The original documents are located in Box 42, folder "1976/03/31 HR12490 Tax Treatment of ConRail Transfer" of the White House Records Office: Legislation Case Files at the Gerald R. Ford Presidential Library.

APPROVED
MAR 3 1 1976

S 3/31/76

THE WHITE HOUSE

WASHINGTON

ACTION

Last Day: April 9

March 30, 1976

Pocket 4/1/76
Tracking 4/1/76

MEMORANDUM FOR THE PRESIDENT

FROM: JIM CANNON

SUBJECT: H.R. 12490 - Tax Treatment of ConRail Transfer

Attached for your consideration is H.R. 12490, sponsored by Representative Ullman and four others, which clarifies the tax treatment of transfers of certain railroad properties into the Consolidated Railroad Corporation under the Regional Rail Reorganization Act of 1973. The transfer of properties from the bankrupt railroads to ConRail is scheduled to take place on April 1.

A detailed discussion of the provisions of the enrolled bill is provided in OMB's enrolled bill report at Tab A.

OMB, Max Friedersdorf, Counsel's Office (Lazarus) and I recommend approval of the enrolled bill.

RECOMMENDATION

That you sign H.R. 12490 at Tab B.

Because of special circumstances in the ConRail transfer the President's signature is required on this as soon as possible today.

EXECUTIVE OFFICE OF THE PRESIDENT
OFFICE OF MANAGEMENT AND BUDGET
WASHINGTON, D.C. 20503

MAR 30 1976

MEMORANDUM FOR THE PRESIDENT

Subject: Enrolled Bill H.R. 12490 - Tax Treatment of ConRail Transfer
Sponsor - Rep. Ullman (D) Oregon and 4 others

Last Day for Action

April 9, 1976 - Friday

Because of special circumstances, it is recommended that this bill be signed by March 31.

Purpose

To clarify the tax treatment of transfers of certain railroad properties into the Consolidated Railroad Corporation under the Regional Rail Reorganization Act of 1973.

Agency Recommendations

Office of Management and Budget	Approval
Department of the Treasury	Approval
Department of Transportation	Approval
U.S. Railway Association	Approval(Informally)
Interstate Commerce Commission	No comment

Discussion

The Regional Rail Reorganization Act of 1973 (P.L. 93-236), as amended by the Railroad Revitalization and Regulatory Reform Act of 1976 (P.L. 94-210), provided for the reorganization of bankrupt railroads in the Northeast and Midwest. It established the U.S. Railway Association (USRA), a nonprofit government corporation,

to design a new rail system for the region. It also provided for the establishment of a new for-profit private corporation called the Consolidated Rail Corporation (ConRail) to acquire and operate the new system. The transfer of properties from the bankrupt railroads to ConRail is scheduled to take place on April 1. H.R. 12490 would clarify the tax treatment of any such property transfers.

Current law contains special tax provisions which apply to insolvent railroads which transfer property under court order in a receivership proceeding or in a proceeding under Section 77 of the Bankruptcy Act. The ConRail transfers, however, will not be under a court order, but rather under congressionally approved legislation. Thus it is not clear that these special provisions would apply. The enrolled bill would provide for tax treatment of the ConRail transfers similar to that which would generally apply under Section 77 proceedings.

Specifically, the enrolled bill would provide that, for tax purposes, the transfer of properties to ConRail is not to result in the recognition of gain or loss to the transferor companies, or generally to their shareholders and security holders, as long as the property is exchanged solely for stocks and securities of ConRail and USRA certificates of value. This provision would apply whether the transferors are railroad corporations or engaged in other businesses, and whether they are solvent or insolvent. It is possible, however, that the Special Court having jurisdiction over the reorganization will rule that the transferor is entitled to cash or other compensation in addition to ConRail stock and securities. In such a case, any gain would be recognized for tax purposes. However, no loss resulting from the transfer would be allowed for tax purposes.

The enrolled bill would also provide that the basis to ConRail of property received would be the same as the transferors' basis in the same assets (generally referred to as a "carryover basis"). This provision is important to ConRail because, in most cases, the properties being transferred to ConRail have a higher basis than their current fair market values, thus resulting in an advantage for depreciation purposes.

H.R. 12490 would specifically prohibit any net operating losses of a transferor from being carried over to ConRail. Existing law would be used to determine whether those net operating losses

would be retained as carryovers to the transferor for future tax years. If it is determined that these losses are retained by the transferor, the enrolled bill would provide special treatment for them. Under existing laws, net operating losses may be carried forward for a period of five years (and for railroads seven years) to be offset against income. However, it is possible that final determinations as to the value of the properties transferred to ConRail may not finally be settled within that time period. The enrolled bill would provide that any such carryovers, if not otherwise used but that would normally expire before final compensation is determined, could be used as an offset against income in the year the award is made and for the succeeding five years. It could be offset only against the awards or settlements, however.

The provisions in the enrolled bill relating to the tax treatment of ConRail property transfers are consistent with current corporate reorganization and railroad bankruptcy tax laws. It is not expected that H.R. 12490 would have any revenue effect for fiscal years 1976 and 1977. Beyond 1977, the revenue effect is speculative.

* * * * *

ConRail and USRA have both expressed the opinion that this enrolled bill should be signed prior to the transfer date of April 1 and forecast future court disputes if this is not done. The Treasury Department agrees that it would be desirable to have the bill signed by then, but believes there will be no serious complications if this is not done. We would agree that signature by March 31 would be highly desirable.

James M. Frey
Assistant Director for
Legislative Reference

Enclosures

Interstate Commerce Commission
Washington, D.C. 20423

OFFICE OF THE CHAIRMAN

March 29, 1976

Mr. James M. Frey
Assistant Director for
Legislative Reference
Office of Management and
Budget
Washington, D.C. 20503

Dear Mr. Frey:

This responds to your request for the Commission's recommendations on H.R. 12490, an enrolled bill amending section 374 of the Internal Revenue Code. The Commission did not participate in the development of this legislation, and we do not have any recommendations to make concerning its enactment.

Thank you for the opportunity to comment on this enrolled bill.

Sincerely yours,

George M. Stafford
Chairman

EXECUTIVE OFFICE OF THE PRESIDENT
OFFICE OF MANAGEMENT AND BUDGET

DATE: 3-31-76

TO: Bob Linder

FROM: Jim Frey

Attached is the USRA views letter on H.R. 12490 for inclusion in the enrolled bill file. Thanks.

OMB FORM 38
REV AUG 73

United States Railway Association

2100 Second Street, S.W.
Washington, D.C. 20595
(202) 426-1991

Arthur D. Lewis
Chairman of the Board

March 26, 1976

Honorable James Frey
Assistant Director for Legislative Reference
Office of Management and Budget
Executive Office Building
17th and Pennsylvania Avenue
Washington, D. C. 20503

Dear Mr. Frey:

In response to your inquiry of this date, relative to H.R. 12490, a bill relating to the tax treatment of the transfers of certain railroad properties into the Consolidated Rail Corporation (ConRail), this measure, in brief would make clear that the tax treatment generally applied to the transfers arising out of railroad reorganizations would apply in this instance, as well, and that, accordingly, such transfers of rail properties to ConRail will not result in the recognition of gain or loss for tax purposes to those making the transfers and that ConRail will have a carryover tax basis for such properties equal to the tax basis of those assets in the hands of the transferors.

This measure would legislatively carry out the thrust and intent of the railroad reorganizational process being conducted by the Association, and as described in the so-called Final System Plan, as further amplified by the provisions of the recently-enacted Railroad Revitalization and Regulatory Reform Act of 1976, in amendment of the Regional Rail Reorganization Act of 1973.

It is supported by both the Association and by ConRail and, we understand, has the approval of both the Department of Transportation and the Department of the Treasury. Accordingly, we would recommend Presidential signature and enactment of H.R. 12490 at the earliest practicable date, and preferably prior to April 1st, 1976, now set as the date for such conveyance to ConRail and, thus, the date when the resulting "taxable event" would take place.

Sincerely,

Arthur Lewis

OFFICE OF THE SECRETARY OF TRANSPORTATION
WASHINGTON, D.C. 20590

MAR 29 1976

Honorable James T. Lynn
Director
Office of Management and Budget
Washington, D.C. 20503

Dear Mr. Lynn:

You have asked for our comments on H.R. 12490, an enrolled bill to provide tax treatment for exchanges under the Final System Plan for ConRail.

We have reviewed the enrolled bill and the Treasury Department's testimony on the bill as introduced. We concur with Treasury's analysis in support of the legislation, and note that there are no material changes in the bill as enrolled.

We, therefore, recommend that the President sign the enrolled bill.

Sincerely,

John Hart Ely
General Counsel

DEPARTMENT OF THE TREASURY
WASHINGTON, D.C. 20220

ASSISTANT SECRETARY

March 29, 1976

Dear Sir:

This is in response to your request for the views of the Treasury Department on H. R. 12490 (94th Congress, 2nd Session) entitled "An Act to provide tax treatment for exchanges under the final system plan for ConRail" (the "Act"). The Act is part of the overall program to revitalize the railroad system in the Northeast and Midwest regions of the nation. For the reasons set forth below the Treasury Department recommends that the Act be signed into law.

