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90TH CONGRESS, 2d Session | SENATE | REPORT No. 1014

TAX ADJUSTMENT ACT OF 1968

MARCH 15, 1968.—Ordered to be printed.

Mr. LONG of Louisiana, from the Committee on Finance, submitted the following

REPORT

[To accompany H.R. 15414]

The Committee on Finance, to which was referred the bill (H.R. 15414) to continue the existing excise tax rates on communication services and on automobiles, and to apply more generally the provisions relating to payments of estimated tax by corporations, having considered the same, reports favorably thereon with amendments and recommends that the bill as amended do pass.

I. SUMMARY

The House bill continues until December 31, 1969, existing excise taxes imposed with respect to manufacturers' sales of passenger automobiles and with respect to certain telephone services. Thereafter it provides for the gradual reduction and eventual elimination of these taxes. The committee accepted these provisions without change. The House bill also provides for the acceleration of income tax payments by corporations to place these payments of tax on a comparable basis to that applying in the case of individual taxpapers, including sole proprietors. The committee made two modifications in this latter provision. It also added a provision dealing with the tax treatment of interest on industrial development bonds. Further it added two public welfare amendments to the bill dealing with provisions which were passed by the Senate last year but not accepted in the conference on the Social Security Amendments Act, and one amendment related to the medical assistance (title XIX) program, All of these amendments added by your committee are summariaed below.

Finance Committee amendments.—Your committee modified the acceleration provisions as passed by the House to provide that the speedup of corporate income tax payments generally is not to apply with respect to the tax payable on the first $25,000 of taxable income

(generally the level where the surtax exemption applies). In addition, the bill as passed by the House provides for "quickie refunds" in the case of overpayments of estimated tax. The House bill provides that such quickie refunds are not to be available unless the overpayment exceeds 105 percent of the then expected tax liability and also amounts to more than $200. Your committee has raised this limitation to 110 percent and $500.

The committee added an amendment to the bill providing that interest on industrial development bonds, which has been excluded from gross income as interest on a State or local government bond in accordance with the regulations previously in effect and the principles set forth in a series of revenue rulings, is to continue to be exempt from income tax unless otherwise provided by some future The law. Internal Revenue Service is directed to issue ruling letters with respect to these bonds in conformity with the statement indicated above.

Present law sets a limitation on Federal financial participation in the program for aid to families with dependent children, related to the proportion of the child population that could be aided because of the absence from the home of a parent. This limitation is deleted by the committee bill.

The committee bill removes certain provisions contained in present law which affect eligibility of children on AFDC when their father is unemployed. Specifically, the requirement that the father have six calendar quarters of work or have been entitled to unemployment compensation would be removed. In addition, the committee bill would permit a State at its option to make payments for a month in which the father received unemployment compensation. Under present law, receipt of any unemployment compensation would bar assistance for the month.

Under present law, effective January 1, 1968, States with medicaid programs which have not purchased part B medicare coverage (supplementary medical insurance) for those older citizens eligible for medicaid benefits, no longer receive Federal matching payments toward the cost of medical services which would have been reimbursable under part B of medicare had the State, in fact, purchased such coverage. The committee amendment postpones the effective date of the cutoff of Federal funds in such cases to January 1, 1970.

Revenue effect.—While this bill does not increase tax liabilities above those now payable, it is estimated the changes made by this bill as amended by your committee will increase tax collections by about $1 billion in fiscal year 1968 and by about $2.9 billion in fiscal year 1969. The larger revenues in part are attributable to continuing existing excise tax rates and in part to speeding up the collection of existing corporation tax liabilities. The public welfare provisions adopted by your committee will involve payments of $15 million in fiscal year 1968 and $134 million in the fiscal year 1969. The House bill as amended by your committee, therefore, will reduce the deficit by about $1 billion in fiscal year 1968 and by about $2.8 billion in fiscal year 1969.

Reasons for action.—In view of the budget deficits in excess of $20 billion forecast in both 1968 and 1969, without taking into account proposed tax increases, it appeared inappropriate to allow a reduction in existing excise tax rates. Moreover, it appeared to be an appropriate time to take further action to place corporation income tax payments

on a more current basis. At the same time, however, provision is made for quick refunds for corporations after the end of the year in those cases where their estimated tax payments significantly exceed their tax liabilities.

Other House bill provisions.—To simplify compliance for corporations, both the House and your committee's bill repeal the present requirement that corporations file a declaration of estimated tax. This does not affect existing payment procedures.

Both versions of the bill also establish that a deposit of tax is to be considered to be paid on time if it is mailed to a depositary at least by the second day before the due date.

II. GENERAL STATEMENT

The President's budget message estimates receipts and expenditures under the new unified budget, before taking into account the President's proposals with respect to tax legislation in fiscal years 1968 and 1969, at the following levels: [1]

BUDGET TOTALS FOR FISCAL YEARS 1968 AND 1969

[In millions of dollars]

	1968	1969
Receipts excluding effect of tax proposals	152,824	164,951
Expenditures and net lending	175,635	186,062
Deficit	22,811	21,111

These data indicate deficits of $22.8 billion in 1968 and $21.1 billion in 1969.

With prospective deficits of such magnitudes, your committee agrees with the House that it is inappropriate to permit reductions in the excise taxes to occur in 1968 or 1969 as scheduled by existing law. It also agrees that this is an appropriate time to remove disparity in the treatment of individuals and corporations under the current tax payment system. These actions also will undoubtedly aid from the standpoint of our present international financial position.

In view of the fact that the excise tax reductions, in the absence of this bill, would occur on April 1, and the fact that the speed-up of corporation income tax payments must occur before April 15 to be fully effective this year, your committee concluded that it is essential to act now on these recommendations.

