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PERMANENT EXTENSION OF DEDUCTION FOR HEALTH INSURANCE COSTS OF SELF-EMPLOYED INDIVIDUALS

MARCH 20 (legislative day, MARCH 16), 1995.—Ordered to be printed

Mr. PACKWOOD, from the Committee on Finance, submitted the following

REPORT

together with

ADDITIONAL VIEWS

[To accompany H.R. 831]

[Including cost estimate of the Congressional Budget Office]

The Committee on Finance, to which was referred the bill (H.R. 831) to amend the Internal Revenue Code of 1986 to permanently extend the deduction for the health insurance costs of self-employed individuals, to repeal the provision permitting nonrecognition of gain on sales and exchanges effectuating policies of the Federal Communications Commission, and for other purposes, having considered the same, reports favorably thereon with an amendment in the nature of a substitute and recommends that the bill as amended do pass.

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The amendment to the bill is as follows:

SECTION 1. PERMANENT EXTENSION AND INCREASE OF DEDUCTION FOR HEALTH INSURANCE COSTS OF SELF-EMPLOYED INDIVIDUALS.

(a) PERMANENT EXTENSION.—Subsection (l) of section 162 of the Internal Revenue Code of 1986 (relating to special rules for health insurance costs of self-employed individuals) is amended by striking paragraph (6).

(b) INCREASE IN DEDUCTION.—Paragraph (1) of section 162(l) of the Internal Revenue Code of 1986 is amended by striking “25 percent” and inserting “30 percent”.

(c) EFFECTIVE DATES.—

(1) EXTENSION.—The amendment made by subsection (a) shall apply to taxable years beginning after December 31, 1993.

(2) INCREASE.—The amendment made by subsection (b) shall apply to taxable years beginning after December 31, 1994.

SEC. 2. REPEAL OF NONRECOGNITION ON FCC CERTIFIED SALES AND EXCHANGES.

(a) IN GENERAL.—Subchapter O of chapter 1 of the Internal Revenue Code of 1986 is amended by striking part V (relating to changes to effectuate FCC policy).

(b) CONFORMING AMENDMENTS.—Sections 1245(b)(5) and 1250(d)(5) of the Internal Revenue Code of 1986 are each amended—

(1) by striking “section 1071 (relating to gain from sale or exchange to effectuate polices of FCC) or”, and

(2) by striking “1071 AND” in the heading thereof.

(c) CLERICAL AMENDMENT.—The table of parts for such subchapter O is amended by striking the item relating to part V.

(d) EFFECTIVE DATE.—

(1) IN GENERAL.—The amendments made by this section shall apply to—

(A) sales and exchanges on or after January 17, 1995, and

(B) sales and exchanges before such date if the FCC tax certificate with respect to such sale or exchange is issued on or after such date.

(2) BINDING CONTRACTS.—

(A) IN GENERAL.—The amendments made by this section shall not apply to any sale or exchange pursuant to a written contract which was binding on January 16, 1995, and at all times

thereafter before the sale or exchange, if the FCC tax certificate with respect to such sale or exchange was applied for, or issued, on or before such date.

(B) SALES CONTINGENT ON ISSUANCE OF CERTIFICATE.—A contract shall be treated as not binding for purposes of subparagraph (A) if the sale or exchange pursuant to such contract, or the material terms of such contract, were contingent, at any time on January 16, 1995, on the issuance of an FCC tax certificate. The preceding sentence shall not apply if the FCC tax certificate for such sale or exchange is issued on or before January 16, 1995.

(3) FCC TAX CERTIFICATE.—For purposes of this subsection, the term "FCC tax certificate" means any certificate of the Federal Communications Commission for the effectuation of section 1071 of the Internal Revenue Code of 1986 (as in effect on the day before the date of the enactment of this Act).

SEC. 3. SPECIAL RULES RELATING TO INVOLUNTARY CONVERSIONS.

(a) REPLACEMENT PROPERTY ACQUIRED BY CORPORATIONS FROM RELATED PERSONS.—

(1) IN GENERAL.—Section 1033 of the Internal Revenue Code of 1986 (relating to involuntary conversions) is amended by redesignating subsection (i) as subsection (j) and by inserting after subsection (h) the following new subsection:

"(i) NONRECOGNITION NOT TO APPLY IF CORPORATION ACQUIRES REPLACEMENT PROPERTY FROM RELATED PERSON.—

"(1) IN GENERAL.—In the case of a C corporation, subsection (a) shall not apply if the replacement property or stock is acquired from a related person. The preceding sentence shall not apply to the extent that the related person acquired the replacement property or stock from an unrelated person during the period described in subsection (a)(2)(B).

"(2) RELATED PERSON.—For purposes of this subsection, a person is related to another person if the person bears a relationship to the other person described in section 267(b) or 707(b)(1)."

(2) EFFECTIVE DATE.—The amendment made by paragraph (1) shall apply to involuntary conversions occurring on or after February 6, 1995.

