IMPORTER

The statute imposes the tax on articles sold by the "manufacturer, producer, or importer." The statute itself does not define the three words. They are defined in the cases, a typical example of which, in the "rebuilding" context, is *United States v. Armature Exchange, Inc.*¹⁴ described above. Apart from the "rebuilding" context, the courts have handled the definitions in a variety of ways, and not altogether consistently.

It is universally held that the tax itself is imposed on the manufacturer and vendor and not upon the purchaser.¹⁵ The manufacturer's excise tax is a tax liability of the manufacturer. It is not a liability of either the intermediate dealer or of the ultimate purchaser.¹⁶

In a situation where one person manufactures or produces a taxable article for another who furnishes materials and retains title to the article, the latter for whom the article is manufactured or produced, not the actual manufacturer, is considered to be the "manufacturer" for purposes of Section 4061 (b).¹⁷

In another situation, the taxpayer's patented booster device for suspension springs was fabricated by a company under contract with the taxpayer and sold to the taxpayer at the contract price. The taxpayer then repackaged the device, added instructions for installation and a warranty, and resold them. The taxpayer was held *not* to be the "manufacturer" of the devices within the provisions of Section 4061 (b).¹⁸ No special meaning is intended by the word "manufacturer" in Section 4061 (b), and patentees or licensees are not per se "manufacturers."¹⁹ But see *Boise Nat. Leasing, Inc. v. United States*²⁰ for a contrary holding.

A company making custom-made seat covers for used automobiles by chalking, marking, cutting, and sewing the covers was a

14. 116 F.2d 969 (9th Cir. 1941), *rehearing denied, cert. denied*, 313 U.S. 573.

15. *Martin's Auto Trimming, Inc. v. Riddell*, 283 F.2d 503 (Cir. Cal. 1960).

16. *Undercofler v. Capital Auto Co.*, 111 Ga. App. 709, 143 S.E.2d 206 (1965).

17. *Import Wholesalers Corp. v. United States*, 368 F.2d 577 (Ct. Cl. 1966).

18. *Air Life Co. v. United States*, 418 F.2d 558 (Cir. Mich. 1969).

19. *Id.*

20. 389 F.2d 633 (Cir. Idaho 1968).

"manufacturer" for excise tax purposes.²¹ Where a company made automobile seat covers on special orders of customers, who selected the material to be used from fabrics carried in stock by the company, the company was the "manufacturer"²² for the purposes of Section 4061(b). But see *Johnnie & Mack, Inc. v. United States*²³ holding that an automobile repair shop making custom seat covers on orders was *not* a "manufacturer" of automobile accessories within the meaning of Section 4061(b).

A taxpayer who purchased glass from glass manufacturers in cut sizes and who then cut the glass, ground off the edges, and delivered the glass to customers for use in automobiles was *not* a "manufacturer" within Section 4061(b).²⁴

An "importer," for excise tax purposes, is the first purchaser resident in the United States who arranges, as a principal not as an agent, for goods to be brought into the United States.²⁵ This applies to a used automobile dealer's first sales in the United States of used automobiles imported from abroad.²⁶

REBUILDING, RECONDITIONING, REPAIRING

As described in *United States v. Armature Exchange, Inc.*,²⁷ rebuilt automobile parts and accessories are "manufactured and produced" for the purposes of Section 4061(b). The question that is immediately conjured up is, "When does an old or used automobile part or accessory that has been restored become a rebuilt part?"

One can conceive of all gradations of restoration. Cleaning up an old part or painting it or replating it constitutes restoration of the part. But do any of these operations or combinations of them constitute rebuilding? When do they fall short of being rebuilding? It is clear that a lot of arbitrary rules of thumb and criteria

21. *Masao Hirasuma v. McKenney*, 245 F.2d 98 (Cir. Hawaii 1957).

22. *United States v. Keeton*, 238 F.2d 878 (Cir. Va. 1956), *cert. denied*, 353 U.S. 973.

23. 151 F. Supp. 748 (D. Fla. 1957).

24. *Earl Glass Co. v. United States*, 197 F. Supp. 707 (D. Nev. 1961).

25. *Handley Motor Co. v. United States*, 338 F.2d 361 (Ct. Cl. 1964); *Weiner v. United States*, 261 F. Supp. 413 (D. Cal. 1966); *Import Wholesalers Corp. v. United States*, 368 F.2d 577 (Ct. Cl. 1966); *U.S. Truck Sales Co. v. United States*, 229 F.2d 693 (Cir. Ohio 1956).

26. *Smith v. United States*, 319 F.2d 776 (Cir. Tex. 1963).

27. 116 F.2d 969 (9th Cir. 1941), *rehearing denied, cert. denied*, 313 U.S. 573.

would arise around these questions. The cases have arisen in profusion and have handled the problem with confusion. Typical examples are as follows:

1) Reassembled generators containing armatures rewound by reassemblers held "manufactured" and hence taxable.²⁸

2) Rebuilt clutch assemblies held taxable as "manufactured" articles.²⁹

3) Taxpayers who made rear fenders from the steel sheet during modification of trucks in order to convert them into specialty vehicles were "manufacturers" of fenders even though the fenders so fabricated were not assembled, stocked, or sold as independent parts or accessories.³⁰

4) Straightening, grinding, stripping old chrome, repolishing, and replating of damaged and otherwise unusable automobile bumpers constituted "manufacturing" under Section 4061(b).³¹

5) Rebuilding of automobile engines constituted "manufacturing" requiring the imposition of the tax upon sales of the rebuilt engines.³²

6) Rebuilding automobile engines from a combination of salvaged parts and newly manufactured parts which were purchased from manufacturers who had already paid the tax on these newly manufactured parts, and subsequent sale of these engines raised an issue as to whether the totality of these operations constituted manufacturing within the meaning of Section 4061(b).³³

7) Taxpayer who sold automobile connecting rods prepared by rebarbitting or regrinding used rods was held to be a "manufacturer."³⁴

8) Acquiring worn-out armatures, stripping them to the core, and through the use of the old core and new material, turning out rebuilt armatures held to be manufacturing within the section.³⁵

9) Where the only new material used by the taxpayer in *reconditioning* of automobile storage batteries were wooden or plastic

28. *Exchange Parts Co. of Fort Worth v. United States*, 279 F.2d 251 (Ct. Cl. 1960).