Between 1967 and 1973 eight railroad corporations operating in the Northeast and Midwest entered into reorganization proceedings. In order to provide a comprehensive solution to this crisis, Congress enacted the Regional Rail Reorganization Act of 1973; this Act subsequently was amended by the Railroad Revitalization and Regulatory Reform Act of 1976. The 1973 Act established a government corporation, the United States Railway Association ("USRA"), which was directed to formulate a plan, referred to as the Final System Plan, to restructure the railroads into a "financially self-sustaining rail system." In July of 1975, USRA presented to Congress the Final System Plan in which it recommended the transfer of a substantial portion of the rail properties of seven of the bankrupt railroads to a new profit-oriented non-government corporation, ConRail. Also, USRA recommended in the Plan that certain related rail properties owned by other persons be transferred to ConRail. These transfers are scheduled to occur on April 1 of this year.

The Plan provides that, in exchange for these rail properties, the bankrupt railroads and the other transferors are to receive stock of ConRail, and in addition are to receive, from USRA, instruments referred to as Certificates of Value. These Certificates of Value in substance represent the guarantee of the Federal government that the bankrupt railroads and the other transferors will receive minimum fair value for their assets. To the extent it is determined in the future that such value has not been received, the Certificates require the government to pay the difference. The Plan also contemplates that the government, through USRA, initially will invest $2.1 billion in ConRail debentures and preferred stock. This amount eventually will be repaid assuming that, as projected by USRA, ConRail becomes financially self-sufficient.

The financial projections for ConRail's operations through 1985, prepared by USRA in connection with its formulation of the Plan, are premised on the assumption that, for tax purposes, ConRail's basis in the transferred rail properties will be the same as the basis of each of the transferors of such properties. This carryover of basis may prove to be quite advantageous to ConRail since the fair market value of these assets in most cases is significantly lower than their tax basis. In our view the 1976 Act both expressly adopted and ratified the Final System Plan, and implicitly approved ConRail's carryover tax basis.

Carryover of tax basis is consistent with the treatment provided by section 374 of the Internal Revenue Code in the case of certain railroad reorganizations. As a matter of policy, the transfer of assets to ConRail clearly falls within the intended scope of section 374. However, technical questions have been raised as to whether section 374 is in fact applicable to this transaction. Accordingly, it was thought advisable to adopt clarifying legislation which would assure the parties to the transaction tax treatment substantially similar to that provided by section 374 and certain related reorganization provisions.

The Act also deals with certain matters relating to the net operating loss carryovers of the transferor railroads. In preparing its financial projections in connection with the Final System Plan, USRA did not anticipate that the net operating loss carryovers of the bankrupt railroad corporations would be transferred to it in the reorganization. The Act therefore provides that net operating loss carryovers of the bankrupt railroads will not be transferred to ConRail. The Act does not attempt, however, to alter current law with respect to the question of whether these net operating loss carryovers will be retained by the bankrupt railroads after the reorganization transaction and after the bankruptcy proceedings.

The Act generally does not alter current law with respect to the taxable years to which the railroads can carry their net operating losses, except in the following limited situation. Certain of the transferor railroads believe they are not receiving fair compensation for the property taken from them in connection with the reorganization and it is anticipated that they will shortly commence legal proceedings based on this claim. The bankrupt railroads currently have net operating loss carryovers which could be used to offset taxable income derived

from court awards, or settlements, relating to these claims, if received before such carryovers expire. However, as is generally the case in litigation arising in connection with bankruptcy, these court proceedings will probably not be resolved for many years and it is probable that these net operating loss carryovers will have expired prior to the receipt of any such awards or settlements. The Act contains a provision which permits these currently available net operating loss carryovers, if not otherwise utilized and if retained by the railroads after the transfer and the bankruptcy proceedings, to be carried forward to the year in which an award is made, or settlement is reached, and to the five succeeding years. However, these loss carryovers can be utilized only to offset taxable income which results from such awards or settlements in such years.

It is estimated that the Act will produce no revenue effect for fiscal years 1976 and 1977. The revenue effect of the Act for fiscal years thereafter is highly speculative since it depends on whether various parties to the transaction generate income in such years in excess of loss carryovers which would be available to them under present law.

With respect to the reorganization, the Act provides for tax treatment which is substantially the same as that presently applicable to similar transactions. With respect to treatment of net operating loss carryovers, the Act provides limited but potentially significant relief in a situation which otherwise could result in inequitable treatment of the bankrupt corporations. Accordingly, the Treasury Department recommends that the Act be signed into law.

Sincerely yours,

William M. Goldstein

William M. Goldstein
Acting Assistant Secretary

Mr. James M. Frey
Assistant Director
for Legislative Reference
Office of Management and Budget
New Executive Office Building
Washington, D.C. 20503

To - 3-30-76
J. Cavanaugh
4:15 p.m.

EXECUTIVE OFFICE OF THE PRESIDENT
OFFICE OF MANAGEMENT AND BUDGET
WASHINGTON, D.C. 20503

MAR 30 1976

MEMORANDUM FOR THE PRESIDENT

Subject: Enrolled Bill H.R. 12490 - Tax Treatment of ConRail Transfer
Sponsor - Rep. Ullman (D) Oregon and 4 others

Last Day for Action

April 9, 1976 - Friday

Because of special circumstances, it is recommended that this bill be signed by March 31.

Purpose

To clarify the tax treatment of transfers of certain railroad properties into the Consolidated Railroad Corporation under the Regional Rail Reorganization Act of 1973.

Agency Recommendations

Office of Management and Budget	Approval
Department of the Treasury	Approval
Department of Transportation	Approval
U.S. Railway Association	Approval (Informally)
Interstate Commerce Commission	No comment

Discussion

The Regional Rail Reorganization Act of 1973 (P.L. 93-236), as amended by the Railroad Revitalization and Regulatory Reform Act of 1976 (P.L. 94-210), provided for the reorganization of bankrupt railroads in the Northeast and Midwest. It established the U.S. Railway Association (USRA), a nonprofit government corporation,

THE WHITE HOUSE

ACTION MEMORANDUM WASHINGTON LOG NO.:

Date: March 30 Time: 420pm

FOR ACTION: Judy Hope
Max Friedersdorf
Ken Lazarus ✓

cc (for information): Jack Marsh
Jim Cavanaugh
Ed Schmults

FROM THE STAFF SECRETARY

DUE: Date: March 31 Time: 900am

SUBJECT:

H.R. 12490 - Tax Treatment of ConRail Transfer

ACTION REQUESTED:

____ For Necessary Action ____ For Your Recommendations

____ Prepare Agenda and Brief ____ Draft Reply

__X__ For Your Comments ____ Draft Remarks

REMARKS:

Please return to Judy Johnston, Ground Floor West Wing

No objection -- Ken Lazarus 3/31/76

OMB recommends this bill be signed prior to March 31.

PLEASE ATTACH THIS COPY TO MATERIAL SUBMITTED.

If you have any questions or if you anticipate a delay in submitting the required material, please telephone the Staff Secretary immediately.

James M. Cannon
For the President

THE WHITE HOUSE

ACTION MEMORANDUM WASHINGTON LOG NO.:

Date: March 30 Time: 420pm

FOR ACTION: Judy Hope ✓
Max Friedersdorf
Ken Lazarus

cc (for information): Jack Marsh
Jim Cavanaugh
Ed Schmults

FROM THE STAFF SECRETARY

DUE: Date: March 31 Time: 900am

SUBJECT:

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ACTION REQUESTED:

____ For Necessary Action ____ For Your Recommendations

____ Prepare Agenda and Brief ____ Draft Reply

__X__ For Your Comments ____ Draft Remarks

REMARKS:

Please return to Judy Johnston, Ground Floor West Wing

Approval JRH

OMB recommends this bill be signed prior to March 31.

Concur. JRH

PLEASE ATTACH THIS COPY TO MATERIAL SUBMITTED.

If you have any questions or if you anticipate a delay in submitting the required material, please telephone the Staff Secretary immediately.

James M. Cannon
For the President

THE WHITE HOUSE

ACTION MEMORANDUM WASHINGTON LOG NO.:

Date: March 30 Time: 420pm

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SUBJECT:

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ACTION REQUESTED:

____ For Necessary Action ____ For Your Recommendations

____ Prepare Agenda and Brief ____ Draft Reply

__x__ For Your Comments ____ Draft Remarks

REMARKS:

Please return to Judy Hohnston, Ground Floor West Wing

PLEASE ATTACH THIS COPY TO MATERIAL SUBMITTED.

If you have any questions or if you anticipate a delay in submitting the required material, please telephone the Staff Secretary immediately.