(b) APPLICATION OF SECTION 1033 TO CERTAIN SALES REQUIRED FOR MICROWAVE RELOCATION.—

(1) IN GENERAL.—Section 1033 of the Internal Revenue Code of 1986 (relating to involuntary conversions), as amended by subsection (a), is amended by redesignating subsection (j) as subsection (k) and by inserting after subsection (i) the following new subsection:

"(j) SALES OR EXCHANGES TO IMPLEMENT MICROWAVE RELOCATION POLICY.—

"(1) IN GENERAL.—For purposes of this subtitle, if a taxpayer elects the application of this subsection to a qualified sale or exchange, such sale or exchange shall be treated as an involuntary conversion to which this section applies.

"(2) QUALIFIED SALE OR EXCHANGE.—For purposes of paragraph (1), the term 'qualified sale or exchange' means a sale or exchange before January 1, 2000, which is certified by the Federal Communications Commission as having been made by a taxpayer in connection with the relocation of the taxpayer from the 1850–1990MHz spectrum by reason of the Federal Communications Commission's reallocation of that spectrum for use for personal communications services. The Commission shall transmit copies of certifications under this paragraph to the Secretary."

(2) EFFECTIVE DATE.—The amendment made by paragraph (1) shall apply to sales or exchanges after March 14, 1995.

SEC. 4. DENIAL OF EARNED INCOME CREDIT FOR INDIVIDUALS HAVING MORE THAN $2,450 OF INVESTMENT INCOME.

(a) IN GENERAL.—Section 32 of the Internal Revenue Code of 1986 is amended by redesignating subsections (i) and (j) as subsections (j) and (k), respectively, and by inserting after subsection (h) the following new subsection:

"(i) DENIAL OF CREDIT FOR INDIVIDUALS HAVING MORE THAN $2,450 OF INVESTMENT INCOME.—

"(1) IN GENERAL.—No credit shall be allowed under subsection (a) for the taxable year if the aggregate amount of disqualified income of the taxpayer for the taxable year exceeds $2,450.

"(2) DISQUALIFIED INCOME.—For purposes of paragraph (1), the term 'disqualified income' means—

"(A) interest which is received or accrued during the taxable year (whether or not exempt from tax),

"(B) dividends to the extent includible in gross income for the taxable year, and

"(C) the excess (if any) of—

"(i) gross income from rents or royalties not derived in the ordinary course of a trade or business, over

"(ii) the sum of—

"(I) expenses (other than interest) which are clearly and directly allocable to such gross income, plus

"(II) interest expenses properly allocable to such gross income."

(b) EFFECTIVE DATE.—The amendments made by this section shall apply to taxable years beginning after December 31, 1995.

SEC. 5. REVISION OF TAX RULES ON EXPATRIATION.

(a) IN GENERAL.—Subpart A of part II of subchapter N of chapter 1 of the Internal Revenue Code of 1986 is amended by inserting after section 877 the following new section:

"SEC. 877A. TAX RESPONSIBILITIES OF EXPATRIATION.

"(a) GENERAL RULE.—For purposes of this subtitle, if any United States citizen relinquishes his citizenship during a taxable year—

"(1) except as provided in subsection (f)(2), all property held by such citizen at the time immediately before such relinquishment shall be treated as sold at such time for its fair market value, and

"(2) notwithstanding any other provision of this title, any gain or loss shall be taken into account for such taxable year.

Paragraph (2) shall not apply to amounts excluded from gross income under part III of subchapter B.

"(b) EXCLUSION FOR CERTAIN GAIN.—The amount which would (but for this subsection) be includible in the gross income of any individual by reason of subsection (a) shall be reduced (but not below zero) by $600,000.

"(c) PROPERTY TREATED AS HELD.—For purposes of this section, except as otherwise provided by the Secretary, an individual shall be treated as holding—

"(1) all property which would be includible in his gross estate under chapter 11 were such individual to die at the time the property is treated as sold,

"(2) any other interest in a trust which the individual is treated as holding under the rules of subsection (f)(1), and

"(3) any other interest in property specified by the Secretary as necessary or appropriate to carry out the purposes of this section.

"(d) EXCEPTIONS.—The following property shall not be treated as sold for purposes of this section:

"(1) UNITED STATES REAL PROPERTY INTERESTS.—Any United States real property interest (as defined in section 897(c)(1)), other than stock of a United States real property holding corporation which does not, on the date the individual relinquishes his citizenship, meet the requirements of section 897(c)(2).

"(2) INTEREST IN CERTAIN RETIREMENT PLANS.—

"(A) IN GENERAL.—Any interest in a qualified retirement plan (as defined in section 4974(c)), other than any interest attributable to contributions which are in excess of any limitation or which violate any condition for taxfavored treatment.

"(B) FOREIGN PENSION PLANS.—

"(i) IN GENERAL.—Under regulations prescribed by the Secretary, interests in foreign pension plans or similar retirement arrangements or programs.

"(ii) LIMITATION.—The value of property which is treated as not sold by reason of this subparagraph shall not exceed $500,000.