29. *Id.*

30. *Whattoff v. United States*, 355 F.2d 473 (Cir. Iowa 1966).

31. *Blake v. United States*, 355 F.2d 23 (Cir. Tex. 1966).

32. *De Boisblanc v. Usry*, 272 F.2d 11 (Cir. La. 1959).

33. *Hartley v. United States*, 252 F.2d 262 (Cir. Tex. 1958).

34. *Clawson & Bals v. United States*, 182 F.2d 402 (Cir. Ill. 1950), *cert. denied*, 340 U.S. 883.

35. *United States v. Armature Exchange*, 116 F.2d 969 (9th Cir. 1941), *cert. denied*, 313 U.S. 573.

insulators, roofing tar, battery acid, and asphalt paint, all of which were either tax-paid or tax exempt items, and where the lead plates in the cells were not replaced, the operations did not constitute "manufacturing" for tax purposes.³⁶

10) Sales of rebuilt automobile motors were held taxable even though they were made up of component parts some of which were taxable to their manufacturers.³⁷

The Internal Revenue Service attempted to cope with the parameters of the possible permutations and combinations of operations and processes by issuing Treasury Decision 6648.³⁸ Treasury Regulation 48.4061(b)-3, a part of Treasury Decision 6648, defined Rebuilt, Reconditioned, Or Repaired Parts Or Accessories, reproduced as Appendix B.

Insofar as the manufacturers excise tax was concerned, neither reconditioned nor repaired parts or accessories were subject. Only the rebuilt articles were. The contests between the Service and taxpayers resolved themselves, for the most part where restorative activities were concerned, into arguments as to whether what was in issue was rebuilding or reconditioning or repairing. The detailed description of the replacement bumper business, *infra*, illustrates the course that argument might have taken in a particular case.

REPLACEMENT AUTOMOBILE BUMPERS

The situation in the replacement automobile bumper industry is illustrative of the situation that prevailed generally in the rebuilt automobile parts and accessories industries, insofar as Section 4061(b) is concerned. That industry is a microcosm of the automobile and truck parts and accessories industries, generally. Accordingly, a description of its experiences, vis-a-vis the manufacturers excise tax would be analogous, if not identical, to that of all those businesses generically termed, "rebuilders." Furthermore, the writer had, for many years, been involved in an interrelated family of corporations exclusively devoted to the making of these bumpers and was personally involved with virtually all of the

36. *Martin Tire Co. v. United States*, 130 F. Supp. 316 (D. Fla. 1955).

37. *Hackendorf v. United States*, 243 F.2d 760 (Cir. Okla. 1957), *cert. denied*, 355 U.S. 826.

38. 1963-1 Cum. Bull. 197.

problems associated with Section 4061(b) and their impact on this interesting industry and is, therefore, qualified to describe the situation quite authoritatively.

By way of introductory information, the replacement bumpers are produced by "restoring" damaged bumpers, i.e., bumpers that have been damaged as a result of motor vehicle accidents. The damaged bumper is called the "core." The bumper is restored by straightening the core employing presses, hammers, and other impact tools and reforming it to its original shape and configuration by the use of templates, molds, and jigs and fixtures. The rough areas are smoothed out using the conventional auto body shop techniques of dollying and disc grinding. This entire procedure is called "straightening." Next, the old chromium plate is stripped leaving intact on the bumper the substrate of nickel or copper and nickel. Then the bumper undergoes one or more polishing operations after which the usual sequence of operations is plating with copper, copper buffing, nickel plating, and finally chromium plating. The foregoing is done so skillfully that there is no discernible visible difference between this restored bumper and the original factory bumper that was on the vehicle.

This bumper "restoring" industry came into existence in the late 1940's and the early 1950's due to certain changes in the engineering principles of the automobile manufacturing industry. Prior to World War II, all auto bumpers were made of heat-treated, hardened steel because manufacturers felt that this was the best way to create something that would protect the car in the event of a collision. Also, in those days, bumpers were fairly simple in design and comparatively inexpensive. After the war, the engineering departments of automobile manufacturers changed their approach deciding that if bumpers were made of soft metal, they would absorb most of the impact shock thus protecting the car and its occupants to a much greater extent. The bumper became an expendable portion of the car. At the same time, as cars became bigger and bigger and more expensive, the bumper became larger, more ornate, and proportionately a more costly part of the car. Since the soft metal of the bumpers could now be reworked, it became commercially expedient and financially feasible to "restore" or "recondition" and thereby reuse damaged automobile bumpers that were previously scrapped. Thus, a change in engineering principles made possible the birth of this new replacement bumper industry.

The bumpers were welcomed by the prime market, the autobody and fender shops and by the insurance companies who eventually

paid most of the bills. The reason for this was that these bumpers were priced considerably below those of the original equipment manufacturer. The lower price structure was made possible because of the savings associated with receiving the raw material gratuitously and because of a very simple distribution pattern employed by the industry.

Initially a craft-like approach was employed by the industry. A damaged bumper would be picked up, restored, and returned to the customer. As a result, usually many days passed before the bumper got back to the car from which it had come. Eventually, members of the industry acquired old damaged bumpers of all types and models, restored them, and put them into inventory. At this stage, it became possible for a customer to phone in an order and have it filled at once from stock. The bumper company, as a condition of the sale, required that when it delivered the replacement bumper, the customer surrender the damaged bumper which in turn was reworked and put into inventory. The industry, at that point in time, became known in the trade as the bumper exchange business, and it expanded rapidly.

As a consequence of the expansion, the existence of the industry and the excise tax possibilities associated therewith filtered into the various local districts of the Internal Revenue Service.

There was little initial agreement among agents of the Service who happened to be assigned to audit any of the replacement bumper companies. With uncertainty, some of them characterized the bumpers as taxable and others as non-taxable. Usually, whenever the status was judged to be taxable the ensuing arguments at the agent's level resulted in a request by the company or an offer by the agent that a ruling from higher-up be made.

