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# WASHINGTON NEWSLETTER



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### Reagan Budget FY 1982

President Reagan transmitted his budget revisions for FY 1982 (and some changes in FY 1981 funding) to Congress on March 10. Reductions are proposed for school, college, and public library programs, as shown in the table below. Although some information on Reagan's proposals was provided in his February 18 "Program for Economic Recovery" and additional proposals in the March 10 budget message, both documents are considerably lacking in detail. Information on the budget cuts affecting libraries is provided in this Newsletter as far as is known, but some details must await a future Newsletter. In addition, the budget message indicated that further cuts may be necessary.

	FY 1981 cont. res. thru 6/5/81	FY 1981 Reagan Revision	FY 1982 Reagan Budget
ESEA IV-B School libraries	\$171,000,000*	\$128,250,000*	\$128,250,000*
HEA II-A College libraries	4,988,000	no change	-0-
II-B Library training	667,000	no change	667,000
II-B Research & demo.	500,000	no change	500,000
II-C Research libs.	6,000,000	no change	6,000,000
LSCA I Pub. lib. services	62,500,000	no change	46,875,000
III Interlibrary coop.	12,000,000	no change	12,000,000
NCLIS	691,000	695,000	702,000

\*Advance funded program. Reagan proposes to include ESEA IV-B in a state block grant in FY 1982.

### School Libraries - Cuts and Block Grants

The Reagan Administration has requested a rescission, or a cut in funds already appropriated, of 25 percent in FY 1981 (actually advance funding for FY 1982) for the Elementary and Secondary Education Act title IV-B school library resources and

instructional materials program. For FY 1982 the Administration proposes to consolidate about 45 separate elementary and secondary education programs into two block grants. The funding proposed for each block grant would be only 75 percent of the current total for the combined programs.

The local education block grant would consolidate over 10 existing programs which provide services to economically disadvantaged and handicapped students, functionally illiterate adults, and children in schools undergoing desegregation. The state education block grant would consolidate about 35 existing programs for three purposes: (1) for elementary and secondary school improvement at the local level; (2) for services to disadvantaged, handicapped, neglected, and delinquent children in state institutions; and (3) for improvement in state educational agency administration and management. States would decide how to use their funds for these purposes. The ESEA IV-B school library program would be part of the state block grant.

Since the elementary and secondary block grant proposals first surfaced, some changes have been made. School libraries were originally part of the local block grant according to Office of Management and Budget documents, but were later shifted to the state block grant. At first, block grant programs were to be cut 20 percent; quite recently this was changed to 25 percent. Bilingual education was first in, then out of, the block grant proposals. Apparently no maintenance of effort or matching requirements are proposed.

The block grant proposals would require changes in the authorizing legislation for all of the involved programs. A legislative proposal to accomplish this is being developed and will be submitted to Congress shortly. Such legislative changes may be sought through the congressional budget process and specifically through a process called "reconciliation." Using as a vehicle a bill to reconcile FY 1981 spending and budget ceilings, the budget committees could include instructions to reconcile FY 1982 spending as well. Such a bill, if passed by Congress, would require the authorizing committees to develop block grants and make other changes to meet the spending cut targets. Such an approach would have several advantages to those in Congress who support the budget cuts. It would speed up the process, keep it together as one large package, and avoid votes on the merits of each program.

The education block grants have a similar appeal in Congress. They allow Congress to cut across the board without having to evaluate the individual programs. The pressure for specific funding decisions would be passed along to the states and localities. However, it seems unlikely that block grant legislation would be in place in time for the FY 1982 appropriations process to be based on block grants. In that case, 25 percent cuts may be pushed for the individual programs involved.

#### College Library Program Zero in Budget

The Higher Education Act title II-A college library program would be wiped out in FY 1982 if Congress goes along with the Reagan budget. This program has been budgeted at zero funding in the past, most recently in the Carter FY 1980 budget, and Congress has always restored the funding. The budget-cutting atmosphere this year is different; the zero budget recommendation will be difficult, though not impossible to reverse.

#### LSCA I Cuts Recommended

The Library Services and Construction Act title I, public library services, would be cut 25 percent, from \$62.5 million to \$46.9 million, in the Reagan budget for FY 1982. LSCA III, interlibrary cooperation, which was increased in FY 1981 from \$5 million to \$12 million, would remain at the current level of \$12 million.

## NCLIS

The National Commission on Libraries and Information Science came through better than many independent agencies. NCLIS had an \$18,000 supplemental request pending for FY 1981 for increased pay costs and other cost increases. The supplemental request was cut by \$14,000, leaving \$4,000 to be added to the \$691,000 already appropriated for FY 1981. For FY 1982, the Reagan budget would allow a very small increase to \$702,000.