"(e) RELINQUISHMENT OF CITIZENSHIP.—For purposes of this section, a citizen shall be treated as relinquishing his United States citizenship on the earliest of—

"(1) the date the individual renounces his United States nationality before a diplomatic or consular officer of the United States pursuant to paragraph (5) of section 349(a) of the Immigration and Nationality Act (8 U.S.C. 1481(a)(5)),

"(2) the date the individual furnishes to the United States Department of State a signed statement of voluntary relinquishment of United States nationality confirming the performance of an act of expatriation specified in paragraph (1), (2), (3), or (4) of section 349(a) of the Immigration and Nationality Act (8 U.S.C. 1481(a)(1)-(4)),

"(3) the date the United States Department of State issues to the individual a certificate of loss of nationality, or

"(4) the date a court of the United States cancels a naturalized citizen's certificate of naturalization.

Paragraph (1) or (2) shall not apply to any individual unless the renunciation or voluntary relinquishment is subsequently approved by the issuance to the individual of a certificate of loss of nationality by the United States Department of State.

"(f) SPECIAL RULES APPLICABLE TO BENEFICIARIES' INTERESTS IN TRUST.—

"(1) DETERMINATION OF BENEFICIARIES' INTEREST IN TRUST.—For purposes of this section—

"(A) GENERAL RULE.—A beneficiary's interest in a trust shall be based upon all relevant facts and circumstances, including the terms of the trust instrument and any letter of wishes or similar document, historical patterns of trust distributions, and the existence of and functions performed by a trust protector or any similar advisor.

"(B) SPECIAL RULE.—In the case of beneficiaries whose interests in a trust cannot be determined under subparagraph (A)—

"(i) the beneficiary having the closest degree of kinship to the grantor shall be treated as holding the remaining interests in the trust not determined under subparagraph (A) to be held by any other beneficiary, and

"(ii) if 2 or more beneficiaries have the same degree of kinship to the grantor, such remaining interests shall be treated as held equally by such beneficiaries.

"(C) CONSTRUCTIVE OWNERSHIP.—If a beneficiary of a trust is a corporation, partnership, trust, or estate, the shareholders, partners, or

beneficiaries shall be deemed to be the trust beneficiaries for purposes of this section.

"(D) TAXPAYER RETURN POSITION.—A taxpayer shall clearly indicate on its income tax return—

"(i) the methodology used to determine that taxpayer's trust interest under this section, and

"(ii) if the taxpayer knows (or has reason to know) that any other beneficiary of such trust is using a different methodology to determine such beneficiary's trust interest under this section.

"(2) DEEMED SALE IN CASE OF TRUST INTEREST.—If an individual who relinquishes his citizenship during the taxable year is treated under paragraph (1) as holding an interest in a trust for purposes of this section—

"(A) the individual shall not be treated as having sold such interest,

"(B) such interest shall be treated as a separate share in the trust, and

"(C)(i) such separate share shall be treated as a separate trust consisting of the assets allocable to such share,

"(ii) the separate trust shall be treated as having sold its assets immediately before the relinquishment for their fair market value and as having distributed all of its assets to the individual as of such time, and

"(iii) the individual shall be treated as having recontributed the assets to the separate trust.

Subsection (a)(2) shall apply to any income, gain, or loss of the individual arising from a distribution described in subparagraph (B)(ii).

"(g) TERMINATION OF DEFERRALS, ETC.—On the date any property held by an individual is treated as sold under subsection (a), notwithstanding any other provision of this title—

"(1) any period during which recognition of income or gain is deferred shall terminate, and

"(2) any extension of time for payment of tax shall cease to apply and the unpaid portion of such tax shall be due and payable at the time and in the manner prescribed by the Secretary.

"(h) RULES RELATING TO PAYMENT OF TAX.—

"(1) IMPOSITION OF TENTATIVE TAX.—

"(A) IN GENERAL.—If an individual is required to include any amount in gross income under subsection (a) for any taxable year, there is hereby imposed, immediately before the individual relinquishes United States citizenship, a tax in an amount equal to the amount of tax which would be imposed if the taxable year were a short tax-

able year ending on the date of such relinquishment.

"(B) DUE DATE.—The due date for any tax imposed by subparagraph (A) shall be the 90th day after the date the individual relinquishes United States citizenship.

"(C) TREATMENT OF TAX.—Any tax paid under subparagraph (A) shall be treated as a payment of the tax imposed by this chapter for the taxable year to which subsection (a) applies.

"(2) DEFERRAL OF TAX.—The provisions of section 6161 shall apply to the portion of any tax attributable to amounts included in gross income under subsection (a) in the same manner as if such portion were a tax imposed by chapter 11.

"(i) REGULATIONS.—The Secretary shall prescribe such regulations as may be necessary or appropriate to carry out the purposes of this section, including regulations providing appropriate adjustments to basis to reflect gain recognized by reason of subsection (a) and the exclusion provided by subsection (b).

"(j) CROSS REFERENCE.—

"For termination of United States citizenship for tax purposes, see section 7701(a)(47)."

(b) DEFINITION OF TERMINATION OF UNITED STATES CITIZENSHIP.—Section 7701(a) of the Internal Revenue Code of 1986 is amended by adding at the end the following new paragraph:

"(47) TERMINATION OF UNITED STATES CITIZENSHIP.—An individual shall not cease to be treated as a United States citizen before the date on which the individual's citizenship is treated as relinquished under section 877A(e)."