The various characterizing words, "rebuilt," "reconditioned," and "repaired" defined as they formally were in Regulation Section 48.4061 (b)-3 (Appendix B), and prior to that in Section 40.4061 (b)-3(a) of the Manufacturers and Retailers Excise Tax Regulations, began to be used in connection with the bumper makers—the Service referring to them more and more as "rebuilders" and the bumper people referring to themselves as bumper "reconditioners." The latter reached the point where their local and national associations were all called associations "Of Bumper Recon-

ditioners," and all price lists and other distributed literature made reference only to bumper "reconditioning."

The proselytizing continued until finally the Internal Revenue Service issued Revenue Ruling 62-162 holding that the restoration operation, described above, accompanied by an exchange sale constituted rebuilding, hence was manufacturing under Section 4061 (b), and hence was taxable. Implied recognition of the indecisive prior position of the Service in this regard, and of the many local confusing and contradictory prior holdings, appears in the prospective application of the ruling. The last paragraph of the Revenue Ruling said, "This Revenue Ruling will not be applied to sales made prior to November 1, 1962," The slate was wiped clean, but the Service had given notice that from that time on the bumper industry was made up of bumper "rebuffers."

Revenue Ruling 62-162, instead of clearing the air, generated a new category of confusion, probably worse than that which had centered around the question of whether the industry was composed of "rebuffers" or "reconditioners."

An eight percent tax was a prohibitive price addition. The Ruling pointed the way (as did Section 48.4061 (b)-3, Appendix B) to escape the tax by "repairing" instead of "rebuilding." The difference is a simple one. One who might otherwise be a "rebuffer" becomes a "repairer" by the simple expedient of returning a "bumper belonging to the owner of an automobile for his personal use." (Revenue Ruling 62-162). In other words, do the customer's own bumper and return it.

The second approach was that relating to the "price for which so sold." Eight percent of what? So all kinds of intermediate selling companies arose leading to Section 4216³⁹ squabbles between companies and Service auditors.

Between problems relating to the concept of "repairer" vs. "rebuffer," to how the bumper company adequately sustained its burden of demonstrating that invoiced items marked "customer's own car" were indeed that, and to those involving constructive pricing, the situation reached a new acme of chaos until the Congress resolved the problem by enacting Section 4063 (c)⁴⁰ in 1964

39. This refers to Internal Revenue Code of 1954, § 4216, a section devoted to defining the price for which an article is sold for excise tax purposes. The section contains an elaborate "constructive sale price" subsection, subsection (b), (1) through (6) designed to define what the "price for which so sold" is to be under a variety of possible circumstances including, for example, the price of an article sold otherwise than through an arm's length transaction at less than fair market price.

40. See note 2, *supra*.

which repealed the tax on rebuilt parts and accessories once and for all.

Clean up of in process audits proceeded quickly with the Service liberally compromising along the way to get rid of them.

As an anti-climax, a 1964 district court of Texas case⁴¹ holding with the Service that bumper restoration was "rebuilding" and, therefore, "manufacturing" was affirmed by an appellate court in 1966.⁴²

By extending what has been described about the bumper business to all the replacement auto and truck parts industries similarly situated in connection with Section 4061(b), a clear concept evolves as to the enormity of the problems that existed up to the time of the 1964⁴³ and 1965⁴⁴ repeal enactments.

It should be pointed out that the similarity between the replacement automobile bumper industry and all of the other after-market rebuilt parts and accessories industries holds up even as to the size characteristics of the member companies. On the overall scale of American industry, the bumper rebuilders are small businesses, most of them are really entrepreneurially operated in the old fashioned ideal of the American business. This is also true of practically all the companies who produce rebuilt parts and accessories for automobiles and trucks.

PARTS OR ACCESSORIES

Every version of the statute has imposed the tax on "parts or accessories." (Appendix A). By "parts or accessories" is meant those articles generally associated with the motor vehicles themselves and the latter typically are those enumerated in subsection (a)(1). (See, for example, the wording of the current version of Section 4061(b) in Appendix A). Ascertaining what are such "parts or accessories" for the purposes of Section 4061(b) is complicated by the fact that motor vehicle owners are apt to, and do, adapt every conceivable kind of accessory item to the vehicle. This has necessitated an extensive classification system by the Service.

41. *Blake v. United States*, 249 F. Supp. 296 (D. Tex. 1964).

42. *Blake v. United States*, 355 F.2d 23 (Cir. Tex. 1966).

43. Pub. L. No. 88-653, Internal Revenue Code of 1954, § 4063(c) added.

44. Pub. L. No. 89-44, § 201(b)(2).

Judicially, parts and accessories subject to the tax have been discussed as follows:

1) Are refrigerator units, mounted on truck or trailer bodies, operated from the trucks own power, and used for the commercial transportation of perishable products and frozen food, commercial refrigeration units or auto parts and accessories? A 1967 Court of Claims held that the units were not subject to the tax but were commercial refrigerator units.⁴⁵

2) Pickup coaches manufactured by the taxpayer to be transported in the bed of pickup trucks for temporary mobile housing were not "automobile truck bodies" or "automobile accessories" within the Section.⁴⁶

3) Baby bottle warmers capable of being operated from the cigarette lighter of an automobile are subject to the tax.⁴⁷

4) An electric sign designed to be attached to the top of a taxicab is not an auto part or accessory for the purpose of the Section.⁴⁸

5) Radio antennae, designed to be attached to automobiles, are taxable under the Section.⁴⁹

6) Car beds for infants having many non-automotive uses, were held taxable as parts or accessories because they were primarily designed, advertised, and sold for use in automobiles.⁵⁰ But in another district, the same year, there was a holding that if an article that is used on automobiles is equally adapted and commonly used for other purposes it will not be an automobile part within the Section.⁵¹ And batteries designed and manufactured specifically for industrial use as a component part of industrial machinery and equipment, and tractor batteries specifically designed for use in farm tractors, identified as such and sold as such, were held not subject to tax under 4061(b) even though the batteries might be used in motor vehicles of a taxable classification.⁵²

7) What constitutes automobile accessories for the purposes of

45. U.S. Thermo Control v. United States, 372 F.2d 964 (Ct. Cl. 1967).
46. United States v. King Trailer Co., 350 F.2d 947 (Cir. Cal. 1965).
47. Aron v. United States, 259 F.2d 757 (Cir. Cal. 1958), *cert. denied*, 358 U.S. 866.