## Arts and Humanities, NHPRC, Other Cuts

Federal cultural activities were hit particularly hard in the Administration's budget revisions for FY 1982. Funding for the Arts and Humanities Endowments would be cut by 50 percent below the Carter budget request. Libraries would definitely feel the effects of such drastic cuts in National Endowment for the Humanities challenge grants and other activities. The Institute for Museum Services in the Education Department would be zeroed out, as would the grant programs of the National Historical Publications and Records Commission in the National Archives. The NHPRC, currently funded at \$4 million, has funded numerous preservation projects in libraries through its Records Program begun in 1974. Its current authorization expires on September 30 of this year. Other cuts affecting libraries are elimination of CETA public service jobs, certain National Science Foundation cuts, and major cuts in postal subsidies.

## Library of Congress

Cutting the Library of Congress budget is "like attacking the book of knowledge," said Sen. Mack Mattingly (R-GA), chair of the Senate Legislative Appropriations Subcommittee at March 11 hearings on LC's budget. Sen. Mattingly asked Librarian of Congress Daniel Boorstin if he would be willing to hold FY 1982 spending to FY 1981 levels. Boorstin said the cut in real dollars involved would necessitate cuts in LC services. Neither House nor Senate subcommittees have made any decisions on LC funding. On the House side, House Legislative Appropriations Subcommittee Chair Vic Fazio (D-CA) provided a rare opportunity for public witnesses to appear at a March 2 hearing. After Ella Yates Edwards, Atlanta Public Library Director, testified for ALA in support of the LC budget, Fazio concluded that what the subcommittee really needed was more anecdotal information from libraries across the country about the value of Library of Congress services.

## ACTION NEEDED on Budget Cuts

While many members of Congress are unhappy with parts of the Administration's program, criticism of the whole package has been muted. There have been some notable exceptions. Rep. Bill Ford (D-MI) said in a February 25 Congressional Record (p. E727) statement: "Critical to all of our education programs and the general population as well are our libraries....To shortchange our libraries is to shortchange our children's future and our citizens' enrichment." Other congressional friends of libraries have asked for data on how the proposals would affect libraries.

The budget cuts would require action by the budget and appropriations committees, and the block grant proposals would involve the authorizing committees as well. This means that almost every state will have one or more members making committee decisions impacting on federal library programs. The mail most members are receiving so far is a carefully orchestrated campaign in support of the budget cuts, a campaign that began even before the specific cuts were announced. What members need now, especially the brand new members, is information on the accomplishments of the programs and specific data or anecdotal information on the impact of the proposed cuts.

For maximum impact, draft a separate letter for each federal library or related program about which you have direct knowledge. Adapt each letter to several uses. First, send them to your own Representative and Senators. Second, send them to the chairs of the authorizing subcommittees -- in the Senate, Sen. Stafford on the education subcommittee; in the House, Rep. Perkins for school libraries; Rep. Simon for academic and public libraries. The authorizing subcommittees include the members who know the programs best; they can influence funding, but they need the specifics only you can provide. Third, and most important, send your letters to the chairs of the relevant appropriations subcommittees. For most library and education programs, these are the Labor-HHS-Ed Appropriations Subcommittees; for LC and GPO, the Legislative Appropriations Subcommittees, and for NHPRC and postal subsidies, the Treasury appropriations subcommittees. Fourth, if you have a member on one of the Budget Committees, take note of this in your letter; it's an increasingly powerful committee.

Appropriations committee lists were attached to the February 10 Newsletter; budget and authorizing committee lists are attached to this issue. If your own members are not on the appropriate subcommittees, ask them to write and convey your message to the appropriations subcommittee chair, and to keep you informed of developments. Please send us blind copies of your letters and of any substantive replies. The specific information you provide your members helps us to do our job better.

Postal Rates

Increased postal rates will become effective March 22 as the result of a March 10 decision by the Postal Service Board of Governors. The Board voted under protest to accept the recommendations of the Postal Rate Commission for an 18¢ first class stamp as well as increases in other postal rates. Contending USPS needs additional revenue, the Board of Governors had wanted even higher rates to avoid an immediate application for larger increases.