(c) CONFORMING AMENDMENT.—Section 877 of the Internal Revenue Code of 1986 is amended by adding at the end the following new subsection:

"(f) APPLICATION.—This section shall not apply to any individual who relinquishes (within the meaning of section 877A(e)) United States citizenship on and after February 6, 1995."

(d) CLERICAL AMENDMENT.—The table of sections for subpart A of part II of subchapter N of chapter 1 of the Internal Revenue Code of 1986 is amended by inserting after the item relating to section 877 the following new item:

"Sec. 877A. Tax responsibilities of expatriation."

(e) EFFECTIVE DATE.—

(1) IN GENERAL.—The amendments made by this section shall apply to United States citizens who relinquish (within the meaning of section 877A(e) of the In-

ternal Revenue Code of 1986, as added by this section) United States citizenship on or after February 6, 1995.

(2) DUE DATE FOR TENTATIVE TAX.—The due date under section 877A(h)(1)(B) of such Code shall in no event occur before the 90th day after the date of the enactment of this Act.

I. LEGISLATIVE BACKGROUND

H.R. 831 was passed by the House of Representatives on February 21, 1995, by a vote of 381 to 44. As passed by the House of Representatives, H.R. 831 would: (1) extend permanently the 25-percent deduction for health insurance costs of self-employed individuals; (2) repeal the provision (Code section 1071) permitting nonrecognition of gain on sales and exchanges effectuating policies of the Federal Communications Commission ("FCC"); (3) provide that the nonrecognition of gain on involuntary conversions is not to apply if replacement property is acquired from a related person (Code section 1033); and (4) deny the earned income tax credit ("EITC") to individuals who have more than $3,150 of taxable interest and dividend income and phase out the EITC for individuals with more than $2,500 of taxable interest and dividend income. [1]

On March 7, 1995, the Committee on Finance held a public hearing on the application of Internal Revenue Code section 1071 under the FCC's tax certificate program. On February 8, 1995, the Committee on Finance held a public hearing on the revenue provisions in the President's fiscal year 1996 budget proposal, which includes provisions relating to the EITC and tax treatment of U.S. citizens who relinquish their citizenship.

On March 15, 1995, the Committee on Finance held a markup of H.R. 831, and ordered the bill to be reported with modifications (a committee amendment in the nature of a substitute for H.R. 831 as passed by the House).

II. SUMMARY

As reported by the Committee on Finance, H.R. 831 would:

(1) Provide a 25-percent deduction for health insurance expenses of self-employed individuals for taxable years beginning in 1994, and a 30-percent deduction for taxable years beginning in 1995 and thereafter.

(2) Repeal Code section 1071, generally effective for sales or exchanges on or after January 17, 1995, and sales or exchanges before that date if the FCC tax certificate with respect to the sale or exchange is issued on or after that date.

(3) Modify Code section 1033 to provide that, in the case of a C corporation, deferral of gain is not available when replacement property or stock is purchased from a related party. This provision is effective with respect to involuntary conversions occurring on or after February 6, 1995. Also, provide that sales or exchanges that are certified by the FCC as made by a taxpayer in connection with a microwave relocation from the 1850–1990MHz spectrum by reason of the FCC's reallocation of that spectrum for use for personal

[1] For a description of H.R. 831 as reported by the House Committee on Ways and Means, see H. Rept. No. 104–32, 104th Cong., 1st Sess. (1995).

communications services ("PCS") would be treated as an involuntary conversion to which section 1033 applies. This provision applies to sales or exchanges occurring before January 1, 2000.

(4) Deny the earned income tax credit to taxpayers if the aggregate amount of interest income (whether or not exempt from tax), dividend income, net rental income and royalties exceeds $2,450, effective for taxable years beginning after December 31, 1995.

(5) Provide that U.S. citizens who relinquish their citizenship are required to recognize, and pay income tax on, unrealized and deferred gains with respect to property held immediately prior to the expatriation. This provision is effective for U.S. citizens who relinquish citizenship on or after February 6, 1995. Provided that the revenues raised from the provision to tax gains on property held by U.S. citizens who relinquish their citizenship will be reserved for deficit reduction, and will not be used to offset the tax relief provisions of the bill or any subsequent legislation.

III. EXPLANATION OF PROVISIONS

A. PERMANENTLY EXTEND AND INCREASE DEDUCTION FOR HEALTH INSURANCE COSTS OF SELF-EMPLOYED INDIVIDUALS (SEC. 1 OF THE BILL AND SEC. 162(L) OF THE CODE)

Present Law

Under present law, the tax treatment of health insurance expenses depends on whether the taxpayer is an employee and whether the taxpayer is covered under a health plan paid for by the employee's employer. An employer's contribution to a plan providing accident or health coverage for the employee and the employee's spouse and dependents is excludable from an employee's income. The exclusion is generally available in the case of owners of a business who are also employees.