48. Smith v. McDonald, 214 F.2d 920 (Cir. Pa. 1954).

49. Van Norman Industries, Inc. v. United States, 361 F.2d 992 (Ct. Cl. 1966).

50. Rose-Derry Co. v. United States, 243 F. Supp. 26 (D. Mass. 1965).

51. Crown Products Co. v. United States, 239 F. Supp. 1009 (D. Neb. 1965).

52. Grant v. White, 219 F. Supp. 774 (D. Ill. 1963).

the tax depends upon the facts of each case.⁵³

The code itself specifically classifies certain articles as parts for the purposes of Section 4061(b).⁵⁴ The Service has attempted to amplify Section 4061(b) and Section 4062 by means of the regulations route,⁵⁵ the result being a rather extensive list of parts and accessories possibly subject to the tax.

The Code itself also includes an exemption section⁵⁶ listing articles specifically exempt from the tax imposed by Section 4061(a) and (b). Prior to 1965 the list of exempt articles was just house trailers or tractors. A 1965 amendment expanded the list of exemptions by substituting camper coaches and bodies for self-propelled mobile homes, feed, seed, and fertilizer equipment, house trailers, and small three wheeled trucks.⁵⁷

The trend in attenuating the scope of Section 4061(b) has been consistent since 1964. Not only has this been manifested by the repeal of the tax on rebuilt parts and accessories⁵⁸ and by the 1965 repeal of the tax on all automobile parts and accessories⁵⁹ but also, as indicated above, by an expansion of the exemption section, Section 4063(a).

THE PRICE FOR WHICH SO SOLD

The tax imposed by Section 4061(b) is currently "eight percent of the price for which so sold." (Appendix A). The words, "the price for which so sold," have always appeared in the statute. This means that once the identity of the manufacturer, producer, or importer has been established, the tax is imposed as a percentage of that identified party's selling price. That "selling price" base, as a readily ascertainable quantity, is complicated by a variety of factors among which are the following:

- 1) What items of cost may be excluded from the tax base?

53. *Benmatt Organization v. United States*, 134 F. Supp. 511 (D. Cal. 1955).

54. Int. Rev. Code of 1954, § 4062.

55. See, e.g., 1963-1 Cum. Bull. 197, 205, *et seq.*, and note 42, *supra*.

56. Int. Rev. Code of 1954, § 4063.

57. See Int. Rev. Code of 1954, § 4063(a) and especially (1), (2), (3), and (4) thereunder.

58. Pub. L. No. 88-653, Int. Rev. Code of 1954, § 4063(c).

59. Pub. L. No. 89-44, § 201(b)(2).

2) What is the tax base of articles sold at retail or on consignment as compared with the tax base of those sold at wholesale? Since the tax is imposed just one time, i.e., on the first sale, the discriminatory implications inherent in this question are apparent.

3) What is the tax base of articles sold from a manufacturing company to a controlled interrelated company and, therefore, at a price other than a fair market price?

Recognition of the complications extant in the manufacturer's selling price concept by Congress led to an extensive codification of the definition of price.⁶⁰ Section 4216, a complex section, is a detailed result of Congress' effort in this regard. All the questions noted above are considered in the context of the broad regulatory powers accorded to the "Secretary or his delegate" because of the recognition of the complexity of the problem of completely adequately defining "the price for which so sold."

The extensive nature of Congress' effort, in this regard, is exemplified by Section 4216(f) which concerns the exclusion of local advertising charges from the tax base sales price. A charge for local advertising may be excluded from the manufacturers' sales price if:

1) The charge does not exceed five percent of the manufacturers' price for the article exclusive of the charge for local advertising.

2) It is made as a separate advertising charge at the time of the sale of the article.

3) It is intended to be refunded to the purchaser or any subsequent vendee of the purchaser.

The local advertising that is excludable is limited to radio, television, or newspaper advertising, and to that advertising which states the name of the article and the retail shop at which that article can be purchased.

Even more extensively defined in the statute, in Section 4216(b), is what is termed "constructive sale price." Constructive sale price is an artificial tax base price established to get a uniform tax on the same or similar articles where these are sold by manufacturers to different classes or levels of customers, such as wholesalers, retailers, consumers, etc. or where special sales relationships exist. In general, it covers sales of articles sold at prices other than wholesale (e.g., retail), consignment sales, and sales made other

60. Int. Rev. Code of 1954, § 4216.

than through arm's length transactions at less than fair market value.

Section 4216(b) (2) codifies the special rule that if an article is sold at retail or to a retailer and if:

1) The manufacturer, producer, or importer of such articles regularly sells such articles at retail, or to retailers, as the case may be;

2) The manufacturer, producer, or importer of such articles regularly sells such articles to one or more wholesale distributor in arm's length transactions, and he establishes that his prices in such cases are determined without regard to any tax benefit;

3) In the case of articles upon which tax is imposed under Section 4061(a) (relating to trucks, buses, tractors, etc.), the normal method of sales for such articles in the industry is not to sell such articles at retail or to retailers; and

4) The transaction is an arm's length transaction; then the tax shall be computed at the lower of the price for which the article is sold or the highest price for which such articles are sold by such manufacturer, producer, or importer to wholesale distributors.

Even further, Section 4216(b) (3) establishes a ninety percent constructive price rule; Section 4216(b) (5) establishes a ninety-eight point five percent constructive price rule; and in Revenue Ruling 62-68;⁶¹ the Internal Revenue Service established a ninety-five percent constructive price rule to cover certain situations that the ninety percent and ninety-eight point five percent rules did not.