K. R. COLE, JR.
For the President

THE WHITE HOUSE

ACTION MEMORANDUM WASHINGTON LOG NO.:

Date: March 30 Time: 420pm

FOR ACTION: Judy Hope OK
Max Friedersdorf OK
Ken Lazarus

cc (for information): Jack Marsh
Jim Cavanaugh
Ed Schmults

FROM THE STAFF SECRETARY

DUE: Date: March 31 Time: 900am

SUBJECT:

H.R. 12490 - Tax Treatment of ConRail Transfer

ACTION REQUESTED:

____ For Necessary Action ____ For Your Recommendations

____ Prepare Agenda and Brief ____ Draft Reply

__x__ For Your Comments ____ Draft Remarks

REMARKS:

Please return to Judy Johnston, Ground Floor West Wing

OMB recommends this bill be signed prior to March 31.

PLEASE ATTACH THIS COPY TO MATERIAL SUBMITTED.

If you have any questions or if you anticipate a delay in submitting the required material, please telephone the Staff Secretary immediately.

James M. Cannon
For the President

THE WHITE HOUSE

WASHINGTON

March 30, 1976

MEMORANDUM FOR: JIM CAVANAUGH

FROM: MAX L. FRIEDERSDORF

SUBJECT: H.R. 12490 - Tax Treatment of ConRail Transfer

The Office of Legislative Affairs concurs with the agencies that the subject bill be signed.

Attachments

94TH CONGRESS } HOUSE OF REPRESENTATIVES { REPORT
2d Session } { No. 94-940

TAX TREATMENT OF EXCHANGES UNDER THE FINAL SYSTEM PLAN FOR CONRAIL

MARCH 22, 1976.—Committed to the Committee of the Whole House on the State of the Union and ordered to be printed

Mr. ULLMAN, from the Committee on Ways and Means, submitted the following

REPORT

[To accompany H.R. 12490]

The Committee on Ways and Means, to whom was referred the bill (H.R. 12490) to provide tax treatment for exchanges under the final system plan for ConRail, having considered the same, report favorably thereon with amendments and recommend that the bill as amended do pass.

The amendments are as follows:

Page 2, line 6, strike out "section 303(b)(1) or 305(d)(2)" and insert in lieu thereof "section 303 or 305(d)".

Page 2, beginning in line 9, strike out "and certificates of value" and all that follows down through line 10, and insert in lieu thereof ", securities of such Corporation, certificates of value of the United States Railway Association, or any combination thereof."

Page 3, beginning in line 17, strike out "owned, leased, or otherwise controlled" and insert in lieu thereof "leased, operated, or controlled".

Page 4, line 21, strike out "stock in" and insert in lieu thereof "stock of".

Page 5, line 9, strike out "stock in" and insert in lieu thereof "stock of".

Page 5, beginning in line 10, strike out "and certificates of value" and all that follows down through line 11, and insert in lieu thereof ", securities of such Corporation, certificates of value of the United States Railway Association, or any combination thereof.' "

Page 5, after line 11, insert the following new sentence:

Clause (i) of section 356(d)(2)(B) of such Code (relating to receipt of additional consideration) is amended by striking out "subsection (c) thereof" and inserting in lieu thereof "subsection (c) or (d) thereof".

Page 5, strike out line 12 and all that follows down through line 20 on page 6, and insert in lieu thereof the following:

(d) USE OF EXPIRED NET OPERATING LOSS CARRYOVERS TO OFFSET INCOME ARISING FROM CERTAIN RAILROAD REORGANIZATION PROCEEDINGS.—Section 374 of such Code (relating to gain or loss not recognized in certain railroad reorganizations) is amended by adding at the end thereof the following new subsection:

"(e) USE OF EXPIRED NET OPERATING LOSS CARRYOVERS TO OFFSET INCOME ARISING FROM CERTAIN RAILROAD REORGANIZATION PROCEEDINGS.—

"(1) IN GENERAL.—If—

"(A) any corporation receives or accrues any amount pursuant to—

"(i) an award in (or settlement of) a proceeding under section 77 of the Bankruptcy Act,

"(ii) an award in (or settlement of) a proceeding before the special court to carry out section 303(c), 305, or 306 of the Regional Rail Reorganization Act of 1973,

"(iii) an award in (or settlement of) a proceeding in the Court of Claims under section 1491 of title 28 of the United States Code, to the extent such proceeding involves a claim arising under the Regional Rail Reorganization Act of 1973, or

"(iv) a redemption of a certificate of value of the United States Railway Association issued to such corporation under section 306 of such Act,

"(B) any portion of such amount is includible in the gross income of such corporation for the taxable year in which such portion is received or accrued, and such taxable year begins not more than 5 years after the date of such award, settlement, or redemption, and

"(C) the net operating loss of such corporation for any taxable year—

"(i) was a net operating loss carryover to, or arose in, the first taxable year of such corporation ending after March 31, 1976 (or, in the case of a proceeding referred to in subparagraph (A)(i) which began after March 31, 1976, ending after the beginning of such proceeding), but

"(ii) solely by reason of the lapse of time, is not a net operating loss carryover to the taxable year referred to in subparagraph (B),

then such net operating loss shall be a net operating loss carryover to the taxable year described in subparagraph (B) but only for use (to the extent not theretofore used under this subsection to offset other amounts) to offset the portion referred to in subparagraph (B).

"(2) SPECIAL RULE.—For purposes of paragraph (1)(C)(i), a corporation which was a regulated transportation corporation (within the meaning of section 172(j)) for its last taxable year ending on or before March 31, 1976, shall be treated as such a regulated transportation corporation for its first taxable year ending after such date."

I. SUMMARY

The bill, H.R. 12490, deals with the tax treatment of transfers of certain railroad properties into the Consolidated Rail Corporation (ConRail). Under the Regional Rail Reorganization Act of 1973, the United States Railway Association (USRA) was directed to develop a "final system plan" to restructure the midwest and northeast railroad system. Under the Railroad Revitalization and Regulatory Reform Act of 1976, Congress approved the final system plan, as previously formulated by USRA. Under this plan, in order to provide a financially self-sustaining rail service, eleven insolvent railroads (along with many of their subsidiaries and affiliates) are to transfer their rail properties to ConRail on or about April 1, 1976. This bill deals with the tax questions raised by the transfer of these properties to ConRail and to some extent the effect of the restructuring on the transferring companies, and their shareholders and creditors.

The bill provides that the transfer of rail properties to ConRail is not to result in the recognition of gain or loss to the transferor companies. The shareholders and security holders of the transferors will also generally not recognize gain or loss on exchanging their existing interests for ConRail stock and USRA certificates of value. The bill also provides that the basis of the assets transferred to ConRail is to be the same in ConRail's hands as in the hands of the transferors.

In addition, the bill provides that no net operating losses are to be transferred from the transferors to ConRail. These losses are generally to be treated in the manner provided by present law in the case of railroad bankruptcies. However, the bill contains a provision that net operating losses eligible for carryover (at the time of transfer of property to ConRail) to years after the date of the transfer are to be kept alive for tax purposes beyond their noramal expiration date, but only for use by the transferor against any future income arising from awards of the courts (and the redemption of certificates of value) with respect to the transfer of their rail assets to ConRail. This provision is to apply in the case of railroad bankruptcy cases generally as well as in the case of the transfers to ConRail.

II. REASONS FOR THE BILL

Congressionally approved railroad reorganizations

As a result of the financial problems encountered by the rail transportation industry in the northeastern and midwestern regions of the United States, the Congress enacted the Regional Rail Reorganization Act of 1973 ("1973 Rail Act").[1] The purpose of this act was to provide a way for the Federal Government to rehabilitate and reorganize the insolvent railroads in these regions into a "financially self-sustaining" rail system capable of providing the railroad service needed.[2]

The 1973 Rail Act established the United States Railway Association (USRA), a nonprofit government corporation. USRA was authorized to study the existing rail services of the affected regions and to prepare a "final system plan" for the railroad reorganization, subject to approval of Congress. A "special court," comprised of three Federal Judges, was authorized to conduct virtually all judicial proceedings concerning implementation of the final system plan.

The 1973 Rail Act also required formation of the Consolidated Rail Corporation ("ConRail"), a nongovernment, for-profit corporation. ConRail was authorized to acquire, operate and rehabilitate those rail properties designated by the final system plan to be conveyed to it. Stock and other securities are to be issued by ConRail to the railroads in exchange for the acquired rail properties.

On January 23, 1976, Congress enacted the Railroad Revitalization and Regulatory Reform Act of 1976,[3] which adopted the final system plan and other provisions to implement the reorganization. This legislation amended the 1973 Rail Act to provide for ConRail's capital structure and to provide for the funding necessary to enable ConRail to proceed with the acquisition and rehabilitation of the rail properties. The legislation provides that ConRail debentures and series A preferred stock are to be issued to USRA. USRA will purchase these securities with Federal funds in currently authorized maximum amounts of $1 billion for the debentures and $1.1 billion for the series A

[1] The Act was signed into law on January 2, 1974 (P.L. 93–236).

[2] It was contemplated that the reorganization would include the systems operated by a group of bankrupt railroads in the midwest and northeast. The primary bankrupts covered by the planned reorganization are the Penn Central Transportation company, Central Railroad Company of New Jersey, Lehigh Valley Railroad Company, Reading Company, Erie Lackawanna Railroad Company, Reading Company, Erie Lackawanna Railroad Company, Lehigh and Hudson River Railway Company, and the Ann Arbor Railroad Company. All of these railroads have entered into reorganization proceedings under section 77 of the Bankruptcy Act (11 U.S.C. 205), which governs the reorganization of railroad corporations.