In the case of self-employed individuals (i.e., sole proprietors or partners in a partnership) no equivalent exclusion applies. However, prior law provided a deduction for 25 percent of the amount paid for health insurance for a self-employed individual and the individual's spouse and dependents. The 25-percent deduction was available with respect to the cost of a self-insured plan as well as commercial insurance. However, in the case of self-insurance, the deduction was not available unless the self-insured plan was in fact insurance (e.g., there is appropriate risk shifting) and not merely a reimbursement arrangement. The 25-percent deduction was not available for any month if the taxpayer was eligible to participate in a subsidized health plan maintained by the employer of the taxpayer or the taxpayer's spouse. In addition, no deduction was available to the extent that the deduction exceeded the taxpayer's earned income. The amount of expenses paid for health insurance in excess of the deductible amount could be taken into account in determining whether the individual was entitled to an itemized deduction for medical expenses. The 25-percent deduction expired for taxable years beginning after December 31, 1993.

For purposes of these rules, more than 2-percent shareholders of S corporations are treated the same as self-employed individuals. Thus, they were entitled to the 25-percent deduction.

Other individuals who purchase their own health insurance (e.g., someone whose employer does not provide health insurance) can deduct their insurance premiums only to the extent that the premiums, when combined with other unreimbursed medical expenses, exceed 7.5 percent of adjusted gross income.

Reasons for Change

The 25-percent deduction for health insurance costs of self-employed individuals was added by the Tax Reform Act of 1986 to reduce the disparity between the tax treatment of owners of incorporated and unincorporated businesses. The provision was enacted on a temporary basis, and has been extended several times since enactment.

The Committee believes it is appropriate to continue to reduce the disparity between the tax treatment of health insurance expenses of owners of incorporated and unincorporated businesses. Further, the Committee believes that the pattern of allowing the deduction to expire and then extending it creates unneeded uncertainty for taxpayers. Thus, the Committee believes the deduction should be made permanent.

In addition, because the Committee believes that self-employed individuals should be entitled to a deduction for their health insurance expenses in the same manner as owners of incorporated businesses, the Committee finds it appropriate to increase the level of the deduction from 25 to 30 percent, beginning in 1995.

Explanation of Provision

The bill retroactively reinstates for 1994 the deduction for 25-percent of health insurance costs of self-employed individuals and extends the deduction permanently. For years beginning after December 31, 1994, the deduction is increased to 30 percent.

Effective Date

The provision is generally effective for taxable years beginning after December 31, 1993. The increase in the deduction to 30 percent of health insurance costs is effective for taxable years beginning after December 31, 1994.

B. REPEAL SPECIAL RULES APPLICABLE TO FCC-CERTIFIED SALES OF BROADCAST PROPERTIES (SEC. 2 OF THE BILL AND SEC. 1071 OF THE CODE)

Present Law and Background

Tax treatment of a seller of broadcast property

General tax rules

Under generally applicable Code provisions, the seller of a business, including a broadcast business, recognizes gain to the extent the sale price (and any other consideration received) exceeds the seller's basis in the property. The recognized gain is then subject to the current income tax unless the gain is deferred or not recognized under a special tax provision.

Special rules under Code section 1031

Under Code section 1031, no gain or loss is recognized if property held for productive use in a trade or business or for investment is exchanged for property of a "like kind" that is to be held for productive use in a trade or business or for investment. The nonrecognition rules do not apply to an exchange of one class or kind of property for property of a different class or kind.[2] The different classes of property are: (1) depreciable tangible personal property; (2) intangible personal property; and (3) real property.[3] Corporate stock or partnership interests do not qualify as like-kind replacement property.

If an exchange consists not only of like-kind property, but also of other property or money, then gain from the transaction is recognized to the extent of the money and the fair market value of the other property, and no loss from the transaction may be recognized. The basis of property received in a like-kind transaction generally is the same as the basis of any property exchanged, decreased by the amount of money received or loss recognized on the exchange and increased by the amount of gain recognized on the exchange. Special rules apply to exchanges between related persons, which generally require the parties to the transaction to hold the exchanged property for at least two years after the exchange.

Special rules under Code section 1033

Under Code section 1033, gain realized by a taxpayer from certain involuntary conversions of property is deferred to the extent the taxpayer purchases property similar or related in service or use to the converted property. The replacement property may be acquired directly or by acquiring control of a corporation (generally, 80 percent of the stock of the corporation) that owns replacement property. The taxpayer's basis in the replacement property generally is the same as the taxpayer's basis in the converted property, decreased by the amount of any money or loss recognized on the conversion, and increased by the amount of any gain recognized on the conversion.

Only involuntary conversions that result from destruction, theft, seizure, or condemnation (or threat or imminence thereof) are eligible for deferral under Code section 1033. In addition, the term "condemnation" refers to the process by which private property is taken for public use without the consent of the property owner but upon the award and payment of just compensation, according to a ruling by the Internal Revenue Service (IRS).[4] Thus, for example, an order by a Federal court to a corporation to divest itself of ownership of certain stock because of anti-trust rules is not a condemnation (or a threat or imminence thereof), and the divestiture is not eligible for deferral under this provision.[5] Under another IRS ruling, the "threat or imminence of condemnation" test is satisfied if, prior to the execution of a binding contract to sell the property, "the property owner is informed, either orally or in writing by a representative of a governmental body or public official authorized

[2] Treas. Reg. sec. 1.1031(a)–1(b).
[3] Treas. Reg. sec. 1.1031(a)–2.
[4] Rev. Rul. 58–11, 1958–1 C.B. 273.
[5] Id.

to acquire property for public use, that such body or official has decided to acquire his property, and from the information conveyed to him has reasonable grounds to believe that his property will be condemned if a voluntary sale is not arranged."[6] However, under this ruling, the threatened taking also must constitute a condemnation, as defined above.