Where rebuilt parts and accessories were concerned, there were further complications. For example, where a company gave credit on used automobile connecting rods in the sale of reground or reworked rods, it was held that the credit given for the old rods was required to be considered a part of the price in computing the tax.⁶²

THE TIDE TURNS—REPEAL ENACTMENTS OF 1964 AND 1965

By 1964, the situation was intolerable what with the multitude of problems associated with its widening scope; with the concept

61. 1962-1 Cum. Bull. 216.

62. *Clawson & Bals v. United States*, 182 F.2d 402 (Cir. Ill. 1950), *cert. denied*, 340 U.S. 883.

of "manufacturer, producer, or importer;" with "rebuilding" vs. "reconditioning" or "repairing;" with identifying "parts or accessories" for the purposes of the section; with precisely what is "the price for which so sold;" and with its impact being felt primarily by large numbers of small businesses.

By 1964 countless numbers of Service audits were in process, most of them unresolved over the technical difficulties associated with the above problems, and characterized by haggling between the taxpayers and the Service. The worst problems, within the entire problem area, were those involving the concepts of "rebuilding" and "reconditioning" and "repairing." These, in particular, involved smaller companies whose record keeping, on the whole, was not characterized by the kind of sophistication ultimately necessary for the resolution of many of the questions that had to arise in auditing what is presumably a "rebuilder."

On October 13, 1964, Congress enacted Public Law Number 88-653 removing the tax on rebuilt parts and accessories. This was accomplished by adding Section 4063(c) to the Internal Revenue Code.⁶³ The repeal was made effective as of January 1, 1965.

Of special importance in assessing what, to the automotive parts rebuilders, was a landmark enactment, is the legislative intent clearly expressed by Congress as to what motivated the repeal. This expression is reflected in Senate Report Number 1251, 88th Congress, 2d Session, reproduced in Appendix C. The reasons given for the repeal, and some of them are essentially reasons that may be advanced to support arguments for the repeal of the tax on light truck parts, may be summarized as follows:

1) There are difficulties associated with distinguishing between rebuilding and reconditioning and, in a dynamic setting, in satisfactorily defining "rebuilding." This has resulted in both disputes between the industry and the Service and in confusion and uncertainty as to the tax status of some processes.

2) The large number of small companies in the field are inordinately burdened trying to comply with the tax.

3) The tax is particularly objectionable in its regressive nature among consumers, its impact being felt more heavily by lower income groups for whom the purchase of these parts is a necessity.

4) The revenue involved is only eight million dollars per year, a small amount for so much trouble.

63. See note 2, *supra*, for text of this section.

The second significant repeal enactment was Public Law Number 89-44, Section 201(b)(2), enacted by the 89th Congress in its first session in 1965. This bill repealed the manufacturers' excise tax on all automobile parts and accessories effective January 1, 1966, allowing the tax to remain on the vehicles themselves, both automobiles and trucks, and on truck parts and accessories.

Of particular significance, insofar as this Comment is concerned, is the legislative intent which motivated Congress to enact the repeal.

The present excise taxes, for the most part, were initially levied as emergency revenue-raising measures at the time of the Korean War or World War II, or the depression of the 1930's. As a result, they were not developed on any systematic basis and are often discriminatory in their application to the taxed industries or to the purchasers of the taxed products.⁶⁴

. . . Consumers of the taxed products where the tax is passed forward must pay a premium, over and above the market price, for the taxed items, which consumers of untaxed items do not pay. These selective excise taxes tend to reduce sales and therefore reduce incomes and jobs in the industries which produce the taxed goods. In these ways, selective excise taxation results in arbitrary and undesirable distortions in the allocation of resources and in this manner interferes with the free play of our competitive market.

Many of these excises also now are objectionable in that they are generally regressive in their impact, absorbing a larger share of the income of low income persons than of those with higher incomes. This stems from the fact that low-income families find it necessary to spend a higher proportion of their incomes for consumption than those with larger incomes. Moreover, the present system of manufacturers' excises tends to impose heavier tax burdens on newly formed families which must invest heavily in purchases of appliances and other taxed commodities.

Another undesirable aspect of the selective excise taxes is that many of them are imposed on items used in business. Such taxes place arbitrary tax burdens on firms depending on their requirements for taxed items. Moreover, these business cost taxes may discourage the use of the most advanced and efficient machines or other products, and their inclusion in costs of the business introduce price distortions in markets for final goods and services. Since these costs tend to be reflected in the prices of final or end consumer products, they probably in their impact are also regressive.

In many instances the selective excises also create heavy compliance burdens. The imposition of Federal excises on a variety of

64. H. Rep. No. 433, 89th Cong., 1st Sess., 1965 U.S. Code Cong. and Ad. News 1645.

relatively inexpensive commodities burdens retailers and manufacturers with compliance duties which are often disproportionately heavy, viewed in relation to the revenues produced by the taxes. Moreover, this burden tends to be heavier for smaller businesses. Removal of this burden, a hidden cost of taxation, will free businessmen to spend more time managing their own affairs.⁶⁵

For additional relevant commentary by the House Committee see Appendix D.

In summary, what Congress has said in connection with the repeal of the manufacturers' excise tax on automobile parts and accessories is as follows:

1) The taxes, levied as emergency revenue-raising devices, were not developed systematically and were often discriminatory to producers and consumers.

2) Price increases necessitated by the discriminatory taxes resulted in reduced sales, incomes, and employment in the taxed industries and also impaired the ability of the taxed industries to compete in a free market.

3) The taxes were regressive in that they placed proportionately heavier burdens on low income persons than on those with higher incomes and also on newly formed families than on older established ones.

4) The taxes discouraged business in investments in more advanced and more efficient machinery because profits that otherwise might be available for development and modernization go to the taxes, instead.

5) Selective excises place heavy compliance burdens on producers, burdens frequently out of proportion to the revenues the taxes produce. Furthermore, the compliance burdens are generally shouldered by smaller businesses less able to stand them. As one consequence of this, less time is devoted to management activities than would be the case if these burdens were removed with resulting benefit all around.