[3] The bill was signed into law by the President on February 5, 1976 (P.L. 94–210).

preferred stock. ConRail will use this capital to modernize its acquired rail properties, acquire equipment, refinancee preacquisition expenditures to improve rail property acquired under the final system plan, and provide working capital.

Series B preferred stock and common stock of ConRail are to be issued to the bankrupt railroads (and to other transferors under the final system plan) in exchange for the rail properties transferred to ConRail. Initially, however, the series B preferred stock and the common stock will be deposited with the special court, pending that court's determination as to whether the exchanges are fair and equitable to the railroads. In addition, there will be deposited with the special court for distribution to the transferors "certificates of value" issued by USRA. The purpose of the certificates of value is basically to assure that the package of series B preferred stock and common stock received by each railroad will have a cash value in 1987 (or earlier) equal to a value which, as determined by the courts, represents fair payment to the transferors for the rail properties conveyed to ConRail.

The certificates of value will be conveyed on a one-for-one basis with each share of series B preferred stock which is distributed by the special court to the transferors. The certificates will be redeemed by USRA on a date specified by it, but not later than December 31, 1987. The redemption value of the certificates will be subsequently determined by the special court.[4]

The transfer of properties to ConRail in return for stock of ConRail and certificates of value of USRA is scheduled to occur on April 1 of this year.

Tax treatment of railroad reorganizations

Under present law corporate reorganizations generally result in the nonrecognition of gain or loss to the transferor corporation and its shareholders and security holders (secs. 354 and 361), and a carryover tax basis to the acquiring corporation for the assets or stock it receives for its own stock and securities (sec. 362). A "carryover" basis means that the acquiring company takes as the basis in the acquired property the same basis the property had in the hands of the transferor company (or where stock is acquired, the same basis the stock had in the hands of its shareholders).

The transferor corporation generally takes as its basis for the stock or securities of the acquiring company the basis it had in the assets or stock given up (sec. 358). If the transferor company distributes these securities to its own stock or security holders (in exchange for their interests in the transferor company), they also take as the basis the basis of the securities they give up (sec. 358).

If the transferor company or its shareholders receive any other property (usually money) in addition to stock or securities of the acquiring company (which is referred to as "boot" received in the exchange), and it a gain is realized on the overall exchange, the gain is taxable up to the amount of the boot (sec. 356).[5]

However, if a transferor company or its shareholders realize a loss (rather than a gain) on the overall exchange, any boot received does not give rise to a deductible loss.

In the case of insolvency reorganizations, creditors of the insolvent or bankrupt company may become interested in acquiring an ownership interest in the company in order to increase their chances of eventually recovering the entire amount of their claims. Up to the time of the reorganization, however, creditors are not equity holders. Largely because of this situation, Congress has enacted special tax rules relating to the treatment of reorganizations involving bankrupt companies (secs. 371–372).

The tax law also provides special rules specifically for insolvent railroads (under sec. 374). In general, the tax rules for insolvent railroad corporations are similar to the rules for corporate reorganizations generally. Under these rules, the debtor railroad corporation generally recognizes neither gain nor loss when its assets are transferred to another corporation (often formed by the creditors). If the bankrupt transferor corporation receives money or other boot, which is not distributed to the shareholders pursuant to the plan of reorganization, gain is recognized to the extent of the boot. However, in these circumstances also, no loss is to be recognized by the transferor. Shareholders and security holders (including creditors) of the insolvent railroad do not recognize gain or loss on surrendering their interests in their corporation for equity interests in the new company (sec. 354(c)).

The new company takes a carryover basis in the assets of the bankrupt transferor.[6] Congress has made these tax results available in railroad insolvency cases without requiring the parties to comply with all of the provisions which reorganizations generally must satisfy.[7]

[4] This value will be based on the value of the rail assets transferred, plus compound interest at 8 percent and compensation (if any) awarded for preconveyance "erosion" in the estate of a transferor, less the market value of the preferred and common stock (on the redemption date) and any dividends paid on this stock, and less the value of any other benefits or consideration received by the transferor railroads.

[5] A "conduit" rule for boot is also provided to prevent taxing boot twice: a transferor company is not taxable if it distributes the boot to its own shareholders or security holders (sec. 361(b)).

[6] A carryover basis is usually important to the new company where the current fair market value of the debtor's assets is lower than the historic cost basis of the assets on the debtor's books. In such a situation, a carryover basis gives the acquiring company a higher basis for future depreciation and other tax purposes than would a current fair market value basis.

[7] For example, insolvency reorganizations are not conditioned on the "solely for voting stock" requirement which applies to a conventional reorganization under section 368(a)(1)(B) or (C) of the code. Nor must there be a transfer of "substantially all" the debtor's assets to the successor company, as is required if the reorganization is to qualify under section 368(a)(1)(C).

The present tax rules for bankrupt railroads (under sec. 374) only apply to property of a railroad corporation transferred under an order of a court having jurisdiction of the railroad corporation in a receivership proceeding or in a proceeding under section 77 of the Bankruptcy Act (which applies specifically to railroad bankruptcies). Your committee understands that the railroad reorganization under the final system plan for ConRail does not meet the technical requirements under the existing tax rules for insolvent railroads (see 374). This is because the reorganizations involved in this case are not under section 77 of the Bankruptcy Act, but rather will occur under congressionally approved legislation. In addition, your committee understands that since the transferor railroads may possibly receive large amounts of cash in future years, as a result of the valuation determinations of the assets transferred to ConRail, the acquired company (or its shareholders) may not meet the "continuity of interest" rules, which require (in tax free reorganizations generally) that no more than one-half of the total consideration be in the form of cash. Your committee believes that since Congress has specifically provided for these railroad reorganizations, the existing tax treatment for reorganizations of insolvent railroads should apply to the ConRail reorganization. In the case of the cash payments, your committee believes that the traditional continuity of interest concepts should not apply in this case but that the cash payments should be treated as "boot."

The tax treatment provided under existing law is important to the ConRail reorganization because, in most of the cases, the rail properties being transferred to ConRail have a basis which is higher than their current fair market values. By applying the nonrecognition treatment under present law to this reorganization, ConRail will have a carryover basis in the assets which, for depreciation purposes, is higher than the current fair market values (which would be the basis of the properties to ConRail if the reorganization were taxable). Your committee understands that when USRA formulated its final system plan, it was assumed that ConRail would obtain the benefit of a carryover tax basis for the railroad properties.

Another factor considered by your committee was the treatment of the net operating losses of the transferor railroads in existence at the time of the ConRail transfer. Present law (in insolvency reorganizations generally) is not clear on whether various tax attributes of the bankrupt company (such as net operating losses) carry over to the successor company or are retained by the transferor company. Since ConRail neither needs nor wants the net operating losses of the transferor companies, the bill specifically prohibits any net operating losses of a transferor from being carried over to ConRail.

In the case of the transferor companies, however, your committee intends that existing law (applicable in the case of bankruptcies) is to apply in determining whether a transfer company in this situation retains its own net operating losses as carryovers after the transfer of its rail assets to ConRail or after its own bankruptcy proceedings.

If (or to the extent) it is determined that the net operating losses are retained by the transferor, your committee provides a special rule with respect to any such loss carryovers of a transferor which will keep them available for compensation paid under the rail acts to the transferor companies. This is needed because, as indicated above, the rail acts provide a special court to determine the amount of the appropriate compensation and this determination may not be made until several years in the future. In the meantime, net operating losses that would have been available to offset any income recognized from the compensation, if paid immediately, may expire and thus not be available. In view of this situation your committee has provided a rule which, in effect, revives a transferor's net operating losses that may otherwise have expired, solely by reason of the lapse of time, before the courts determine the exact amounts of compensation to the railroads. When these determinations are made, the expired net operating losses may be used to offset the income recognized by the transferor railroads.

III. EXPLANATION OF BILL

Nonrecognition treatment

Your committee's bill extends to transfers of rail properties in the ConRail reorganization the same nonrecognition treatment which is available generally under present law to reorganizations of insolvent railroads (sec. 374). The bill provides, in general, that no gain or loss is to be recognized when, in order to carry out the final system plan, rail properties of a transferor railroad are transferred to ConRail in exchange solely for stock or securities of ConRail and USRA certificates of value.

The effects of this nonrecognition treatment with respect to the various parties involved in the ConRail reorganization are described below.

ConRail.—The bill provides that ConRail's basis in the rail properties which it acquires from the transferor railroads generally is to be the same as the transferors' basis in the same assets (referred to generally as a "carryover" basis). However, ConRail's carryover basis in the properties is to be increased by the gain, if any, recognized by any transferor (ConRail will recognize no gain or loss on its receipt of rail properties in exchange for its own stock or securities (sec. 1032).)

Transferor companies.—The bill applies to all transferors to ConRail regardless of whether the transferors are railroad corporations or are engaged in other businesses, and regardless whether the transferor is solvent or is undergoing bankruptcy.[8] In the case of a transferor, the bill provides that no gain or loss is to be recognized on the exchange with ConRail.