Special rules under Code section 1071

Under Code section 1071, if the FCC certifies that a sale or exchange of property is necessary or appropriate to effectuate a change in a policy of, or the adoption of a new policy by, the FCC with respect to the ownership and control of "radio broadcasting stations," a taxpayer may elect to treat the sale or exchange as an involuntary conversion. The FCC is not required to determine the tax consequences of certifying a sale or to consult with the IRS about the certification process.[7] No other provision of the Internal Revenue Code grants a Federal agency or any other party the type of complete discretion conveyed to the FCC by Code section 1071.

Under Code section 1071, the replacement requirement in the case of FCC-certified sales may be satisfied by purchasing stock of a corporation that owns broadcasting property, whether or not the stock represents control of the corporation. In addition, even if the taxpayer does not reinvest all the sales proceeds in similar or related replacement property, the taxpayer nonetheless may elect to defer recognition of gain if the basis of depreciable property that is owned by the taxpayer immediately after the sale or that is acquired during the same taxable year is reduced by the amount of deferred gain.

Tax treatment of a buyer of broadcast property

Under generally applicable Code provisions, the purchaser of a broadcast business, or any other business, acquires a basis equal to the purchase price paid. In an asset acquisition, a buyer must allocate the purchase price among the purchased assets to determine the buyer's basis in these assets. In a stock acquisition, the buyer generally takes a basis in the stock equal to the purchase price paid, and the business retains its basis in the assets. This treatment applies whether or not the seller of the broadcast property has received an FCC certificate exempting the sale transaction from the normal tax treatment.

FCC tax certificate program

Multiple ownership policy

The FCC originally adopted multiple ownership rules in the early 1940s.[8] These rules prohibited broadcast station owners from owning more than one station in the same service area, and, generally, more than six high frequency (radio) or three television stations. Owners wishing to acquire additional stations had to divest them-

[6] Rev. Rul. 74–8, 1974–1 C.B. 200.

[7] The FCC allows sellers applying for FCC certificates in cable transactions to delete both the sales price and the number of subscribers from the transaction documents submitted with the request for the certificates.

[8] 5 Fed. Reg. 2382 (June 26, 1940) (multiple ownership rules for high frequency broadcast stations); 5 Fed. Reg. 2284 (May 6, 1941) (multiple ownership rules for television stations).

selves of stations they already owned in order to remain in compliance with the FCC's rules.

In November 1943, the FCC adopted a rule that prohibited duopolies (ownership of more than one station in the same city).[9] After these rules were adopted, owners wishing to acquire additional stations in excess of the national ownership limit had to divest themselves of stations they already owned in order to remain in compliance with the FCC's rules. After Code section 1071 was adopted in 1943, in some cases, parties petitioned the FCC for tax certificates pursuant to Code section 1071 when divesting themselves of stations. These divestitures were labeled "voluntary divestitures" by the FCC. When the duopoly rule was adopted, 35 licensees that held more than one license in a particular city were required by the rule "involuntarily" to divest themselves of one of the licenses.[10]

Minority ownership policy

In 1978, the FCC announced a policy of promoting minority ownership of broadcast facilities by offering an FCC tax certificate to those who voluntarily sell such facilities (either in the form of assets or stock) to minority individuals or minority-controlled entities.[11] The FCC's policy was based on the view that minority ownership of broadcast stations would provide a significant means of fostering the inclusion of minority views in programming, thereby serving the needs and interests of the minority community as well as enriching and educating the non-minority audience. The FCC subsequently expanded its policy to include the sale of cable television systems to minorities as well.[12]

"Minorities," within the meaning of the FCC's policy, include "Blacks, Hispanics, American Indians, Alaska Natives, Asians, and Pacific Islanders."[13] As a general rule, a minority-controlled corporation is one in which more than 50 percent of the voting stock is held by minorities. A minority-controlled limited partnership is one in which the general partner is a minority or minority-controlled, and minorities have at least a 20-percent interest in the partnership.[14] The FCC requires those who acquire broadcast properties with the help of the FCC tax certificate policy to hold those properties for at least one year.[15] An acquisition can qualify even if there is a pre-existing agreement (or option) to buy out the minority interests at the end of the one-year holding period, providing that the transaction is at arm's-length.

In 1982, the FCC further expanded its tax certificate policy for minority ownership. At that time, the FCC decided that, in addition to those who sell properties to minorities, investors who contribute to the stabilization of the capital base of a minority enter-

[9] 8 Fed. Reg. 16065 (Nov. 23, 1943).

[10] FCC Announces New Policy Relating to Issuance of Tax Certificates, 14 FCC2d 827 (1956).