Fourth class library postal rates are in the midst of a phased rate schedule of increases. For the first pound, the rates increase from 19¢ at present to 38¢ in 1987. Effective March 22 the rate schedule will range from 21¢ to 50¢ for an average increase in the library rate of 32 percent. This is a larger increase than the Postal Service originally requested. The Postal Rate Commission recommended the rates shown below, claiming that the attributable costs had increased due to a significant increase in the average distance and weight of library rate mail over the last few years. If Congress agrees to a major reduction in Postal Service subsidies as recommended by President Reagan, the full 50¢ rate may be implemented sooner than 1987.

Permanent Phased Rate Increases in Cents  
(Each step begins on July 6 of the indicated year)

	<u>Step and Year</u>							
	<u>9</u> <u>'80</u>	<u>10</u> <u>'81</u>	<u>11</u> <u>'82</u>	<u>12</u> <u>'83</u>	<u>13</u> <u>'84</u>	<u>14</u> <u>'85</u>	<u>15</u> <u>'86</u>	<u>16</u> <u>'87</u>
<u>Library Rate</u>								
First pound	21	25	29	33	37	42	46	50
Each addit. lb. thru 7 lbs.	8	9	10	12	13	14	16	17
Each addit. lb.	5	6	6	7	8	8	9	9.5

Taxation - Thor Power Tool Bill. Sen. Moynihan's bill, S. 578, to modify the Thor Power Tool tax ruling, was introduced February 26 (see attachment). Also attached is the ALA Council resolution on the Thor issue. The Association of American Publishers is studying the effect of the bill on its members and has not yet taken a position.

Emergency Building Temperature Restrictions were rescinded by President Reagan February 17 (February 19 Federal Register, p. 12941).

U. S. HOUSE OF REPRESENTATIVES

Committee on Education and Labor

97th Congress, 1st Session

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William D. Ford, Michigan  
Phillip Burton, California  
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William (Bill) Clay, Missouri  
Mario Biaggi, New York  
Ike Andrews, North Carolina  
Paul Simon, Illinois  
George Miller, California  
Austin J. Murphy, Pennsylvania  
Ted Weiss, New York  
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Thomas E. Petri, Wisconsin  
Millicent Fenwick, New Jersey  
Marge Roukema, New Jersey  
Eugene Johnston, North Carolina  
Lawrence J. DeMardis, Connecticut  
Larry Craig, Idaho  
Wendell Bailey, Missouri

American Library Association  
Washington Office  
March 1981

(See over for Subcommittees on  
Elementary, Secondary and  
Vocational Education, and  
Postsecondary Education.)

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Ike Andrews, North Carolina  
George Miller, California  
Baltasar Corrada, Puerto Rico  
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Pat Williams, Montana  
Augustus F. Hawkins, California  
Mario Biaggi, New York  
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Harold Washington, Illinois  
- To be appointed -

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Lawrence J. DeNardis, Connecticut  
Wendall Bailey, Missouri  
- To be appointed -

\* Ex Officio

March 1981

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97th Congress, 1st Session

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97th Congress, 1st Session

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U. S. SENATE

Committee on Budget

97th Congress, 1st Session

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Daniel Patrick Moynihan, New York  
J. James Exon, Nebraska





United States  
of America

# Congressional Record

PROCEEDINGS AND DEBATES OF THE 97<sup>th</sup> CONGRESS, FIRST SESSION

Vol. 127

WASHINGTON, THURSDAY, FEBRUARY 26, 1981

No. 31

## Senate

\* \* \* \* \*

\* On February 26, Sen. Daniel Moynihan (D-NY) introduced S. 578, \*  
 \* a bill which would modify the Thor Power Tool tax ruling. The \*  
 \* intent of the bill is to develop a method for publishers and \*  
 \* other companies to show evidence that their inventories have \*  
 \* a low market value for tax purposes without destroying the in- \*  
 \* ventory itself. \*  
 \* \* \* \* \*

By Mr. MOYNIHAN:

S. 578. A bill to amend the Internal Revenue Code to change certain accounting rules related to inventory; to the Committee on Finance.

MODIFICATION OF THOR POWER TOOL TAX RULING

Mr. MOYNIHAN. Mr. President, I am introducing legislation today that would modify the Thor Power Tool tax ruling.

The bill has three provisions. The first would let any company that can demonstrate that a portion of its inventory will eventually be sold below cost write down that portion to its net realizable value.

The second provision would drop the so-called conformity requirement for LIFO accounting.

And the third would give companies that switch from FIFO to LIFO accounting 10 years over which to spread out any sudden profits that result from the change.

The heart of the bill is section 1. It, more than any other part, is aimed at the real Thor controversy. The controversy arises because of a decision by the Supreme Court in the case *Thor Power Tool Co. v. Commissioner*, 439 U.S. 522 (1979).