[1] The administrative budget estimates are as follows:

[In millions of dollars]

	1968	1969
Receipts excluding effect of tax proposals	115,569	122,669
Expenditures	137,182	147,363
Deficit	21,613	24,694

Excise tax extensions

Under present law the 7-percent manufacturers excise tax on passenger automobiles [2] is scheduled to drop from 7 to 2 percent on April 1, 1968, and then on January 1, 1969, to drop to 1 percent. The 1-percent rate under present law is to be a permanent tax. Your committee has concluded, as did the House, that the present 7-percent rate of tax should be continued until 1970.

Your committee is also in accord with the House that reductions in the manufacturers excise tax on passenger automobiles should be enacted in a series of gradual steps to prevent possible dislocations in the industry. It agrees that the anticipation by consumers of a substantial reduction in the excise tax-rate might delay purchases of new automobiles for a period before the rate reduction actually took place. Therefore, the House bill and your committee's bill provide for the reduction in the excise tax on passenger automobiles in a series of steps which is to begin on January 1, 1970, and conclude on January 1, 1973, with the repeal of the tax. As indicated previously, under existing law the tax would have been retained at a permanent level of 1 percent.

Under present law the excise tax on local telephone service, toll service, and teletypewriter exchange service is scheduled to be reduced from 10 percent to 1 percent as of April 1, 1968, and on January 1, 1969, the 1 percent tax is to be repealed. Your committee has concluded, as did the House, that the present 10-percent rate of tax should be continued until 1970.

Your committee's bill and the House bill provide a schedule of rate reductions for the tax on telephone service comparable to that provided in the case of passenger automobiles; that is, the 10-percent rate on these various types of telephone service is reduced to 5 percent as of January 1, 1970, and is reduced by 2 percentage points a year thereafter until 1973, when the final 1 percent tax is removed.

Current payment of corporation income tax liabilities

In view of the budgetary outlook, it appeared appropriate now to take further action to place corporations under substantially the same obligations with respect to the current payment of income tax liabilities as those placed upon individuals and unincorporated businesses.

This objective has long been sought by Congress. Action was taken in each of the revenue acts of 1950, 1954, 1964, and 1966 to place the payment of corporate tax liabilities on more nearly the same basis as that of individuals and unincorporated businesses. The development has been gradual because of a desire to ease possible transitional problems for the corporations involved, but commitment to the objective has not varied.

For these reasons, the House bill and your committee's bill raise the percentage of estimated tax liability necessary to be paid currently by corporations from 70 to 80 percent—the percentage applicable to individuals. This change is made fully effective for 1968 tax liabilities.

The bill as passed by the House also reduced the exemption from the corporate current payment provisions from $100,000 to $40.

[2] Passenger automobile chassis and bodies and other chassis and bodies for trailers and semitrailers (other than housetrailers) suitable for use in connection with passenger automobiles.

The bill as modified by your committee also substantially reduces this exemption for corporations below $100,000. However, your committee believes that it is desirable to maintain a favored position for corporate small business because of its difficulties in obtaining adequate financing. For that reason it has reduced the exemption from the corporate current payment provisions from $100,000 to the level at which the surtax exemption applies, generally, $25,000 of taxable income, or $5,500 of tax. The first $25,000 of taxable income is the amount which Congress previously decided should be exempt from the 26 percent surtax rate applicable to higher incomes. Therefore, deferring tax payments on income below this level is consistent with the existing policy of preferential treatment for these small incomes.

The reduction of the exemption from current payment provisions under your committee's action, as under the House action, is made effective gradually over a 5-year period beginning with 1968 tax liabilities. This is accomplished by requiring the inclusion in 1968 (in addition to tax liabilities in excess of $100,000) of 20 percent of the tax liabilities between $100,000 and $5,500, by increasing this to 40 percent for 1969 liabilities, 60 percent for 1970 liabilities, 80 percent for 1971 liabilities, and 100 percent for 1972 liabilities and the liabilities of later years.

The reduction of the $100,000 exemption for corporate estimated tax payments is phased in because it is believed that to do otherwise would impose a hardship on many corporations not now required to make quarterly payments of estimated tax and also on those corporations which will be required to make substantial increases in the amount of estimated tax they pay.

Another provision of the bill will simplify the estimated tax payment requirements of corporations by repealing the existing requirement that corporations file declarations of their estimated tax. Under the terms of the bill, corporations will not have to complete a form indicating the manner in which they determine their estimated tax payments, but will merely have to make those payments on or before the quarterly due dates.

Your committee also has agreed to a further change designed to ease the impact of the current payment provisions on corporations. It recognizes that applying the new system might in some cases result in substantial overpayments by corporate taxpayers if the final results of their operations fall below their expectations in the forepart of the year, since the last estimated tax payment by corporations is required to be made before the end of their tax year. These overpayments could result from such circumstances as the burning or flooding out of a business, a strike, or a sharp downturn in expected sales. For some of these firms the overpayment of estimated tax may create a cash shortage at the very time the need is the greatest. These corporations cannot obtain a refund of estimated tax under current law until they file their tax returns. However, many corporations have difficulty filing their returns within 2½ months after the close of their tax year and must ask for a 3-or 6-month extension before filing their returns. This delays still further the time when any overpayment of estimated tax can be refunded to them.

For these reasons your committee has endorsed the provision of the House bill which permits a corporation to obtain a quick refund of overpayment of estimated tax by filing an application during the

period between the end of its taxable year and the time it files its tax return for that year (or the due date of the return if earlier). When these quick refund applications are filed, the Internal Revenue Service is to make payment within 45 days. The refund in this case is only available with respect to estimated tax payments in excess of the tax liability reasonably estimated at that time, and not the 80 percent of estimated tax liability on which the earlier payments may be made.