6) There is a strong inference that the sequence of tax removal steps should be, first, removal of the tax on parts and accessories and then removal of the tax on the vehicles, not the other way around.

7) The tax revenue derived from all truck parts and accessories upon which the tax was retained was twenty million dollars per year.

65. *Id.*, at 1655.

REPEAL ENACTMENT OF 1971

Up to 1971, the repeal sequence had been, first, the elimination of the tax on rebuilt parts and accessories and, second, the elimination of the tax on all automobile parts and accessories. The tax on automobiles and trucks was still effective. Then, in the Revenue Act of 1971, the tax imposed on automobiles and on light-duty trucks was removed.⁶⁶ Light-duty trucks were defined as those "having a gross vehicle weight of ten thousand pounds or less (as determined under regulations prescribed by the Secretary or his delegate)."⁶⁷ Basically, this included one half and three quarter ton pickup trucks.

The reasons for excluding light-duty trucks from the imposition of the tax, insofar as Congress was concerned,⁶⁸ were as follows:

1) Light-duty trucks, to a substantial degree, are used by farmers and other individuals for the same purposes as passenger automobiles.⁶⁹ It is logical, therefore, from an excise tax point of view that they should be exempt from the tax if passenger automobiles are.

2) "The action taken in this bill continues the trend begun in 1965 to repeal excise taxes which place discriminatory tax burdens on the consumers and producers of the taxed products."⁷⁰

3) To preserve the passenger automobile treatment, for the purposes of consistency, the bill exempted ambulances and hearses from the tax.⁷¹

The reversal of the manufacturers excise tax trend which had commenced in 1965, with the repeal of the tax on rebuilt parts and accessories, was almost complete and almost logically consistent, with the enactment of Public Law Number 92-178. Parts first and then the vehicles themselves had finally been made exempt from the tax.

In the light of the above, the treatment accorded to the parts and accessories of light trucks sold separately from the trucks them-

66. Pub. L. No. 92-178, § 401.

67. Int. Rev. Code of 1954, § 4061(a)(2).

68. H. Rep. No. 92-533, 92nd Cong., 1st Sess., 1971 U.S. Code Cong. and Ad. News 1866.

69. *Id.*, at 1826, 1831.

70. *Id.*, at 1831.

71. *Id.*, at 1867.

selves is startling in its incongruity. As a result of the 1971 enactment, light trucks are exempt from the tax along with the truck parts and accessories included as original equipment on the truck when it is first sold. Yet, these same parts and accessories are subject to the excise tax when sold separately from the truck.

This is an anomalous situation in that automobiles and/or their parts and accessories are exempt from the manufacturers excise tax. Light trucks also have been excluded by the 1971 Act because they are used by farmers and others like automobiles and are, therefore, treated like automobiles for excise tax purposes. Yet, the replacement parts and after-market accessories for light trucks continue to be taxable.

The reason that this legislative result occurs can be seen from a perusal of Section 4061(b)(2) in Appendix A as that section reads just prior to and then after the Revenue Act of 1971. Note that, in subsection (2) just prior to the Revenue Act of 1971, the tax exclusion is applicable to "any article enumerated in subsection (a)(2) . . ." The Revenue Act of 1971 added light-duty trucks to subsection (a)(2) but then, inexplicably, eliminated the words, "any article enumerated in subsection (a)(2) . . ." from subsection (b)(2) and substituted, in their place, an explicitly designated group of exclusions which did not include light-duty trucks.

LEGISLATIVE RECOMMENDATIONS

Starting with the first repeal enactment in 1964, Congress has consistently made clear its attitude towards manufacturers excise taxes on automotive parts and accessories and has acted in concert with that expressed attitude from 1964 to the present except with regard to the limited category, truck parts and accessories. What Congress has effectively said about these taxes is:

- 1) They were initially levied as emergency revenue-raising measures during periods of crisis.
- 2) They were not developed on any systematic basis.
- 3) They were often discriminatory in their application to the taxed industries and to the purchasers of the taxed products causing reduced sales, incomes, and employment in the taxed industries.
- 4) They imposed a particular burden on the large number of what are on the whole small companies trying to comply with the tax in its complex ramifications. Removal of the burden will free businessmen to spend more time managing their own affairs.

5) They are regressive taxes in their impact on consumers, being felt more heavily by lower income groups than by higher income groups.

6) The revenues involved are small for the amount of trouble they create both for the taxpayer in his effort to comply and the Service in its enforcement activities.

7) They have throttled progress towards efficiency, development, and modernization of the businesses involved.

Objectively, the history of the manufacturers excise taxes has been characterized by:

1) Low revenues relative to the amount of effort involved in establishing practical definitive standards for enforcement and compliance. The multitudes of problems that arose and remained around the concepts of rebuilding v. reconditioning v. repairing, of what and who is a manufacturer, of what are parts and accessories for the purposes of the tax, and of the complex doctrines defining price give testimony to this fact.

2) A plethora of disputes between taxpayers and the Service and constant confusion as to bases for their resolution.

3) A steady attenuation of the scope of the taxes from 1964 on.

4) A continuing expansion of the number of articles exempted from the taxes until, at present, very few remain, relatively speaking.

Specifically as to light trucks:

1) Congress has decided to treat them like automobiles because of the purposes they serve for their owners. Accordingly, Congress has removed the tax on the light trucks but has neglected to do so on truck parts and accessories although doing so on automobile parts and accessories.

2) Total truck parts tax revenues in 1965 were only twenty million dollars, only a portion of which were derived from the parts of light trucks.

3) In the entire history of the manufacturers excise tax, this is the only time the tax on a vehicle has been removed without the prior removal of the tax on that vehicle's parts and accessories.

Viewed in the context of all of the foregoing, there is no justi-

fication for retaining the tax as it now exists. It is recommended that Congress repeal Part I of Subchapter A of Chapter 32 of 26 United States Code, thereby eliminating the manufacturers excise tax from all motor vehicles and their parts and accessories.