However, if the special court should order that additional compensation payments be made to the transferors in the form of cash or other property, and if any transferor realizes a gain on its overall exchange with ConRail, the portion of the gain equal to the amount of "boot" will be taxable. (This tax treatment is the same as the rules in present law for reorganizations generally). The bill also follows existing law in providing that "boot" will not be taxable to a transferor if the railroad distributes the boot to its own share-

[8] The 1973 and 1976 rail acts permit ConRail to acquire rail properties from both bankrupt railroads and from certain corporations operated or controlled by the railroads or which are leased by the various railroads. Some of these other companies are technically not railroads within the definition in section 77(m) of the Bankruptcy Act; some are also in a solvent condition.

holders or security holders. (In the case of the bankrupt transferors, any distributions which they make to their own shareholders or creditors will be made under the supervision of the court supervising their own Bankruptcy Act proceedings.)

If a transferor realizes a loss (rather than a gain) on its overall exchange with ConRail, no portion of the loss may be allowed even if the transferor has received money or property other than ConRail stock or securities and USRA certificates of value. (This rule is also in accord with long-established rules for tax-free reorganizations).

The bill also follows present law in providing that ConRail's assumption of certain liabilities of the bankrupt railroads (principally those involving equipment obligations) will not be treated as boot received by the transferors.[9]

In the case of ConRail stock and USRA certificates of value received in the exchange by the transferor railroad, the transferor's basis in the stock and certificates is to be the basis which it had in its rail properties transferred to ConRail. Thus, both ConRail and the transferor railroads will use the transferors' asset basis.[10]

Shareholders and creditors of the transferor companies.—The bill provides that no gain or loss is to be recognized by any shareholder or creditor of a transferor who surrenders stock or a debt interest (amounting to a security) in the transferor and receives in exchange ConRail stock and USRA certificates of value.[11]

If the distribution includes "boot" (that is, money or property other than ConRail stock or securities or USRA certificates of value), a shareholder or security holder who realizes gain on the exchange will be taxable to the extent of the boot received.[12]

With respect to basis, a shareholder or security holder will take a substituted basis in the ConRail stock or USRA certificates of value which is received; that is, the basis will equal the basis the shareholder or security holder had in the stock or security of the bankrupt railroad.

Your committee's bill does not prescribe how a railroad's basis (or that of any of its shareholders or creditors) is to be allocated among ConRail common stock, series B preferred stock and USRA certificates of value. Since the values of the stock and certificates will change over time (probably in inverse relation to each other), it will be difficult at the conveyance date (April 1, 1976 to make a proper allocation of the railroads' asset basis between the stock and the certificates. In light of this situation, an allocation of basis made as of the conveyance date might result in improper measurement of taxable income or loss on the

[9] The provision of present law, which adopts this rule for corporate reorganizations generally is section 357 of the Code.

[10] Each railroad's "substituted" basis in the ConRail stock and USRA certificates of value will be increased (under sec. 358) by the amount of gain, if any, which the transferor recognizes on the exchange.

[11] Under present law, shareholders or security holders in a bankrupt railroad are not subject to the excess principal amount rule of sec. 354(a)(2); the bill follows the same treatment in the ConRail reorganization. Thus, if a shareholder of a transferor receives ConRail debt securities (as possibly could be ordered by the special court), he will also receive nonrecognition treatment.

The bill makes no change in the rule under present law that a creditor's claim against the debtor company must be a "security" interest in order that he will not recognize gain or loss on exchanging his interest for ConRail stock in an acquiring company. A short-term note holder or general creditor who is not considered to hold a "security" interest will therefore recognize gain or loss on such an exchange. See Rev. Rul. 59-222, 1959-1 Cum. Bull. 80.

[12] Under present law, boot received in a reorganization of a bankrupt railroad under section 374 is subject to the dividend-effect test in sec. 356 to determine whether the boot is taxable as ordinary income or capital gain. The bill follows present law in this regard, so that boot received by a shareholder or security holder of a transferor, will be subject to the dividend-effect test (sec. 356).

separate sale of ConRail stock or certificates of value, or on a redemption of a certificate of value.

In order to prevent potential problems of this type, the bill provides that so long as the stock and certificates are held together in a single "package" by either a transferor railroad or by a shareholder or creditor of the railroad, the holder may not allocate his basis specifically between the stock and the certificates. Only at the time that the owner of the stock and certificates sells the instruments separately (or the certificates of value are redeemed), is a specific allocation of basis to be made among the ConRail common and preferred stock (or other ConRail securities, if any) and the USRA certificates of value. As a result, the bill provides that the allocation of basis then is to be made under rules provided in regulations prescribed by the Internal Revenue Service. It is expected that after the special court determines the compensation to be paid in the transfers, the allocation of basis by the Internal Revenue Service under the regulations will take into account respective values, including any established by the special court.

Net operating losses

No carryover to ConRail.—The bill provides that where ConRail (or any of its subsidiaries) acquires assets from the transferor companies (railroads and nonrailroads), ConRail is not to succeed to any net operating loss carryovers of these companies.[13] In the few situations where ConRail acquires stock in a subsidiary owned by a transferor, the assets of the subsidiary are to remain with the existing corporate entity and only the stock ownership of the subsidiary is to change.[14] In these situations, any net operating loss carryover which the subsidiary may have will remain with the subsidiary and are to be available against that company's future income.[15]

Net operating loss carryovers of transferors.—The bill provides for the use of what would otherwise be expired net operating loss carryovers to offset income arising from railroad bankruptcy reorganizations generally. This provision covers any awards (or settlements) resulting from a proceeding in the ConRail reorganization as well as in other railroad bankruptcy reorganizations.

Under present law, taxpayers are generally allowed to carry over unused net operating losses to apply against income received in the succeeding five years. However, a regulated transportation corporation (including a railroad) is allowed (under sec. 172(b)(1)(C)) to carry over a net operating loss to the following seven years.[16] For a corporation to use the additional two-year carryover (from five to seven years) allowed regulated transportation corporations, it must be a regulated

[13] Your committee intends that the treatment of net operating losses transferring to ConRail will be governed exclusively by the provisions of this bill.

[14] In some cases the transferor railroad presently owns all the stock in a subsidiary. In other cases, it owns either a controlling stock interest or a minority stock interest. ConRail will acquire whatever amount of stock in a designated company the transferor owns. The stock holdings in the subsidiary not presently owned by a transferor railroad will not be changed.

[15] Under this provision of the bill, a company whose stock is acquired by ConRail would retain its own net operating loss carryovers. Therefore, the prohibition in the bill against ConRail succeeding to net operating loss carryovers applies only to acquisitions by ConRail of assets other than stock.

[16] A regulated transportation corporation is generally defined in Code sec. 172(j) as a corporation whose rates must be approved by a governmental agency and which realizes 80 percent or more of its gross income (other than dividends and capital gains and losses) from the furnishing of transportation services (including rail transportation services).

transportation corporation not only in the loss year, but also in the sixth and seventh carryover years (sec. 172(j)(3)).

As indicated above (in the Reasons for the Bill), your committee makes no determination as to whether, and to what extent, the net operating losses of a bankrupt transferor company survive either a reorganization, transfer or bankruptcy proceedings for the benefit of that company. The bill does not give or assure to a transferor railroad in the ConRail reorganization the benefit of any net operating losses, or of any carryover period for such losses, to which the transferors would not be entitled apart from the bill. Your committee intends existing law to govern questions of this nature. However, to the extent it is determined that net operating losses of a transferor company do survive as carryovers by that company, a special problem arises in the ConRail reorganization (as well as in other railroad bankruptcies) where compensation for the transfer of the railroads' assets is to be determined by the courts and the final outcome of such litigation may not occur until some time in the future.[17] In the meantime, the net operating loss carryovers may have expired unused by the time the compensation is actually paid to the transferors.

Your committee's bill provides that any net operating loss carryovers which are available to the transferor railroads (including the transferors to ConRail) at the time of the transfers but which are unused after the expiration of the carryover period available under present law, are to be revived to be available to offset certain income which is later received or accrued by the company. The net operating loss carryovers are to be revived in the case of: (1) an award in (or settlement of) a bankruptcy proceeding under section 77 of the Bankruptcy Act; (2) an award in (or settlement of) a proceeding before the special court under the Rail Act of 1973; (3) an award in (or settlement of) a proceeding in the Court of Claims under the Tucker Act[18] to the extent the proceeding involves a claim arising under the Rail Act of 1973; and (4) a redemption of an USRA certificate of value (under sec. 306 of the Rail Act of 1973). The net operating loss revival in these cases applies only to taxable income which arises from an amount received or accrued in these specified circumstances. It does not apply, for example, to taxable income attributable to other court proceedings, such as tort or contract litigation.