To prevent the use of this quick refund provision where the amounts are small, the bill passed by the House provided that the refund is to be made only where the estimated payments have equaled or exceeded 105 percent of tax liability and the excess payments equal or exceed $200. Your committee concluded that the limits provided in the House bill should be raised to 110 percent of tax liability and a minimum of $500 to insure that the quick refund provision will only be used when the amounts are significant.

Timely mailing treated as timely deposit

At the present time taxpayers who are required to deposit payments of estimated, withheld income, employment, or excise taxes in a designated bank for tax collection purposes must bear the responsibility for insuring that the payment reaches the depositary on or before the specified due date. It has been pointed out that this places the responsibility for delays which occur in the delivery of mail on the taxpayer. Taxpayers, particularly those whose headquarters are located at some distance from the depositary banks they may wish to use, must mail deposits well in advance of the due date to avoid the risk of an additional tax if there is a delay in the mails. Under legislation passed in 1954, certain documents and claims are held to be filed on time if they were timely mailed. In 1966, this treatment was extended to returns and payments of tax. Your committee agrees with the House that similar treatment should be provided with respect to deposits of tax and endorses the provision of the House bill under which a deposit received at the depositary bank after the due date is to be considered received on or before the due date if it is mailed on or before the second day prior to the due date.

Interest on industrial development bonds

The Treasury Department on March 6 announced (in TIR 972) that it was reconsidering its position on the tax-exempt status, under section 103 of the Internal Revenue Code, of interest paid on industrial development bonds. These are bonds issued by, or on behalf of, a municipality or other political subdivision where the bonds are used to finance the purchase and/or construction of a facility to be leased to a private corporation. The bonds in these cases are usually amortized wholly from the rental payments received from the private corporation.

The Treasury Department stated that proposed regulations concerning industrial development bonds would be published which would provide that these bonds would not be considered obligations of a State or local government within the meaning of section 103(a)(1) of the Internal Revenue Code. It was announced that these regulations would apply to bonds sold after March 15, 1968, and the Treasury announced that effective March 15, 1968, it is withdrawing its rulings holding industrial revenue bonds to be exempt. In applying this effective date, it was stated that bonds would be considered sold on

the date when a buyer or underwriter enters into a binding contract with the issuer to purchase the bonds at a fixed price.

The Committee on Finance is concerned that the Treasury Department in taking this action is, in effect, legislating on this subject. It does not believe that a change should be made in the status of the interest on these bonds without specific legislative action on the part of the Congress.

For the reasons indicated above, your committee has added a section (sec. 5) to the bill providing that interest on industrial revenue bonds is to be excluded from gross income under section 103 of the Internal Revenue Code in accordance with the regulations prescribed by the Treasury Department as in effect on March 13, 1968, and in accordance with the principles set forth in three revenue rulings; namely, revenue ruling 54-106, revenue ruling 57-187, and revenue ruling 63-20. In addition, the section provides that the Internal Revenue Service is authorized and directed to issue ruling letters with respect to industrial development bonds in conformity with the position stated above.

The revenue rulings referred to in general provide as follows:

Revenue Ruling 54-106 (C.B. 1954-1, 28) provides that bonds issued by a municipality for the construction of municipally owned industrial plants for lease to private enterprises constitute obligations of a political subdivision within the meaning of what is now section 103(a)(1) of the Internal Revenue Code and that interest on these bonds is exempt from Federal income tax notwithstanding the purpose for which they were issued or the fact that the promise to pay is limited to the revenue to be derived from leasing the property. It is also stated that it is not necessary for this purpose that the obligation be a general one pledging the general credit of the municipality or the use of its taxing power.

Revenue Ruling 57-187 (C.B. 1957-1, 65) holds that interest on bonds issued by an industrial development board formed under a State statute is exempt from Federal income taxes under section 103(a)(1) of the Internal Revenue Code. In this case the bonds were payable only out of the revenue produced by the property in question, the industrial development boards (and the interest on the bonds) were exempt from all State taxes, and upon the dissolution of any such board the title to the property owned by it was to become the property of the municipality in which the board was located.

Revenue Ruling 63-20 (C.B. 1963-1, 24) states that obligations issued by a nonprofit corporation formed for the purpose of stimulating industrial development would be considered issued "on behalf of" a political subdivision for purposes of section 1.103.1 of the income tax regulations where the following five requirements were met:

(1) The corporation must engage in activities which are essentially public in nature;

(2) The corporation must be one which is not organized for profit (except to the extent of retiring indebtedness);

(3) The corporate income must not inure to any private person;

(4) The State or political subdivision must have a beneficial interest in the corporation while the indebtedness remains outstanding and must obtain full legal title to the property upon retirement of the indebtedness; and

(5) The corporation must have been approved by the State or political subdivision and the State or political subdivision must also have approved of the obligations issued by the corporation.

Repeal of limitation on Federal participation in Aid to Families with Dependent Children

The Social Security Amendments of 1967 set a limitation on Federal financial participation in the AFDC program related to the proportion of the child population under age 18 aided because of the absence of a parent from the home. Under the limitation, this proportion is calculated based on the child population in each State on January 1, 1968, and the average monthly number of children dependent because of the absence of a parent during the first calendar quarter of 1968. The limitation becomes effective July 1, 1968.

The House version of the 1967 amendments contained this limitation (though with different dates); the Senate version did not. In the conference the Department of Health, Education, and Welfare presented estimates that the limitation would not reduce Federal participation in assistance payments because of the effect of the work incentive provisions of the amendments, in reducing the number of people on the rolls.