At the very least, the parts and accessories of light trucks should be exempted from the manufacturers excise tax. This can be accomplished by amending Section 4061(b)(2) to read as follows:

(2) No tax shall be imposed under this subsection upon any part or accessory which is suitable for use (and ordinarily is used) on or in connection with, or as a component part of, [any article enumerated in subsection (a)(2)], any chassis or body for a passenger automobile, any chassis or body for a trailer or semi-trailer suitable for use in connection with a passenger automobile, or a house trailer.

The bracketed portion inserted into the present section as shown would accomplish the purpose and would effect the suggested correction of the statute.

JEROME L. BLEIWEIS

Appendix A

Wording of Internal Revenue Code, Section 4061 (b) and its predecessors at various significant states of its history.

Acts June 6, 1932, Section 606.

There is hereby imposed upon the following articles sold by the manufacturer, producer, or importer, a tax equivalent to the following percentages of the price for which so sold:

(a) Automobile truck chassis and automobile truck bodies (including in both cases parts or accessories therefor sold on or in connection therewith or with the sale thereof), two per centum. A sale of an automobile truck shall, for the purposes of this subsection, be considered to be a sale of the chassis and of the body.

Amendment of above by Revenue Act of 1938.

(a) Automobile truck chassis, automobile truck bodies, tractors of the kind chiefly used for highway transportation in combination with a trailer or semi-trailer (including in each of the above cases parts or accessories therefor sold on or in connection therewith or with the sale thereof), two per centum. A sale of an automobile truck shall, for the purposes of this subsection, be considered to be a sale of the chassis and of the body.

(b) Other automobile chassis and bodies and motorcycles (including in each case parts or accessories therefor sold on or in connection therewith or with the sale thereof), except tractors, three per centum. A sale of an automobile shall, for the purposes of this subsection, be considered to be a sale of the chassis and of the body.

(c) Parts or accessories (other than tires and inner tubes) for any of the articles enumerated in subsection (a) or (b), two per centum. For the purposes of this subsection and subsections (a) and (b), spark plugs, storage batteries, leaf springs, coils, timers, and tire chains, which are suitable for uses on or in connection with, or as component parts of any of the articles enumerated in subsection (a) or (b), shall be considered parts or accessories for such articles, whether or not primarily adapted for such use. This subsection shall not apply to chassis or bodies for automobile trucks or other automobiles

Internal Revenue Code of 1939, Chapter 29, Subchapter A, 26 United States Code Annotated, Section 3403 (c) at October 1, 1955, through the end of the 1st Session, 84th Congress.

There shall be imposed upon the following articles sold by the manufacturer, producer, or importer, a tax equivalent to the following percentages of the price for which so sold: . . .

(c) Parts or accessories (other than tires and inner tubes and other than radio or television receiving sets) for any of the articles enumerated in subsection (a) or (b), eight per centum except that on and after April 1, 1955, the rate shall be five per centum. For the purposes of this subsection and subsections (a) and (b), spark plugs, storage batteries, leaf springs, coils, timers, and tire chains, which are suitable for use on or in connection with, or as component parts of, any of the articles enumerated in subsection (a) or (b), shall be considered parts or accessories for such articles, whether or not primarily adapted for such use. This subsection shall not apply to chassis or bodies for automobile trucks or other automobiles. . . . In determining the sale price of a rebuilt automobile part or accessory there shall be excluded from the price, in accordance with regulations prescribed by the Secretary, the value of a like part or accessory accepted in exchange.

(Note: On October 13, 1964, Public Law Number 88-653 repealed the tax on rebuilt parts and accessories by adding Section 4063 (c).) Section 4061 (b) just prior to Revenue Act of 1971, Public Law Number 92-178.

(1) Except as provided in paragraph (2), there is hereby imposed upon parts or accessories (other than tires and inner tubes) for any of the articles enumerated in subsection (a) (1) sold by the manufacturer, producer, or importer a tax equivalent to eight percent of the price for which so sold, except that on and after October 1, 1972, the rate shall be five percent.

(2) No tax shall be imposed under this subsection upon any part or accessory which is suitable for use (and ordinarily is used) on or in connection with, or as a component part of, any article enumerated in subsection (a) (2) or a house trailer.

Section 4061(b) after Revenue Act of 1971, Public Law Number 92-178.

(1) Except as provided in paragraph (2), there is hereby imposed upon parts or accessories (other than tires and inner tubes) for any of the articles enumerated in subsection (a) (1) sold by the manufacturer, producer, or importer a tax equivalent to eight percent of the price for which so sold, except that on and after October 1, 1977, the rate shall be five percent.

(2) No tax shall be imposed under this subsection upon any part or accessory which is suitable for use (and ordinarily is used) on or in connection with, or as a component part of, any chassis or body for a passenger automobile, any chassis or body for a trailer or semi-trailer suitable for use in connection with a passenger automobile, or a house trailer.

Appendix B

Section 48.4061(b)-3 Rebuilt, Reconditioned, Or Repaired Parts Or Accessories.

(a) *Rebuilt parts or accessories.* Rebuilding of automobile parts or accessories, as distinguished from reconditioning or repairing, constitutes manufacturing, and the rebuilder of such parts or accessories is liable for the tax imposed by Section 4061(b) with respect to his sales of such rebuilt parts or accessories. Reboring or other machining, rewrinding, and comparable major operations constitute rebuildings. The person owning the part or accessory being rebuilt is the manufacturer of the article and is liable for the tax on his sale of the rebuilt part or accessory. The tax attaches whether the machining or other operation is performed by the rebuilder himself or by some other person in his behalf. For example, the tax attaches with respect to sales of (1) rebuilt batteries, (2) rebabbitted or machined connecting rods, (3) reassembled clutches after operations such as the resurfacing of clutch plates, (4) rewound armatures, (5) reassembled generators with armatures rewound by or for the person reassembling the generator, (6) reground or remetalized crankshafts, and (7) engines in which blocks are machined (such as cylinders rebored) or new blocks installed. For provisions relating to the sale price of rebuilt parts or accessories, see Section 48.4062(b)-1.