This provision of the bill applies to the extent the amounts received are properly includable in income by the bankrupt transferor railroad

[17] A bankrupt railroad which transfers assets in a proceeding under either section 77 of the Bankruptcy Act or under the Rail Act of 1973 may receive a cash award from the court having jurisdiction over this proceeding. It is possible (and indeed likely in the case of a transfer under the 1973 Rail Act) that any such cash award will be paid at a time long after the carryover period has expired for net operating losses which were incurred before the court proceedings were begun.

[18] The Tucker Act (28 U.S.C. 1491) provides (in relevant part) that the Court of Claims has jurisdiction to render judgment upon "any claim against the United States founded either upon the Constitution, or any Act of Congress, or any regulation of an executive department, or upon any express or implied contract with the United States, or for liquidated or unliquidated damages in cases not sounding in tort."

In upholding the constitutionality of the Rail Act of 1973, the U.S. Supreme Court has held that the Rail Act does not bar any transferor railroad from bringing suit under the Tucker Act to litigate its claim that the Rail Act caused a taking of private property for public use without payment of just compensation, in violation of the Fifth Amendment of the Constitution. *Regional Rail Reorganization Act Cases*, 419 U.S. 102 (1974). Since an action under the Tucker Act is available to the railroads which will convey rail properties to ConRail (in addition to the transferors' rights in the special court), your committee believes it is appropriate and consistent with the Supreme Court decision to permit a revival of net operating losses against any Tucker Act recovery which might occur

for a taxable year and (in order to cover delayed payments) for 5 years after the date of the specific award, settlement, or redemption.

In the case of an award, settlement or redemption in connection with a proceeding under the 1973 Rail Act, the net operating losses of the transferor corporation which are eligible for revival are limited to those which arose in, or were carryovers to, the first taxable year of the corporation which ends on or after April 1, 1976 (the date on which the rail property transfers under the 1973 Rail Act are to occur). Where the transfer of rail properties does not take place under the 1973 Rail Act, as in the case of a regular railroad reorganization under section 77 of the Bankruptcy Act, the revival provision will apply only to those losses which arose in, or were a carryover to, the first taxable year of the transferor which ends after commencement of the section 77 bankruptcy proceeding. The provision relating to bankruptcy reorganizations in general (those where property will be transferred other than under the 1973 Rail Act) applies for taxable years ending after March 31, 1976.

It has been pointed out to your committee that some of the bankrupt railroads which will transfer properties to ConRail on April 1 may cease to be regulated transportation corporations for their tax year during which the transfer takes place. As a result, these companies (were it not for the provision referred to below) would be allowed to revive only those net operating loss carryovers which arise from their five taxable years immediately before 1976 (i.e., 1971–1975). Since the railroads transferring assets to ConRail were regulated transportation corporations during the years before the transfer and incurred losses in a number of years preceding the five-year period, your committee believes that it is appropriate to accord those companies which cease to be regulated transportation corporations because of the ConRail transfer an opportunity to revive net operating losses which are carryovers from the seven tax years immediately preceding the year of the transfer. As a result, the bill provides that, for purposes of determining which net operating loss carryovers are potentially eligible for this revival provision, a corporation which was a regulated transportation corporation in its last taxable year ending before the date of the planned transfers to ConRail, is to be considered to be a regulated transportation corporation during the taxable year in which the April 1, 1976, ConRail transfers occur. Thus, a qualifying calendar year transferor to ConRail will be entitled to revive not only its loss carryovers from 1971 through 1975, but also any net operating losses sustained in 1969 and 1970 which remained unused at the end of 1976.[19]

IV. EFFECT ON THE REVENUES OF THE BILL AND VOTE OF THE COMMITTEE IN REPORTING THE BILL

In compliance with clause 7 of rule XIII of the Rules of the House of Representatives, the following statement is made relative to the effect on the revenues of this bill. Although the bill would become effec-

[19] It should be noted that net operating losses from 1971 through 1975 will be eligible for revival under the bill only to the extent that such losses are not used to offset taxable income of the transferor, if any, during the five carryover years to which the same losses may be carried under present law.

tive for taxable years ending after March 31, 1976, it is estimated there will be no revenue effect for fiscal years 1976 or 1977 and for other immediate future fiscal years because both the transferee (ConRail) and the major bankrupt transferor railroads will, under existing law, incur no Federal income tax liabilities due to the anticipated net operating losses (in the case of ConRail) and large net operating loss carryovers (in the case of the major transferor railroads).

In compliance with clause 2(l)(2)(B) of rule XI of the Rules of the House of Representatives, the following statement is made relative to the vote by the committee on the motion to report the bill. The bill was ordered reported by a voice vote.

V. OTHER MATTERS REQUIRED TO BE DISCUSSED UNDER HOUSE RULES

In compliance with clauses 2(l)(3) and 2(l)(4) of rule XI of the Rules of the House of Representatives, the following statements are made.

With respect to subdivision (A) of clause 3 relating to oversight findings, it was as a result of your committee's oversight activity concerning the tax treatment of the ConRail acquisition of rail properties and of other railroad reorganizations that it concluded the provisions of this bill are appropriate to cover certain aspects of the ConRail transfer and other railroad reorganizations.

In compliance with subdivision (B) of clause 3 of rule XI of the Rules of the House of Representatives, the committee states that the changes made to this bill involve no new budget authority.

With respect to subdivisions (C) and (D) of clause 3 of rule XI of the Rules of the House of Representatives, your committee advises that no estimate of comparison has been submitted to your committee by the Director of the Congressional Budget Office relative to the changes made by your committee, nor have any oversight findings or recommendations been submitted to your committee by the Committee on Government Operations.

In compliance with clause 2(l)(4) of rule XI of the Rules of the House of Representatives, your committee states that the inflation impact of the changes results from this bill should be negligible.

VI. CHANGES IN EXISTING LAW MADE BY THE BILL, AS REPORTED

In compliance with clause 3 of rule XIII of the Rules of the House of Representatives, changes in existing law made by the bill, as reported, are shown as follows (existing law proposed to be omitted is enclosed in black brackets, new matter is printed in italics, existing law in which no change is proposed is shown in roman):

INTERNAL REVENUE CODE OF 1954

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Subtitle A—Income Taxes

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CHAPTER 1—NORMAL TAXES AND SURTAXES

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SUBCHAPTER C—CORPORATE DISTRIBUTIONS AND ADJUSTMENTS

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PART III—CORPORATE ORGANIZATIONS AND REORGANIZATIONS

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Subpart B—Effects on Shareholders and Security Holders

SEC. 354. EXCHANGES OF STOCK AND SECURITIES IN CERTAIN REORGANIZATIONS.

(a) GENERAL RULE.—

(1) IN GENERAL.—No gain or loss shall be recognized if stock or securities in a corporation a party to a reorganization are, in pursuance of the plan of reorganization, exchanged solely for stock or securities in such corporation or in another corporation a party to the reorganization.

(2) LIMITATION.—Paragraph (1) shall not apply if—

(A) the principal amount of any such securities received exceeds the principal amount of any such securities surrendered, or

(B) any such securities are received and no such securities are surrendered.

(3) CROSS REFERENCE.—

For treatment of the exchange if any property is received which is not permitted to be received under this subsection (including an excess principal amount of securities received over securities surrendered), see section 356.

(b) EXCEPTION.—

(1) IN GENERAL.—Subsection (a) shall not apply to an exchange in pursuance of a plan of reorganization within the meaning of section 368(a)(1)(D), unless—

(A) the corporation to which the assets are transferred acquires substantially all of the assets of the transferor of such assets; and

(B) the stock, securities, and other properties received by such transferor, as well as the other properties of such transferor, are distributed in pursuance of the plan of reorganization.

(2) CROSS REFERENCE.—

For special rules for certain exchanges in pursuance of plans of reorganization within the meaning of section 368(a)(1)(D), see section 355.

(c) CERTAIN RAILROAD REORGANIZATIONS.—Notwithstanding any other provision of this subchapter, subsection (a)(1) (and so much of section 356 as relates to this section) shall apply with respect to a plan of reorganization (whether or not a reorganization within the meaning of section 368(a)) for a railroad approved by the Interstate Commerce Commission under section 77 of the Bankruptcy Act, or under section 20b of the Interstate Commerce Act, as being in the public interest.

(*d*) *EXCHANGES UNDER THE FINAL SYSTEM PLAN FOR CONRAIL.—No gain or loss shall be recognized if stock or securities in a corporation are, in pursuance of an exchange to which paragraph (1) or (2) of section 374(c) applies, exchanged solely for stock of the Consolidated Rail Corporation, securities of such Corporation, certificates of value of the United States Railway Association, or any combination thereof.*

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SEC. 356. RECEIPT OF ADDITIONAL CONSIDERATIONS.

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(d) SECURITIES AS OTHER PROPERTY.—For purposes of this section—

(1) IN GENERAL.—Except as provided in paragraph (2), the term "other property" includes securities.

(2) EXCEPTIONS.—

(A) SECURITIES WITH RESPECT TO WHICH NONRECOGNITION OF GAIN WOULD BE PERMITTED.—The term "other property" does not include securities to the extent that, under section 354 or 355, such securities would be permitted to be received without the recognition of gain.

(B) GREATER PRINCIPAL AMOUNT IN SECTION 354 EXCHANGE.