[11] Minority Ownership of Broadcasting Facilities, 68 FCC2d 979 (1978).

[12] Minority Ownership of Cable Television Systems, 52 R.R.2d 1469 (1982).

[13] 52 R.R.2d at n. 1.

[14] Commission's Policy Regarding the Advancement of Minority Ownership in Broadcasting, Policy Statement, and Notice of Proposed Rulemaking, 92 FCC2d 853–855 (1982).

[15] See Amendment of Section 73.3597 of the Commission's Rules (Applications for Voluntary Assignments or Transfers of Control), 57 R.R.2d 1149 (1985). Anti-trafficking rules require cable properties to be held for at least three years (unless the property is sold pursuant to a tax certificate).

prise would be entitled to a tax certificate upon the subsequent sale of their interest in the minority entity.[16] To qualify for an FCC tax certificate in this circumstance, an investor must either (1) provide start-up financing that allows a minority to acquire either broadcast or cable properties, or (2) purchase shares in a minority-controlled entity within the first year after the license necessary to operate the property is issued to the minority. An investor can qualify for a tax certificate even if the sale of the interest occurs after participation by a minority in the entity has ceased. In these situations, the status of the divesting investor and the purchaser of the divested interest is irrelevant, because the goal is to increase the financing opportunities available to minorities.

Personal communications services ownership policy

In 1993, Congress provided for the orderly transfer of frequencies, including frequencies that can be licensed pursuant to competitive bidding procedures.[17] The FCC has adopted rules to conduct auctions for the award of more than 2,000 licenses to provide personal communications services ("PCS"). PCS will be provided by means of a new generation of communication devices that will include small, lightweight, multi-function portable phones, portable facsimile and other imaging devices, new types of multichannel cordless phones, and advanced paging devices with two-way data capabilities. The PCS auctions (which began last year) will constitute the largest auction of public assets in American history and are expected to generate billions of dollars for the United States Treasury.[18]

The FCC has designed procedures to ensure that small businesses, rural telephone companies and businesses owned by women and minorities have "the opportunity to participate in the provision" of PCS, as Congress directed in 1993.[19] To help minorities and women participate in the auction of the PCS licenses, the FCC took several steps including up to a 25-percent bidding credit, a reduced upfront payment requirement, a flexible installment payment schedule, and an extension of the tax certificate program for businesses owned by minorities and women.[20]

The FCC will employ the tax certificate program in three ways: (1) initial investors (who provide "start-up" financing or purchase interests within the first year after license issuance) in minority and woman-owned PCS businesses will be eligible for FCC tax certificates upon the sale of their investments; (2) holders of PCS licenses will be able to obtain FCC tax certificates upon the sale of the business to a company controlled by minorities and women; and (3) a cellular operator that sells its interest in an overlapping cellular system to a minority or a woman-owned business to come into compliance with the FCC PCS/cellular cross-ownership rule will be eligible for a tax certificate. In addition, as discussed below, the FCC will issue tax certificates for PCS to encourage fixed micro-

[16] Commission Policy Regarding the Advancement of Minority Ownership in Broadcasting, 92 FCC2d 849 (1982).
[17] Omnibus Budget Reconciliation Act of 1993, P.L. 103–66, Title VI.
[18] Fifth Report and Order, 9 FCC Rcd 5532 (1994).
[19] Omnibus Budget Reconciliation Act of 1993, P.L. 103–66, section 6002(a).
[20] Installment payments are available to small businesses and rural telephone companies.

wave operators voluntarily to relocate to clear a portion of the spectrum for PCS technologies.

Microwave relocation policy

PCS can operate only on frequencies below 3GHz. However, because that frequency range is currently occupied by various private fixed microwave communications systems (such as railroads, oil pipelines, and electric utilities), there are no large blocks of unallocated spectrum available to PCS. To accommodate PCS, the FCC has reallocated the spectrum; the 1850–1990MHz spectrum will be used for PCS, and the microwave systems will be required to move to higher frequencies. Current occupants of the 1850–1990MHz spectrum allocated to PCS must relocate to higher frequencies not later than three years after the close of the bidding process.[21] In accordance with FCC rules, these current occupants have the right to be compensated for the cost of replacing their old equipment, which can operate only on the 1850–1990MHz spectrum, with equipment that will operate at the new, higher frequency. At a minimum, the winners of the new PCS licenses must pay for and install new facilities to enable the incumbent microwave operators to relocate. The amount of these payments and characteristics of the new equipment will be the subject of negotiation between the incumbent microwave operators and the PCS licensees; thus, the nature of the compensation (i.e., solely replacement equipment, or a combination of replacement equipment plus a cash payment) is unknown at present. If no agreement is reached within the 3-year voluntary negotiation period, the microwave operators will be required by the FCC to vacate the spectrum; however, the timing of such relocation is uncertain because the relocation would take place only after completion of a formal negotiation process in which the FCC would be a participant.