The Department has subsequently revised these estimates, and the President's budget (p. 462) states that assistance payments to about 475,000 AFDC recipients will not receive Federal matching totaling $125 million in fiscal year 1969. It is unlikely that the conference committee would have acted as it did if the members had been aware of the effects now predicted by the Department of Health, Education, and Welfare.

At the same time, there have been other developments which will have a major impact on the AFDC limitation as it applies to some States. Court decisions in a number of States, including Connecticut, Delaware, the District of Columbia, Wisconsin, and Pennsylvania, have forced those States to eliminate eligibility requirements based on length of residence. A court decision in Alabama, and litigation in process in Louisiana, would not permit those States to declare families ineligible for assistance because of the presence of a man in the house who is not married to the mother of the family.

Some 40 States now have requirements based on length of residence; 18 States have man-in-the-house rules. The Department of Health, Education, and Welfare estimates that in the United States as a whole, a range of from 200,000 to 400,000 AFDC recipients might be added to the rolls if all States eliminated the man-in-the-house rule; another 100,000 to 200,000 AFDC recipients could be added to the rolls with the elimination of duration-of-residence related requirements.

If court decisions prohibit these requirements, the unforeseen new recipients will place an additional burden on the States affected. For the most part, there will be no Federal financial participation on their behalf under present law since they will exceed the number of recipients in the first calendar quarter of 1968, the period used in calculating the proportion of the child population affected by the Federal limitation.

For these reasons, the committee again recommends that the limitation on Federal participation be deleted.

Assistance to families with unemployed fathers

Federal participation in assistance to children dependent because of their father's unemployment began in 1961. But the Social Security Amendments of 1967 for the first time authorized a Federal definition of "unemployment," and tied the program to the new work-incentive program established in the same bill.

Two provisions of last year's House bill were deleted in the Senate but restored in conference. The first of these provisions requires that in order to qualify for assistance on the basis of unemployment, a father must meet certain tests of prior attachment to the labor force. While the committee does not wish to encourage irresponsible marriages, it believes that no one needs the advantages of the work and training programs more than the man who has a wife and children but has no significant history of employment. The committee bill returns to last year's Senate bill by not including work attachment requirements.

The second provision of present law prohibits the payment of assistance (with Federal participation) to a family when the father receives any amount of unemployment compensation during the same month. Since the unemployment compensation may be for only a small part of the month, a family's income could be far below the State's standard of need and still the family would be ineligible for federally aided assistance.

The committee bill returns to last year's Senate bill under which the choice as to whether unemployment compensation payments can be supplemented is left to the States.

Medical assistance (medicaid)

Public Law 90-248 extended the period during which States could elect to cover under part B of medicare those aged cash assistance recipients eligible for medicaid. States now have until January 1, 1970, to make such election rather than the January 1, 1968, date which obtained under prior law. Aged persons not receiving cash assistance but eligible for medicaid were also authorized to be included in a State's "buy-in" group as well as those persons who first go on medicaid rolls after 1967.

Public Law 90-248 further provided that there would be no Federal matching toward the States' share of buying-in for those medicaid eligibles who were not also cash assistance recipients.

Additionally, the new law prohibits, effective January 1, 1968, the payment of Federal matching funds under title XIX toward the cost of services which would have been covered under the supplementary medical insurance program had a State purchased such coverage for its medicaid eligibles. For example, a medicaid eligible in a State with a title XIX program is operated on in a hospital. The surgeon's charge would have been a covered service under part B of medicare had the State enrolled this recipient in part B. However, inasmuch as the State did not so elect, the surgeon's fee is payable wholly from State funds—no Federal matching is available toward that expense as would ordinarily be payable toward a title XIX medical vendor payment.

The basic purposes of the above provisions are to encourage employment of a uniform mechanism—part B of medicare—in the governmental programs designed to cover medical costs of older people and

to assure the broadest possible participation of older persons in the supplementary medical insurance plan.

The general revenues of the Federal Government bear a substantial portion of the total part B premium cost for both welfare and nonwelfare participants. Effective April 1968, this amounts to a Federal share of $4 monthly of the total $8 monthly premium cost for each participant in the program. In view of this general revenue contribution, the Congress did not find it appropriate to authorize additional Federal payment toward the $4 per person cost incurred by a State in buying-in for medically needy persons. However, the Congress did find it appropriate to continue Federal matching payments under title XIX toward the $4 monthly cost incurred with respect to eligible individuals who are also cash assistance recipients.

The committee amendment would not alter any of the objectives of the buy-in. It would simply postpone to January 1, 1970, the date when Federal matching payments would no longer be payable for medical services which could have been covered under part B of Medicare had a State elected to buy-in for its title XIX eligibles.

There are several sound reasons for this postponement:

1. States which did not buy in did not have a reasonable opportunity to do so following enactment of a law which, in effect, makes the buy-in virtually mandatory. Public Law 90-248 was not signed by the President until January 2, 1968, and yet the cutoff of Federal matching became effective January 1, 1968.

2. Postponement until January 1, 1970, coordinates the operation of the buy-in restriction with the effective date of two other related requirements. Under present law, States are required to have title XIX programs by that date or forfeit Federal matching for all of their medical assistance programs. Further, as has been noted, under Public Law 90-248, States have until January 1, 1970, to elect to buy in part B coverage.

3. Delay of the cutoff of matching for medical services which could have been covered under the buy-in will also avoid penalizing those States which elected to participate in title XIX prior to January 1, 1970. In contrast, States which delay entry into title XIX and which do not purchase part B coverage can continue to receive Federal matching for vendor payments made in behalf of aged recipients under titles I and XVI—despite the fact that those same services could have been covered under part B of medicare. The committee amendment thus treats the 50 States equally and equitably.