—If—

(i) in an exchange described in section 354 (other than subsection (c) *or* (*d*) thereof), securities of a corporation a party to the reorganization are surrendered and securities of any corporation a party to the reorganization are received, and

(ii) the principal amount of such securities received exceeds the principal amount of such securities surrendered,

then, with respect to such securities received, the term "other property" means only the fair market value of such excess. For purposes of this subparagraph and subparagraph (C), if no securities are surrendered, the excess shall be the entire principal amount of the securities received.

(C) GREATER PRINCIPAL AMOUNT IN SECTION 355 TRANSACTION.—If, in an exchange or distribution described in section 355, the principal amount of the securities in the controlled corporation which are received exceeds the principal amount of the securities in the distributing corporation which are surrendered, then, with respect to such securities received, the term "other property" means only the fair market value of such excess.

* * * * * * *

SEC. 358. BASIS TO DISTRIBUTEES.

(a) GENERAL RULE.—In the case of an exchange to which section 351, 354, 355, 356, 361, [or 371(b)] *371(b), or 374* applies—

(1) NONRECOGNITION PROPERTY.—The basis of the property permitted to be received under such section without the recognition of gain or loss shall be the same as that of the property exchanged—

(A) decreased by—

(i) the fair market value of any other property (except money) received by the taxpayer,

(ii) the amount of any money received by the taxpayer, and

(iii) the amount of loss to the taxpayer which was recognized on such exchange, and

(B) increased by—

(i) the amount which was treated as a dividend, and

(ii) the amount of gain to the taxpayer which was recognized on such exchange (not including any portion of such gain which was treated as a dividend).

(2) OTHER PROPERTY.—The basis of any other property (except money) received by the taxpayer shall be its fair market value.

(b) ALLOCATION OF BASIS.—

(1) IN GENERAL.—Under regulations prescribed by the Secretary or his delegate, the basis determined under subsection (a)(1) shall be allocated among the properties permitted to be received without the recognition of gain or loss.

(2) SPECIAL RULE FOR SECTION 355.—In the case of an exchange to which section 355 (or so much of section 356 as relates to section 355) applies, then in making the allocation under paragraph (1) of this subsection, there shall be taken into account not only the property so permitted to be received without the recognition of gain or loss, but also the stock or securities (if any) of the dis-

tributing corporation which are retained, and the allocation of basis shall be made among all such properties.

(3) CERTAIN EXCHANGES INVOLVING CONRAIL.—To the extent provided in regulations prescribed by the Secretary or his delegate, in the case of an exchange to which section 354(d) (or so much of section 356 as relates to section 354(d) or section 374(c) applies, for purposes of allocating basis under paragraph (1), stock of the Consolidated Rail Corporation and the certificate of value of the United States Railway Association which relates to such stock shall, so long as they are held by the same person, be treated as one property.

(c) SECTION 355 TRANSACTIONS WHICH ARE NOT EXCHANGES.—For purposes of this section, a distribution to which section 355 (or so much of section 356 as relates to section 355) applies shall be treated as an exchange, and for such purposes the stock and securities of the distributing corporation which are retained shall be treated as surrendered, and received back, in the exchange.

(d) ASSUMPTION OF LIABILITY.—Where, as part of the consideration to the taxpayer, another party to the exchange assumed a liability of the taxpayer or acquired from the taxpayer property subject to a liability, such assumption or acquisition (in the amount of the liability) shall, for purposes of this section, be treated as money received by the taxpayer on the exchange.

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SUBPART C—EFFECTS ON CORPORATION

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PART IV—INSOLVENCY REORGANIZATIONS

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SEC. 374. GAIN OR LOSS NOT RECOGNIZED IN CERTAIN RAILROAD REORGANIZATIONS.

(a) EXCHANGES BY CORPORATIONS.—

(1) NONRECOGNITION OF GAIN OR LOSS.—No gain or loss shall be recognized if property of a railroad corporation, as defined in section 77(m) of the Bankruptcy Act (49 Stat. 922; 11 U.S.C. 205), is transferred after July 31, 1955, in pursuance of an order of the court having jurisdiction of such corporation—

(A) in a receivership proceeding, or

(B) in a proceeding under section 77 of the Bankruptcy Act,

to another railroad corporation (as defined in section 77(m) of the Bankruptcy Act) organized or made useof to effectuate a plan of reorganization approved by the court in such proceeding, in exchange solely for stock or securities in such other railroad corporation.

(2) GAIN FROM EXCHANGES NOT SOLELY IN KIND.—If an exchange would be within the provisions of paragraph (1) if it were not for the fact that the property received in exchange consists not only of stock or securities permitted by paragraph (1) to be received without the recognition of gain, but also other property or money, then—

(A) if the corporation receiving such other property or money distributes it in pursuance of the plan of reorganization, no gain to the corporation shall be recognized from the exchange, but

(B) if the corporation receiving such other property or money does not distribute it in pursuance of the plan of reorganization, the gain, if any, to the corporation shall be recognized, but in an amount not in excess of the sum of such money and the fair market value of such other property so received, which is not so distributed.

(3) LOSS FROM EXCHANGES NOT SOLELY IN KIND.—If an exchange would be within the provisions of paragraph (1) if it were not for the fact that the property received in exchange consists not only of property permitted by such paragraph to be received without the recognition of gain or loss, but also of other property or money, then no loss from the exchange shall be recognized.

(b) BASES.—If the property of a railroad corporation (as defined in section 77(m) of the Bankruptcy Act) was acquired after July 31, 1955, in pursuance of an order of the court having jurisdiction of such corporation—

(1) in a receivership proceeding, or

(2) in a proceeding under section 77 of the Bankruptcy Act,

and the acquiring corporation is a railroad corporation (as defined in section 77(m) of the Bankruptcy Act) organized or made use of to effectuate a plan of reorganization approved by the court in such proceeding, the basis shall be the same as it would be in the hands of the railroad corporation whose property was so acquired, increased in the amount of gain recognized under subsection (a)(2) to the transferor on such transfer.

(c) EXCHANGES UNDER THE FINAL SYSTEM PLAN FOR CONRAIL.—

(1) IN GENERAL.—No gain or loss shall be recognized if, in order to carry out the final system plan, rail properties of a transferor railroad corporation are transferred to the Consolidated Rail Corporation (or any subsidiary thereof) pursuant to an order of the special court under section 303 or 305(d) of the Regional Rail Reorganization Act of 1973 in exchange solely for stock of the Consolidated Rail Corporation, securities of such Corporation, certificates of value of the United States Railway Association, or any combination thereof.

(2) EXCHANGES NOT SOLELY IN KIND.—If paragraph (1) would apply to an exchange if it were not for the fact that the property received in exchange consists not only of property permitted by paragraph (1) to be received without the recognition of gain or loss, but also of other property or money, then rules similar to the rules set forth in paragraph (2) or (3) of subsection (a) (whichever is appropriate) shall be applied.

(3) BASIS.—The basis of the property transferred to the Consolidated Rail Corporation (or any subsidiary thereof) in an ex-

change to which paragraph (1) or (2) applies shall be determined under rules similar to the rules set forth in subsection (b).

(4) DENIAL OF NET OPERATING LOSS CARRYOVERS TO CONRAIL.—Neither the Consolidated Rail Corporation nor any subsidiary thereof shall succeed to any net operating loss carryover of any transferor railroad corporation.

(5) DEFINITIONS.—For purposes of this subsection—

(A) RAIL PROPERTIES.—The term "rail properties" means rail properties within the meaning of paragraph (12) of section 102 of the Regional Rail Reorganization Act of 1973.

(B) TRANSFEROR RAILROAD CORPORATION.—The term "transferor railroad corporation" means a corporation which, on March 11, 1976, was—

(i) a railroad in reorganization (within the meaning of paragraph (14) of section 102 of the Regional Rail Reorganization Act of 1973) in the region (within the meaning of paragraph (15) of such section 102), or

(ii) a corporation leased, operated, or controlled by such a railroad in reorganization.

(C) FINAL SYSTEM PLAN.—The term "final system plan" means the final system plan (within the meaning of paragraph (6) of section 102 of such Act). Such term includes supplemental transactions under section 305 of such Act.

(D) SUBSIDIARY.—The term "subsidiary" means any corporation 100 percent of whose total combined voting shares are, directly or indirectly, owned or controlled by the Consolidated Rail Corporation.

[(c)](*d*) ASSUMPTION OF LIABILITIES.—In the case of a transaction involving an assumption of a liability or the acquisition of property subject to a liability, the rules provided in section 357 shall apply.