The Thor Power Tool Co. was—and still is—a FIFO taxpayer. FIFO is an accounting method; the acronym stands for first-in, first-out. And under that accounting method, a company must figure out at the end of each tax year how much its inventory is worth. The law says that the inventory must be listed at its cost—or at its market value, but only if the market value is lower. The law also says that each item of inventory must be valued separately.

In 1963, the Thor Co. had in its inventory 44,000 spare parts for hand-held power tools and rubber products. The company had recently come under new management. The new managers decided that many of these spare parts would never be sold; hence, in the managers' view, the parts had little, if any, market value. Consequently, the company used the market value, rather than the cost of the parts, when it reported how much its inventory was worth at the end of 1964 to the IRS.

This process of suddenly choosing a low-market value, when up to now a company has listed its inventory at cost, is known as "writing down" one's inventory. In 1964, it yielded the Thor Power Tool Co. a tax deduction of \$744,030.

However, there was one problem with what the company did. And that is there was no evidence that the spare parts were worth what the company said they were.

Company officials merely projected demand for the parts using their experience with sales in 1964. Parts that the company expected to sell in 1965 were said to be worth something, and were listed on the company's books at cost. But parts that the company expected to sell in 1966 were said to have a market value of from 50 to 75 percent below cost. And the company claimed that the parts it might sell in 1967 or in later years were worthless. These were listed at zero, or thereabouts—their assumed market value.

The company's claim was absurd. The market values it selected had no demonstrable basis in fact. Therefore, the Internal Revenue Service disallowed the company's deduction. And when the case went to the Supreme Court the Justices agreed with the IRS. Their decision was unanimous.

What the Court said is that a taxpayer must be able to prove that his inventory has a low market value, before he may write down the inventory. And the IRS may insist on "a high evidentiary standard."

Tax regulations, in effect at the time, said that a company may prove that its inventory has a low market value in one of two ways. The company may sell the inventory at less than cost within 30 days after the close of the tax year. Or it may cut its prices below cost, in which case the IRS will accept the company's word that the inventory is not worth more than the company is charging for it.

The Court did not say that there are no other ways that a company may prove that its inventory has a low market value. What it said was there must be proof. And it is reasonable for the IRS to demand the kind of evidence that it wanted of taxpayers.

My bill suggests a third method of proof.

Consider the following case: A publisher has 1,000 copies of a 1960 best seller in his warehouse. The books are still being held out for sale at the list price, although there are few purchasers. Intuitively, one knows that each book is not worth the list price; some of the books will never be sold and are not worth even the cost of printing them. But how does one prove it?

That is the "Thor problem." The answer is that a taxpayer should be able to look to his experience. If the publisher's records show that, on average, 10 percent of any books that have not been sold within a year after they were printed will eventually be remaindered, then each year the publisher should be able to write down 10 percent of his 1-year-old books to their remainder value.

(over)

By the same token, if the records show that, on average, 40 percent of 2-year-old books are eventually remaindered, then 40 percent of 2-year-old books would be written down each year to their remainder value.

I hasten to add that the books need not actually be remaindered in the strictest sense of the word. It is enough that they will be sold eventually at less than cost. And when that is the case, they may be written down to what the publisher's experience tells him he will receive for them.

I want also to stress that while I used a book publisher in my example, this new approach would be available to all companies in all industries. The only restrictions are that a company would have to segregate its inventory items by age. And it would have to point to its most recent 5 years of experience with inventories.

The bill would take effect retroactively and apply to the 1979 tax years. A company would be able to redo its taxes for 1979 and 1980 using this new method, if it wishes; 1979 was the year in which the IRS began aggressively to enforce the holding in the Supreme Court decision. Companies would not have to seek the IRS' permission in order to file amended returns.

That is section 1 of the bill.

The other two sections deal with LIFO, or last-in, first-out, accounting. There are two ways to resolve the "Thor problem"; one is to address the issue directly, as I have already done. The other is to persuade more companies to switch to LIFO; companies on LIFO do not have a Thor problem since under LIFO, all inventories must be valued at cost. There is no need to supply evidence of market value.

LIFO is more favorable to taxpayers since it makes them appear less profitable. Nevertheless, many companies do not use it because of the so-called conformity requirement—a rule that says a company that uses LIFO for its taxes must also use LIFO for its financial statements to shareholders.

My bill would drop the conformity requirement. The Internal Revenue Service recommended this last month and, in fact, is in the process of removing the requirement from its regulations. But Congress will have to act, too, because the rule appears in section 472 of the Tax Code.