4. Delay of the Federal matching prohibition until January 1, 1970, will also provide a reasonable opportunity for those States which have not bought-in to seek necessary approvals and appropriations from their legislatures. Orderly budgeting and administration will be enhanced by the additional time provided under the committee amendment.

The need to allow an adequate opportunity for consideration of the buy-in by State legislatures is further underlined because legislatures will undoubtedly want to consider this question in the context of the limitations on eligibility and other modifications to title XIX included in Public Law 90-248. The matter of the buy-in is not necessarily separable from these other title XIX considerations.

The need for prompt action

The measures proposed in the House bill and your committee's bill should be enacted promptly. The existing excise tax rates on

passenger automobiles and telephone service will fall sharply at the end of this month unless legislative action is taken to prevent the reductions. Furthermore, buyers may begin to postpone purchases of autos in expectation of the scheduled reductions unless Congressional action is completed soon. The longer the delay in the action to extend the excise tax rates, the greater is the risk that the volume of deferred purchases will become substantial. Prompt action also is necessary on the provisions regarding the current payment of corporate tax liabilities. These provisions will provide a substantial increase in tax receipts in fiscal year 1968 only if they are enacted in time for corporations to put them into effect before the April 15 and June 15 estimated tax payment due dates for corporations that use the calendar year as their tax year.

Revenue effects

As indicated in the following table, this bill is expected to increase tax receipts in fiscal year 1968 by $986 million and in fiscal year 1969 by $2,940 million.

The $680 million increase in receipts from the provisions to accelerate corporate tax payments which is estimated for fiscal year 1968 under the bill as amended by your committee reflects the combined impact of the increase in the percentage of tax required to be paid currently to avoid an addition to tax and a reduction in the current exemption level. Since the reduction in the exemption level is to be phased over a 5-year period, receipts in each of the fiscal years 1969 through 1972 will also be increased by $280 million a year. The impact of the increase of 70 to 80 percent in the amount of tax liability which must be paid currently to avoid additions to tax will increase receipts by $400 million only in fiscal year 1968. The increase in revenue from the excise tax extensions is small in fiscal year 1968 since the extensions are to apply only for 3 months in this fiscal year.

It is estimated that the public welfare amendments approved by your committee will increase Federal payments by $15 million in the fiscal year 1968 and $134 million in the fiscal year 1969.

The bill as amended by your committee will, therefore, reduce the deficit in fiscal year 1968 by $971 million and will decrease the deficit in fiscal year 1969 by $2,806 million.

The bill as approved by the House would have increased fiscal year 1968 receipts by $1.106 billion and fiscal year 1969 receipts by $3.060 billion.

ESTIMATES OF THE EFFECT ON BUDGET OF H.R. 15414 AS AMENDED BY THE FINANCE COMMITTEE

[In millions of dollars]

	Fiscal year 1968	Fiscal year 1969
a. Increase in receipts:		
Excise taxes—Extension of present rates:		
Passenger automobiles	190	1,500
Telephone service	116	1,160
Total, excise extensions	306	2,660
Proposals for corporate estimated tax payments	680	280
Total revenue provisions	986	2,940
b. Increase in expenditures: Public welfare provisions	15	134
c. Net reduction in deficit	971	2,806

III. GENERAL EXPLANATION OF EXCISE CHANGES AND ACCELERATION PROVISIONS, ETC.

1. The excise tax on passenger automobiles (sec. 2(a) of the bill and sec. 4061 of the code)

Present law.—As a result of amendments in the Excise Tax Reduction Act of 1965 and the Tax Adjustment Act of 1966, the excise tax on passenger automobiles (imposed on the manufacturer's price) is 7 percent. Before the passage of the Excise Tax Reduction Act, the rate was 10 percent. Under the amendments made by those acts, the rate now is scheduled to fall from 7 to 2 percent on April 1 of the current year, and to a permanent rate of 1 percent on January 1, 1969.

Explanation of provisions.—Both the committee and the House substitute a new timetable for the scheduled reductions in the excise tax on passenger automobiles. In addition, it provides for the repeal of the tax effective January 1, 1973.

The new timetable postpones the scheduled reductions in the excise tax on passenger automobiles for a temporary period. At the same time it tempers the effect that the scheduled reductions would have on consumer purchases—as previously described—by providing for a gradual reduction in rate. Finally, the new timetable provides for the repeal of the tax at the end of the postponement period.

Under the bill, the present 7-percent excise tax on passenger automobiles is to continue until January 1, 1970. On that date the rate is to fall to 5 percent. Further annual reductions of 2 percentage points each then are to occur on January 1, 1971, and January 1, 1972, as the rate falls from 5 to 3 percent and from 3 to 1 percent, respectively. On January 1, 1973, the tax rate is to fall to zero. As in the past, refunds are to be paid to dealers with respect to automobiles held in inventory on the date of any rate reduction. The bill provides the following schedule of excise tax rates applicable in the case of passenger automobiles:

	Percent
Before Jan. 1, 1970	7
During 1970	5
During 1971	3
During 1972	1
Thereafter	0

2. The excise tax on communications (sec. 2(b) of the bill and sec. 4251 of the code)

Present law.—Present law imposes a 10-percent excise tax on amounts paid for local and toll telephone and teletypewriter exchange service. Scheduled reductions under the Excise Tax Reduction Act of 1965 and the Tax Adjustment Act of 1966 call for the tax to fall to 1 percent on April 1, 1968, and for its repeal on January 1, 1969.

Explanation of provisions.—Both the committee and the House bills postpone the scheduled repeal of the excise tax on telephone services and teletypewriter service. It also provides for a graduated reduction in the rate before the rate falls to zero on January 1, 1973.