(e) USE OF EXPIRED NET OPERATING LOSS CARRYOVERS TO OFFSET INCOME ARISING FROM CERTAIN RAILROAD REORGANIZATION PROCEEDINGS.—

(1) IN GENERAL.—If—

(A) any corporation receives or accrues any amount pursuant to—

(i) an award in (or settlement of) a proceeding under section 77 of the Bankruptcy Act,

(ii) an award in (or settlement of) a proceeding before the special court to carry out section 303(c), 305 or 306 of the Regional Rail Reorganization Act of 1973,

(iii) an award in (or settlement of) a proceeding in the Court of Claims under section 1491 of title 28 of the United States Code, to the extent such proceeding involves a claim arising under the Regional Rail Reorganization Act of 1973, or

(iv) a redemption of a certificate of value of the United States Railway Association issued to such corporation under section 306 of such Act,

(B) any portion of such amount is includible in the gross income of such corporation for the taxable year in which such portion is received or accrued, and such taxable year begins not more than 5 years after the date of such award, settlement, or redemption, and

(C) the net operating loss of such corporation for any taxable year—

(i) was a net operating loss carryover to, or arose in, the first taxable year of such corporation ending after March 31, 1976 (or, in the case of a proceeding referred to in subparagraph (A)(i) which began after March 31, 1976, ending after the beginning of such proceeding), but

(ii) solely by reason of the lapse of time, is not a net operating loss carryover to the taxable year referred to in subparagraph (B),

then such net operating loss shall be a net operating loss carryover to the taxable year described in subparagraph (B) but only for use (to the extent not theretofore used under this subsection to offset other amounts) to offset the portion referred to in subparagraph (B).

(2) SPECIAL RULE.—For purposes of paragraph (1)(C)(i), a corporation which was a regulated transportation corporation (within the meaning of section 172(j)) for its last taxable year ending on or before March 31, 1976, shall be treated as such a regulated transportation corporation for its first taxable year ending after such date.

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H. R. 12490

Ninety-fourth Congress of the United States of America

AT THE SECOND SESSION

Begun and held at the City of Washington on Monday, the nineteenth day of January, one thousand nine hundred and seventy-six

An Act

To provide tax treatment for exchanges under the final system plan for ConRail.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,

SECTION 1. TAX TREATMENT OF EXCHANGES UNDER THE FINAL SYSTEM PLAN FOR CONRAIL.

(a) IN GENERAL.—Section 374 of the Internal Revenue Code of 1954 (relating to gain or loss not recognized in certain railroad reorganizations) is amended by redesignating subsection (c) as subsection (d) and by inserting after subsection (b) the following new subsection:

"(c) EXCHANGES UNDER THE FINAL SYSTEM PLAN FOR CONRAIL.—

"(1) IN GENERAL.—No gain or loss shall be recognized if, in order to carry out the final system plan, rail properties of a transferor railroad corporation are transferred to the Consolidated Rail Corporation (or any subsidiary thereof) pursuant to an order of the special court under section 303 or 305(d) of the Regional Rail Reorganization Act of 1973 in exchange solely for stock of the Consolidated Rail Corporation, securities of such Corporation, certificates of value of the United States Railway Association, or any combination thereof.

"(2) EXCHANGES NOT SOLELY IN KIND.—If paragraph (1) would apply to an exchange if it were not for the fact that the property received in exchange consists not only of property permitted by paragraph (1) to be received without the recognition of gain or loss, but also of other property or money, then rules similar to the rules set forth in paragraph (2) or (3) of subsection (a) (whichever is appropriate) shall be applied.

"(3) BASIS.—The basis of the property transferred to the Consolidated Rail Corporation (or any subsidiary thereof) in an exchange to which paragraph (1) or (2) applies shall be determined under rules similar to the rules set forth in subsection (b).

"(4) DENIAL OF NET OPERATING LOSS CARRYOVERS TO CONRAIL.—Neither the Consolidated Rail Corporation nor any subsidiary thereof shall succeed to any net operating loss carryover of any transferor railroad corporation.

"(5) DEFINITIONS.—For purposes of this subsection—

"(A) RAIL PROPERTIES.—The term 'rail properties' means rail properties within the meaning of paragraph (12) of section 102 of the Regional Rail Reorganization Act of 1973.

"(B) TRANSFEROR RAILROAD CORPORATION.—The term 'transferor railroad corporation' means a corporation which, on March 11, 1976, was—

"(i) a railroad in reorganization (within the meaning of paragraph (14) of section 102 of the Regional Rail Reorganization Act of 1973) in the region (within the meaning of paragraph (15) of such section 102), or

"(ii) a corporation leased, operated, or controlled by such a railroad in reorganization.

"(C) FINAL SYSTEM PLAN.—The term 'final system plan' means the final system plan (within the meaning of paragraph (6) of section 102 of such Act). Such term includes supplemental transactions under section 305 of such Act.

"(D) SUBSIDIARY.—The term 'subsidiary' means any corporation 100 percent of whose total combined voting shares are, directly or indirectly, owned or controlled by the Consolidated Rail Corporation."

(b) BASIS AMENDMENTS.—

(1) BASIS OF PROPERTY RECEIVED BY TRANSFEROR RAILROAD CORPORATIONS.—Section 358(a) of such Code (relating to basis to distributees) is amended by striking out "or 371(b)" and inserting in lieu thereof "371(b), or 374".

(2) ALLOCATION OF BASIS.—Subsection (b) of section 358 of such Code (relating to allocation of basis) is amended by adding at the end thereof the following new paragraph:

"(3) CERTAIN EXCHANGES INVOLVING CONRAIL.—To the extent provided in regulations prescribed by the Secretary or his delegate, in the case of an exchange to which section 354(d) (or so much of section 356 as relates to section 354(d)) or section 374(c) applies, for purposes of allocating basis under paragraph (1), stock of the Consolidated Rail Corporation and the certificate of value of the United States Railway Association which relates to such stock shall, so long as they are held by the same person, be treated as one property."

(c) EFFECTS ON SHAREHOLDERS AND SECURITY HOLDERS.—Section 354 of such Code (relating to exchanges of stock and securities in certain reorganizations) is amended by adding at the end thereof the following new subsection:

"(d) EXCHANGES UNDER THE FINAL SYSTEM PLAN FOR CONRAIL.—No gain or loss shall be recognized if stock or securities in a corporation are, in pursuance of an exchange to which paragraph (1) or (2) of section 374(c) applies, exchanged solely for stock of the Consolidated Rail Corporation, securities of such Corporation, certificates of value of the United States Railway Association, or any combination thereof."

Clause (i) of section 356(d)(2)(B) of such Code (relating to receipt of additional consideration) is amended by striking out "subsection (c) thereof" and inserting in lieu thereof "subsection (c) or (d) thereof".

(d) USE OF EXPIRED NET OPERATING LOSS CARRYOVERS TO OFFSET INCOME ARISING FROM CERTAIN RAILROAD REORGANIZATION PROCEEDINGS.—Section 374 of such Code (relating to gain or loss not recognized in certain railroad reorganizations) is amended by adding at the end thereof the following new subsection:

"(e) USE OF EXPIRED NET OPERATING LOSS CARRYOVERS TO OFFSET INCOME ARISING FROM CERTAIN RAILROAD REORGANIZATION PROCEEDINGS.—

"(1) IN GENERAL.—If—

"(A) any corporation receives or accrues any amount pursuant to—

"(i) an award in (or settlement of) a proceeding under section 77 of the Bankruptcy Act,

"(ii) an award in (or settlement of) a proceeding before the special court to carry out section 303(c), 305, or 306 of the Regional Rail Reorganization Act of 1973.

"(iii) an award in (or settlement of) a proceeding in the Court of Claims under section 1491 of title 28 of the United States Code, to the extent such proceeding involves a claim arising under the Regional Rail Reorganization Act of 1973, or

"(iv) a redemption of a certificate of value of the United States Railway Association issued to such corporation under section 306 of such Act,

"(B) any portion of such amount is includible in the gross income of such corporation for the taxable year in which such portion is received or accrued, and such taxable year begins not more than 5 years after the date of such award, settlement, or redemption, and

"(C) the net operating loss of such corporation for any taxable year—

"(i) was a net operating loss carryover to, or arose in, the first taxable year of such corporation ending after March 31, 1976 (or, in the case of a proceeding referred to in subparagraph (A) (i) which began after March 31, 1976, ending after the beginning of such proceeding), but

"(ii) solely by reason of the lapse of time, is not a net operating loss carryover to the taxable year referred to in subparagraph (B),

then such net operating loss shall be a net operating loss carryover to the taxable year described in subparagraph (B) but only for use (to the extent not theretofore used under this subsection to offset other amounts) to offset the portion referred to in subparagraph (B).

"(2) SPECIAL RULE.—For purposes of paragraph (1) (C) (i), a corporation which was a regulated transportation corporation (within the meaning of section 172(j)) for its last taxable year ending on or before March 31, 1976, shall be treated as such a regulated transportation corporation for its first taxable year ending after such date.".

SEC. 2. EFFECTIVE DATE.

The amendments made by section 1 shall apply to taxable years ending after March 31, 1976.

Speaker of the House of Representatives.

Vice President of the United States and
President of the Senate.

March 29, 1976

Dear Mr. Director:

The following bills were received at the White House on March 29th:

H.J. Res. 857
H.R. 10624
H.R. 12490

Please let the President have reports and recommendations as to the approval of these bills as soon as possible.

Sincerely,

Robert D. Linder
Chief Executive Clerk

The Honorable James T. Lynn
Director
Office of Management and Budget
Washington, D.C.