19 T.C. 879 (1953)

Mexican mining production taxes, based on the extraction of ore, are not considered income taxes or taxes in lieu of income taxes for the purpose of claiming foreign tax credits under U.S. tax law.

Summary

American Metal Company sought a foreign tax credit for production taxes paid by its Mexican subsidiary, Minera. The Tax Court held that these production taxes, imposed on the extraction of metals and metallic compounds under Mexican Mining Tax Laws, did not qualify as income taxes or taxes in lieu of income taxes under U.S. Internal Revenue Code Section 131. The court reasoned that the taxes were based on the value of extracted minerals, not on profits, and were imposed regardless of profitability. The court also rejected the Commissioner's argument regarding the exchange rate to be used for calculating the credit, finding that the subsidiary's books were maintained in U.S. dollar equivalents, negating any exchange rate issue.

Facts

American Metal Company (petitioner) sought a tax credit for taxes paid by its Mexican subsidiary, Compania Minera de Penoles, S. A. (Minera). Minera extracted ores of nonferrous metals in Mexico. Mexican Mining Tax Laws imposed production taxes on the extraction of these metals. Minera properly deducted these production taxes but was not allowed to deduct for depletion in computing its taxable net income under Mexican Income Tax Laws. The Republic of Mexico owns all minerals in place within the Republic, and all mining of those minerals is through concessions from the Government. These taxes were calculated based on the value of the metals extracted, with rates varying based on the metal and its stage of refinement.

Procedural History

American Metal Company filed a consolidated income tax return for 1947, claiming a credit for taxes paid by Minera to the Republic of Mexico. The Commissioner of Internal Revenue partially disallowed the claimed credit, determining that the taxes paid under the Mexican Mining Tax Laws were not income taxes or taxes in lieu of income taxes within the meaning of Section 131 of the Internal Revenue Code. The Commissioner also argued for a different exchange rate for calculating any allowable credit. The Tax Court reviewed the Commissioner's determination.

Issue(s)

1. Whether the mining production taxes imposed by the Republic of Mexico constitute income taxes or taxes in lieu of income taxes within the meaning of Section 131(a)(1) or (h) of the Internal Revenue Code, entitling the petitioner to a foreign tax credit.
2. Whether the credit for foreign taxes paid should be computed by converting

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foreign taxes at the exchange rate existing at the time of dividend declaration, rather than at the time the taxes were paid.

Holding

1. No, because the Mexican mining production taxes were based on the value of extracted minerals, not on net income or profits, and were imposed regardless of whether the mining operation was profitable.
2. No, because the foreign subsidiary kept its books in U.S. dollar equivalents, thus eliminating any foreign exchange calculation problem.

Court's Reasoning

The court considered the petitioner's argument that mining proceeds are traditionally viewed as income and that the Mexican production taxes possessed characteristics of income taxation. However, the court emphasized that the key question was whether the Mexican production taxes qualified as income taxes or taxes in lieu of income taxes under Section 131(a)(1) or (h). The court acknowledged that the Mexican government considered the profitability of mining operations when setting production tax rates, as evidenced by preambles to tax decrees. However, the court found that the taxes were ultimately based on the value of the minerals extracted, not on profits. The court highlighted several factors: The production taxes were in effect before Mexican income taxes were established; The production taxes paid were substantially higher than income taxes; Deductions were allowed for production taxes when calculating income taxes; The Republic of Mexico owned the minerals; The taxes were payable upon extraction regardless of subsequent sale or profit; and Minera paid production taxes even in years when it had no income tax liability. Regarding the exchange rate issue, the court distinguished *Bon Ami Co., 39 B.T.A. 825* because Minera kept its books in U.S. dollar equivalents, eliminating the need for currency conversion at the time of dividend declaration. The court stated, "Here the foreign subsidiary kept its books so that tax payments, earnings, and dividends were currently and exclusively reflected in the equivalent of United States currency as opposed to foreign currency, and the 'proportionate part' of the foreign tax represented in the dividend can only be determined by reference to the subsidiary's books."

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