In taking the action described above, your committee continues to recognize, as it stated at the time of the Excise Tax Reduction Act of 1965, "that the tax on local and toll telephone service and teletypewriter exchange service is undesirable as a permanent feature of our excise tax system." The committee also recognizes, however,

that "while elimination of the tax is desirable * * *, since the tax is an important source of revenue for the Federal Government, reduction should be staged over a period of years."

Under the bill, the scheduled reduction and repeal of the excise tax on telephone services and teletypewriter service generally parallels the scheduled reduction and repeal of the excise tax on passenger automobiles. Thus, the present 10-percent rate is to continue until January 1, 1970, when it is to fall to 5 percent—the same rate then scheduled for the automobile excise tax. Annual reductions of 2 percentage points each then are to occur on January 1, 1971, and January 1, 1972, so that the tax rate is to be 3 percent in 1971 and 1 percent in 1972. On January 1, 1973, the tax is to cease. As under existing law, in applying these new rates, bills for services before November 1 of a calendar year are to bear the tax of that year even if the bill for the services is not rendered before the close of the year. As a result the schedule of rates under the House bill and your committee's bill in the case of these telephone services is as follows:

	Percent
Before Jan. 1, 1970	10
During 1970	5
During 1971	3
During 1972	1
Thereafter	0

3. Repeal of requirement for filing declaration of estimated tax (sec. 3(a) of the bill and secs. 6016 and 6074 of the code)

Present law.—Present law requires a corporation with an estimated income tax (after credits) in excess of $100,000 to file a declaration of estimated tax in the current year. A corporation subject to the filing requirement also must make payments of estimated tax in the current year. Payments are deposited with authorized banks by using deposit forms provided by the Treasury.

With the shift in 1967 to the collection of estimated tax of corporations through the use of banks as depositaries, the filing of declarations of estimated tax by corporate taxpayers became unnecessary. The declarations formerly were used as a means of identifying and billing the taxpayer but since shifting to the depositary system, the Service supplies the taxpayer with deposit forms for each quarterly payment, which contain the taxpayer's identifying number. The deposit forms provide both the Service and the corporation (through the retention of a stub) with a record of payments and also serve as reminder to the corporation as to when payments are due.

Explanation of provisions.—Your committee's bill and the House bill repeal the requirement that a corporation file a declaration of estimated tax. This action is taken because there is no justification for requiring a corporation to continue filing a form which, under present practices, serves no useful purpose. Elimination of the requirement for filing this form will simplify present practices both for the corporate taxpayer and for the Internal Revenue Service. The repeal of the filing requirement, however, does not change the requirements regarding the payments of estimated tax by a corporation.

4. Payment of estimated tax by corporation on tax liability below $100,000 (sec. 3(b) of the bill and sec. 6154 of the code)

Present law.—Before the amendments made by the Revenue Act of 1950, a corporation had the option of paying its entire tax on the

15th day of the third month following the close of its taxable year or of paying one-fourth of its tax on that date and the balance in equal quarterly installments on the 15th day of the third, sixth, and ninth months following the month of the first installment. The amendments made by the 1950 Revenue Act provided for an acceleration of the installment payments of tax liability over a 5-year transitional period. As a result, at the end of the transitional period, a corporation had to pay either all or one-half of its tax on the 15th day of the third month following the close of its taxable year; if it elected to pay only one-half of its liability at that time, it had to pay the balance 3 months later.

Provisions added by the Internal Revenue Code of 1954 now require a corporation with an estimated income tax (after credits) in excess of $100,000 to file a declaration and make payments of estimated tax in the current year. A corporation whose estimated income tax (after credits) does not exceed $100,000 is not subject to the requirements; one whose estimated income tax (after credits) does exceed $100,000 is subject to the requirements only to the extent of the excess.

As a result of amendments made by the Revenue Act of 1964 and the Tax Adjustment Act of 1966, estimated tax payments for calendar year corporations now are payable in four equal installments on April 15, June 15, September 15, and December 15. In total the payments must equal the amount of the tax shown on the return less $100,000. However, no underpayment, for purposes of imposing an addition to tax, results if the corporation pays 70 percent of this amount.

A corporation required to make estimated tax payments may avoid an addition to tax for an underpayment, as previously described, if it comes within one of three exceptions. The first exception allows a corporation to pay an amount equal to the prior year's tax reported on its return in lieu of its current year's estimate. A second exception determines the amount payable by reference to the results of the corporation's operations in the prior year but at the current year's income tax rates. The third exception determines the amount payable by reference to the corporation's income in the months preceding the payment; the corporation annualizes this income and must pay 70 percent of the tax determined on this annualized amount. The $100,000 corporate exemption noted above also applies in the case of each of these exceptions.

Explanation of provisions.—The bill as reported by your committee provides for a reduction in the present $100,000 corporate exemption from the estimated taxpayments requirement. As in the past, your committee again is providing for a 5-year transitional period in this regard. At the end of the transitional period, the corporate exemption from the estimated taxpayments requirement is to be the same as the exemption which the corporation enjoys under existing law from the corporate surtax; that is, the corporation (unless it is a member of an affiliated group, which is to divide one exemption among its members) is not to be required to make estimated taxpayments with respect to its first $25,000 of estimated taxable income (or its first $5,500 of estimated tax liability). In addition, under an amendment made by your committee, only if a corporation's estimated income tax exceeds $5,500 by at least $40 is it to be required to make estimated

taxpayments. The House bill would have reduced the present $100,000 exemption to $40 over a 5-year transitional period.