(b) *Reconditioned parts or accessories.* The mere disassembling, cleaning, and reassembling (with any necessary replacements of worn parts) of automobile parts or accessories, such as fuel pumps, water pumps, carburetors, distributors, shock absorbers, windshieldwiper motors, brake shoes, clutch discs, voltage regulators, and other parts or accessories, are regarded as reconditioning operations rather than the manufacturing or production of rebuilt parts or accessories. The sale of a reconditioned part or accessory is not subject to tax if previous to the reconditioning there had been a prior sale of such part or accessory

in the United States. Any new taxable parts or accessories produced, or purchased tax free for use in further manufacture, and used as replacements in reconditioning such units are subject to tax when used by the reconditioner.

(c) *Repaired parts or accessories.* The tax does not apply to the amount paid for the repair of automobile parts or accessories for the owner thereof. Repairing consists of the restoration, whether by rebuilding or reconditioning, of an owner's part or accessory to useable condition for his own use rather than for sale. The person who performs the repairing must retain in his possession evidence or documents from which the nontaxable nature of the operation can be ascertained. Any person engaged in rebuilding parts or accessories for purposes of sale incurs liability for tax with respect to his own use of any part or accessory rebuilt by him for sale.

Appendix C

Senate Report Number 1251, 88th Congress, 2d Session, 1964-2 Cum. Bull. 870, 872.

REPEAL OF TAX ON REBUILT AUTO PARTS

Present law imposes an excise tax of eight percent (scheduled to revert to five percent as of July 1, 1965) on the sale of automobile parts and accessories by the manufacturer. Under longstanding regulations, this tax has been held to apply to rebuilt parts and accessories on the grounds that the rebuilding constitutes "manufacturing." This taxable status of rebuilt parts has been recognized by Congress in that it has provided that the sales price of rebuilt automobile parts or accessories is not to include the value of a like part traded in on the rebuilt part.

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

In addition to the troublesome administrative problems arising in defining what constitutes a taxable operation,

the large number of small rebuilders scattered throughout the country are burdened in trying to comply with the tax. This tax also is particularly objectionable in that its distribution among consumers is undoubtedly highly regressive. Certainly more than a proportionate part of the purchasers of automotive rebuilt parts (as distinct from new parts) are made by those with relatively low incomes; thus, the impact of the tax is believed to be heavily concentrated on the lower income groups. Moreover, since the revenue involved in this case amounts to only approximately eight million dollars a year, your committee does not believe that it is necessary to await consideration of all excise taxes before acting with respect to this small, but troublesome, problem.

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

Appendix D

House Report Number 433, 89th Congress, 1st Session, 1965 United States Code Congress and Ad. News 1666.

2. Automobile parts and accessories (Section 201 of the bill and Section 4061 of the Code).

Generally, parts and accessories for automobile trucks, etc. are, when sold separately, presently subject to an eight percent tax based upon the manufacturer's or importer's price. Tires and inner tubes and automobile radio and television receiving sets presently are subject to other taxes in lieu of the auto parts tax. However, to the extent of the manufacturer's markup on these parts, the auto tax in effect applies here also.

Your committee concluded that the automobile parts and accessories tax is an undesirable tax because it is regressive in its impact on the incomes of purchasers and also on the grounds that an estimated thirty percent of this tax represents a business cost item. In addition, this tax presents serious compliance and administrative burdens in large part because of the large number of taxpayers. It is estimated that there are close to eight thousand manufacturers or importers of automobile parts and accessories, which is many times the number of taxpayers involved in any other manufacturers' excise tax except those on gasoline.

For the reasons indicated above, your committee's bill repeals the general eight percent tax on automobile parts and

accessories. However, parts and accessories included as original equipment on automobiles will continue to be included in the base of the passenger car tax as long as that tax remains applicable. Although the ten percent radio and television set tax is repealed effective July 1, 1965, the eight percent auto parts and accessories tax will apply to these automobile radio and television sets for the period from July 1, 1965, to January 1, 1966, the date of the repeal of the general tax on automobile parts and accessories.

Your committee's bill, although repealing the general tax on automobile parts and accessories, retains the present eight percent manufacturers' tax on truck and bus parts and accessories. Since the tax on trucks and buses is considered a highway user charge and allocated to the highway trust fund, your committee believes that it is also appropriate to classify the tax on truck and bus parts as a highway user charge. In addition it believes that attempts might be made to avoid the truck tax by selling parts separately if no tax were imposed on truck parts. The bill, therefore, retains this tax and assigns it to the highway trust fund effective January 1, 1966.

The taxable truck or bus part or accessory is one which is not suitable for use (or ordinarily used) on or in connection with, or as a component part of a passenger automobile (or trailer used with a passenger car) or house trailer. Under this definition parts and accessories which are used interchangeably on automobiles and trucks (or buses) will not be taxed. For example, a battery which ordinarily is used in either an automobile or a light truck will not be taxed as a truck part although a heavy duty battery which ordinarily is used only in a truck will be so taxed.

The eight percent manufacturer's excise tax on automotive parts and accessories is continued by your committee's bill during the remainder of 1965. At that time, the general parts and accessories tax is repealed but the eight percent tax will continue to apply to truck parts and accessories until October 1, 1972, at which time the rate will revert to the permanent rate of five percent.

Your committee's bill makes provision for floor stock refunds with respect to parts and accessories (other than truck parts and accessories) held in dealer's inventories on January 1, 1966. In general, the procedure for claiming such a refund is the same as that outlined in the case of the passenger car tax. The refunds or credits must be claimed from the Government by the manufacturer or importer and he must base this claim upon a request submitted to him by the dealer who held the inventory stock on the date of the elimination of the tax. The manufacturer or importer must also have reimbursed the dealer for the tax or have obtained his consent to the allowance of the credit or refund from the Government.

It is estimated that the repeal of the tax on parts and accessories for passenger automobiles will reduce revenues by two hundred thirty million dollars a year. Assignment of the revenues derived from the tax on truck parts and accessories to the highway trust fund will reduce general fund revenues by an additional twenty million dollars a year, but increase the revenues of the highway trust fund by a like amount.