Another reason companies do not use LIFO is that when a company switches to it from FIFO, adjustments must be made to the company's inventory and this often causes the company's income to increase suddenly in the year of the change. My bill would give a company making a switch 10 years over which to spread out the adjustments.

I intend to let a taxpayer make a 10-year spread without having to seek the advance consent of the IRS. Under present law, a taxpayer must get the IRS's permission for a spread within the first 180 days of the tax year. That rule would not apply here.

The LIFO provisions of the bill would take effect prospectively in tax years beginning after the date of enactment.

That is the plan.

In concluding, let me note that the bill has been carefully written over a period of several months. Almost everyone who has told me he has an interest in the subject has been consulted and given a chance to participate in the drafting.

In addition, Treasury and Joint Tax Committee experts have been kept advised of the bill's progress at every step of the way.

I am proposing that we resolve the Thor problem in a manner that is consistent with the Supreme Court's decision. A company should be able to prove that its inventory has a low market value before it claims a loss on its taxes. The only question is what kind of evidence should the company be required to provide.

I ask unanimous consent, Mr. President, that the text of the bill be printed in the Record.

There being no objection, the bill was ordered to be printed in the Record, as follows:

S. 578

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

**SECTION 1. EXCESS INVENTORY ITEMS MAY BE WRITTEN DOWN TO SCRAP VALUE.**—Section 471 of the Internal Revenue Code of 1954 (relating to the general rule for inventories) is amended by adding at the end thereof the following new sentences: "A taxpayer may value his excess inventory at its net realizable value. For purposes of this section, the term 'excess inventory' means that portion of the taxpayer's inventory which the taxpayer reasonably expects will be disposed of at less than full realization of its cost. Such portion shall be determined with respect to each group of articles by age by referring to the taxpayer's most recent 5-year experience with inventories."

**SEC. 2. REPEAL OF REQUIREMENT THAT THE LIFO METHOD USED FOR TAX PURPOSES CONFORM TO THE ACCOUNTING METHOD USED FOR FINANCIAL PURPOSES.**—Section 472 of such Code (relating to last-in, first-out inventories) is amended by striking out subsections (c) and (e) and by redesignating subsection (d) as subsection (c).

**SEC. 3. TEN-YEAR SPREAD PERMITTED FOR INCREASES IN INVENTORY VALUE REQUIRED FOR ADOPTION OF LIFO METHOD.**—Subsection (b) of section 472 of such Code (relating to last-in, first-out inventories) is amended by adding at the end thereof the following new sentence: "For purposes of section 481, any increase in the valuation of inventory required by paragraph (2) shall be treated as an adjustment attributable to a change in a method of accounting initiated by the taxpayer."

**SEC. 4. EFFECTIVE DATES.**—

(a) The amendment made by section 1 of this Act shall apply to taxable years ending on or after December 25, 1979.

(b) The amendments made by sections 2 and 3 of this Act shall apply to taxable years beginning after the date of enactment.

(Pages S1620-S1621)

THOR RESOLUTION

WHEREAS, the Supreme Court's decision in Thor Power Tool Co. v. Commissioner (439 U.S. 522 (1979)) has the effect of forcing publishers either to maintain backlist inventories at full initial value or to cause unconscionable waste by destroying the books so that they can deduct a tax loss and untie assets to invest in new titles; and

WHEREAS, the Thor decision will, in the long term, have an impact upon the business environment such that publishers will tend to publish only those titles likely to sell very quickly, before the end of the taxable year, and forego publishing titles likely to sell more slowly; and

WHEREAS, many worthwhile titles and vital resources are nonetheless relatively slow-selling works and are therefore apt to be very hard to acquire or even unavailable after the full impact of the Thor decision is felt; and

WHEREAS, libraries order large parts of their collections from backlists especially during times of budget reductions when they are forced to maintain periodical subscriptions and postpone the purchase of worthy book titles until the following year; and

WHEREAS, the free flow of ideas in the marketplace is the very cornerstone of our country's constitutional foundation; intellectual exchange between solution-seekers is made possible by specialized literature and is the foundation of advancement in every area; and the value of making classical, educational, scientific, and children's literature available to America's citizens is impossible to measure in strictly economic terms;

NOW THEREFORE BE IT RESOLVED that the American Library Association express its grave concern over the impact of the Thor decision on the dissemination of knowledge throughout society and urges Congress to take action to alleviate this negative impact.

Adopted by the Council of the  
American Library Association  
Washington, D.C., February 4, 1981