Under the bill the substitution of the new surtax exemption for the existing $100,000 corporate exemption is to be phased in over a 5-year period with taxable years beginning in 1968. This phasein, provided to allow a corporation time to arrange its financial affairs to meet the new estimated tax payments requirement, is accomplished by providing a "transitional exemption" during the 5-year period. This transitional exemption is a percentage of the difference between the first $100,000 of the corporation's extimated income tax (after credits) and $5,500 (or a smaller amount in the case of multiple surtax exemptions). This percentage, called the exclusion percentage, falls from 80 percent in 1968 to 60 percent in 1969, to 40 percent in 1970, to 20 percent in 1971, and is eliminated in 1972. An example will illustrate how the new surtax exemption and the transitional exemption are to apply.

Assume that in 1968 a corporation has a tax liability of $100,000. The corporation in this case does not have to make estimated taxpayments with respect to the first $5,500 of its estimated tax liability. In addition, it does not have to make estimated tax-payments with respect to its transitional exemption. In 1968, this exemption is 80 percent of the difference between the corporation's $100,000 of estimated tax liability and its $5,500 exemption. Thus, in this case the corporation's transitional exemption is $75,600 (or 80 percent of $94,500). The corporation, therefore, must make estimated tax-payments of $18,900 ($100,000 minus $75,600 minus $5,500). In 1969, when the transitional exemption is to fall to 60 percent, the corporation's estimated tax-payments, if its income remains the same, are to equal $37,800 since in that year the corporation's transitional exemption is to be $56,700 which together with its $5,500 exemption accounts for the aggregate exemption of $62,200.

As a result of the above described manner of phasing out the existing $100,000 exemption and substituting the new surtax exemption in its stead, a corporation whose estimated income tax (after credits) exceeds $5,500 is to pay an increasing amount in estimated tax each year until the end of the transition period. As noted above, the phasein gives the corporation time to arrange its financing to meet the new requirements in an orderly fashion. At the same time the phasein requires all corporations whose estimated tax exceeds $5,500 to begin immediately to pay some of their tax currently.

5. *Increase from 70 to 80 percent in liability corporation must pay by estimated tax to avoid addition to tax (sec. 3(c) of the bill and sec. 6655 of the code)*

Present law.—Present law imposes an addition to tax if a corporation fails to pay its estimated tax. This addition is at the rate of 6 percent per annum on the amount of the underpayment. An underpayment is the difference between an actual payment and 70 percent of the payment that the corporation would have owed if its estimated tax had been accurately determined; that is, if its estimated tax equaled its actual tax for the year as subsequently shown on its income tax return (determined for this purpose with regard to the $100,000 exemption from the estimated tax payments referred to

previously). The 70-percent test applies with respect to each installment payment.

As previously indicated, a corporation may avoid the addition to tax for an underpayment if it comes within one of three exceptions. The first of these exceptions allows a corporation to pay an amount equal to the prior year's tax reported on its return in lieu of its current year's estimate. The second exception determines the amount payable by reference to the results of the corporation's operations in the prior year but applies the current year's income tax rates. The third exception determines the amount payable by reference to the corporation's income in the months preceding the payment.

The last exception noted above, which determines the amount of a payment necessary to avoid the addition to tax by reference to the corporation's income for the months preceding the payment, also has a 70-percent test. Under this exception the corporation may annualize its income for the months preceding an installment payment and determine the tax for the year (above the $100,000 exemption) on this annualized amount. The corporation then may avoid the addition to tax by making an estimated payment equal to 70 percent of the payment it would owe if its estimated tax were the tax on this annualized amount.

As a result of amendments made by the Tax Adjustment Act of 1966, the two 70-percent tests noted above are 80-percent tests in the case of an individual businessman. Before that act raised the percentage test for the individual, the corporate and individual taxpayer had been treated alike in this regard.

Explanation of provisions.—Your committee's bill and the House bill raise the two 70-percent tests noted above for a corporate taxpayer to 80 percent. This provision is effective for taxable years beginning in 1968. Thus, under the bill, to avoid an addition to tax, a corporation's estimated tax payments in 1968 must equal 80 percent of the tax liability it shows on its income tax return (determined with regard to the transitional rules explained above for reducing the $100,000 exemption to $5,500). Alternatively, if it uses the annualization rule to avoid additions to tax, the payments must equal 80 percent of its tax as determined by annualizing the corporate income for the appropriate months preceding the payment. In the latter case, also, the determination is made with regard to the transitional rules for reducing the $100,000 exemption.

An example will illustrate the interaction of the new 80-percent test and the transitional exemption during the period of the phasein of the $5,500 exemption:

Assume a corporation, as in the example above, has an estimated tax liability of $100,000 in 1968. As the result of its surtax exemption and its transitional exemption, the corporation is required to make estimated taxpayments of $18,900 in that year (as explained above). Thus, it may avoid an addition to tax if it pays only $15,120 (or 80 percent of $18,900). In 1969, when the corporation's transitional exemption is to fall to 60 percent, the corporation's required estimated taxpayments, if its estimated taxable income remains the same, are to equal $37,800. It may avoid an addition to tax in that year if it pays only $30,240 (or 80 percent of $37,800).

In raising the 70-percent tests to 80 percent, the bill restores the balance between the corporate taxpayer and the individual which

existed before the 1966 amendments. Moreover, in raising the percentage tests (as in phasing out the existing exemption) the bill also brings corporations closer to a full-pay-as-you-go basis.

6. Quick refund of overpayment of estimated income tax by corporation (sec. 3(d) of the bill and sec. 6425 of the code)

Present law.—As previously indicated, existing law requires a corporation with an estimated income tax in excess of $100,000 to file a declaration and make payments of its estimated tax in the current year. If the total of these payments exceeds the tax shown on the return, the corporation may claim the overpayment as a refund. It may not claim this refund, however, until it files its income tax return for the year. Unlike the individual, who makes his last installment payment after the close of the year, the corporation must complete its payments during the year, and therefore cannot reduce these payments to reflect yearend losses.

Present law generally requires a corporation on a calendar year to file an income tax return by March 15. The corporation may claim automatic 3- or 6-month extensions of time for filing, however, merely by filing requests (but it is required to make payments of proper estimates of tax on the March 15 due date). The result is that a calendar year corporation often does not file its income tax return until sometime in September, more than 8 months after the close of its taxable year. Even then, the Internal Revenue Service may wait another 45 days before refunding any overpayment of tax without paying interest on the overpayment. Thus, a total of 10 months may elapse between the close of the year and the time a corporation receives a refund of an overpayment of tax.

Explanation of provisions.—Your committee's bill and the House bill allow a corporation to apply for a quick refund or, more technically, an adjustment of overpayment of estimated tax, immediately after the close of its taxable year. Under the House bill a corporation could do so when its current revised estimate of its income tax liability shows that its estimated taxpayments exceed its revised estimate by at least 5 percent of the revised estimate and that the excess amounts to at least $200. Under your committee's bill, the corporation can do so only if its estimated taxpayments exceed its revised estimate by at least 10 percent and the excess amounts to at least $500.

The provision for quick repayment which the bill contains is effective for taxable years beginning in 1968.

This provision for quick repayment is somewhat similar to the provision now available for "quickie" refunds resulting from net operating loss carrybacks or carrybacks of investment tax credits. This quick adjustment of an overpayment will make less burdensome the overpayments corporations now may be more likely to make because of the larger portion of their expected tax liability which they will have to pay on a current basis as a result of reducing the $100,000 exemption and raising the 70-percent test to 80 percent.

Under the bill, the adjustment application must be filed before the date a corporation first files its income tax return (whether or not it subsequently amends the return) or the date for filing its returns (determined without regard to any extension), whichever is earlier. The filing date for corporations is the 15th day of the third month following the close of their taxable year, or March 15 for calendar year taxpayers.

In order to discourage frivolous adjustment applications and applications from corporations which merely want to borrow funds from the Government, the bill imposes (in a new subsec. (g) of sec. 6655 of the code) an addition to tax at an annual rate of 6 percent on a corporation if it requests and receives an adjustment which subsequently is determined to be excessive. This 6-percent amount, as in the case of an underpayment of estimated tax, is not deductible for income tax purposes. The addition to tax is computed from the time of the excessive adjustment to the due date for the tax return (March 15 in the case of a calendar year taxpayer). (The normal interest for late payment at 6 percent applies thereafter.) The computation of this addition to tax is made independently of, and does not affect the computation of, any addition to tax which a corporation may otherwise owe for an underpayment of an installment of estimated tax.

On its application for adjustment, the corporation is to set forth the estimated tax which it paid during the year, the amount of its revised estimated tax liability, the amount of the adjustment which it requests, and such other information as the Secretary of the Treasury by regulations may prescribe. Before making an adjustment, the Internal Revenue Service may make a very limited examination of an adjustment application. The examination is not to prejudice any right of the Service to claim later that the adjustment was improper. The Service may disallow an application when it finds that the application contains material omissions or errors which the Service deems that it cannot correct within the 45-day period allowed it in making an adjustment. If the Service disallows the adjustment, it is expected that the Service will inform the taxpayer of this action. If it allows the adjustment, the Service may first credit the amount of a claimed adjustment against an outstanding tax liability of the corporation before making payment of the balance to the corporation. In this case it is understood that the Service will notify the corporation of the credit.

An adjustment is generally to be treated as a reduction of prior estimated taxpayments as of the date of the adjustment. However, for purposes of the provision relating to additions to tax for failure to pay estimated income tax (sec. 6655), the adjustment is to be ignored—that is, treated as if not made—in determining whether there has been any underpayment of estimated income tax and, if there is an underpayment, the period during which the underpayment existed.

7. *Timely mailing of tax deposits (sec. 4 of the bill and sec. 7502(e) of the code)*

Present law.—The Internal Revenue Service is placing increasing reliance of the deposit method for the collection of taxes and now is collecting about $80 billion a year in this manner. Presently most withheld income taxes, estimated corporate income taxes, and excise taxes are collected in this manner. About 90 percent of the banks in the country are designated as depositaries for this purpose. This allows most taxpayers to hand deliver deposits on the last day prescribed for deposit and avoid any addition to tax that would otherwise result.

Some taxpayers, however, find it more convenient to mail tax deposits than to hand deliver them. This may occur, for example, because a corporation with centralized financial management desires to make deposits with banks in the various communities in which its

plants are located. Under the regulations, these deposits which are mailed are not considered as made until received by depositaries. The responsibility for timely mail delivery thus falls on the taxpayers. This differs from the general rule which treats payments as made when mailed.

Explanation of provisions.—Your committee's bill and the House bill provide that where a taxpayer mails his tax deposit 2 or more days before the prescribed due date, the mailing is to be considered a timely deposit even though the deposit is received after the due date (but only if it is actually received). Thus, under the bill, the Government, and not the taxpayer, bears the responsibility for timely mail delivery.

Under both versions of the bill, the mailing of a deposit 2 or more days before the due date for payment is to be considered as payment only where the taxpayer can establish that he timely mailed the deposit. In the case of a deposit sent by registered mail, the date of registration is to be deemed the date of mailing. The taxpayer, of course, could also establish the date of mailing by other competent evidence.

IV. CHANGES IN EXISTING LAW

In the opinion of the committee, it is necessary, in order to expedite the business of the Senate, to dispense with the requirements of subsection 4 of rule XXIX of the Standing Rules of the Senate (relating to the showing of changes in existing law made by the bill, as reported).