The FCC will employ the tax certificate program for PCS to encourage fixed microwave operators voluntarily to relocate from the 1850–1990MHz band to clear the band for PCS technologies.[22] Tax certificates will be available to incumbent microwave operators that relocate voluntarily within three years following the close of the bidding process. Thus, the certificates are intended to encourage such occupants to relocate more quickly than they otherwise would and to clarify the tax treatment of such transactions.[23]

Congressional appropriations rider

Since fiscal year 1988, in appropriations legislation, the Congress has prohibited the FCC from using any of its appropriated funds to repeal, to retroactively apply changes in, or to continue a reexamination of its comparative licensing, distress sale and tax certificate policies.[24] This limitation has not prevented an expansion of

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[21] The PCS auctions for the 1850–1990MHz spectrum commenced in December, 1994.

[22] See, Third Report and Order and Memorandum Opinion and Order, 8 FCC Rcd 6589 (1993).

[23] The transaction between the PCS licensee and the incumbent microwave operator might qualify for tax-free treatment as a like kind exchange under Code section 1031 or as an involuntary conversion under Code section 1033. However, the availability of deferral under these Code provisions may be uncertain in certain circumstances. For example, it may be unclear whether the transaction would qualify as an involuntary conversion under currently applicable IRS standards.

[24] Pub. L. No. 100–202 (1987).

the existing program.[25] The current rider will expire at the end of the 1995 fiscal year, September 30, 1995.

Reasons for Change

The Committee, in its review of the administration and operation of Code section 1071, found serious tax policy problems with this provision. As an initial matter, the standards pursuant to which the FCC will issue tax certificates have evolved far beyond what Congress originally contemplated. Congress originally intended Code section 1071 to alleviate the burden of taxpayers who had been forced to sell their radio stations under difficult wartime circumstances. The FCC has interpreted the provision to permit the FCC to grant unlimited tax benefits for routine and voluntary sales of a wide range of communication properties.

In addition, the FCC's standards for issuing tax certificates have been so vague that the program appears to have been subject to significant abuse. For example, the FCC's definition of "control" for purposes of its minority ownership policies provides little guarantee that a minority will effectively manage a broadcast property after the sale of property has been certified. In addition, because the FCC generally requires only one year of minority ownership or control to qualify for a tax certificate, section 1071 has frequently resulted in only transitory minority ownership of broadcast properties, i.e., in many cases the granting of the tax certificate has not resulted in achieving the objective of minority ownership or control.

Further, the FCC's interpretation and administration of the tax certificate program has not been supervised or subject to any systematic review by the IRS, or any other government body that could evaluate the tax cost of the program. In granting tax certificates, the FCC does not take into account or request any information regarding the size of the potential tax benefit involved. The FCC also does not request any showing or representation that the amount of the tax benefits, which at least initially accrue to the non-minority seller generally, is in any way reflected in the form of a lower purchase price to the minority-owned or controlled purchaser. As a result, it is possible that, in many cases, the entire tax benefit accrues to the non-minority seller.

From a tax policy perspective, the Committee found serious deficiencies in section 1071. No other provision of the Internal Revenue Code conveys the level of discretion to a Federal government agency comparable to the discretion conveyed on the FCC by section 1071. Thus, section 1071 grants the authority to the FCC to administer what is, in effect, an open-ended entitlement program with no constraints imposed to limit the extent to which the FCC may utilize the provision.

As a result of these considerations, the Committee concluded that the tax cost of the FCC tax certificate program far outweighs any demonstrated benefit of the program. The Committee also concluded that the section is inconsistent with sound tax policy. The Committee therefore is repealing the provision.

[25] The appropriations restriction "does not prohibit the agency from taking steps to create greater opportunity for minority ownership." H. Rept. No. 103–708 (Conf. Rept.), 103d Cong. 2d Sess. 40 (1994).

Explanation of Provision

The bill repeals Code section 1071. Thus, a sale or exchange of broadcast properties would be subject to the same tax rules applicable to all other taxpayers engaged in the sale or exchange of a business.

Effective Date

The repeal of section 1071 is effective for (1) sales or exchanges on or after January 17, 1995,[26] and (2) sales or exchanges before that date if the FCC tax certificate with respect to the sale or exchange is issued on or after that date. The provision does not apply to taxpayers who have entered into a binding written contract (or have completed a sale or exchange pursuant to a binding written contract) before January 17, 1995, and who have applied for an FCC tax certificate by that date. A contract is treated as not binding for this purpose if the sale or exchange pursuant to the contract (or the material terms of the contract) were contingent on January 16, 1995, on issuance of an FCC tax certificate. A sale or exchange would not be contingent on January 16, 1995, on issuance of an FCC tax certificate if the tax certificate had been issued by the FCC by that date.

C. PROHIBIT NONRECOGNITION OF GAIN ON INVOLUNTARY CONVERSIONS IN CERTAIN RELATED-PARTY TRANSACTIONS; APPLICATION OF SECTION 1033 TO CERTAIN MICROWAVE RELOCATION TRANSACTIONS (SEC. 3 OF THE BILL AND SEC. 1033 OF THE CODE)

Present Law

As described above (Part III.B.), under Code section 1033, gain realized by a taxpayer from certain involuntary conversions of property is deferred to the extent the taxpayer purchases property similar or related in service or use to the converted property within a specified period.

Under rulings issued by the IRS to taxpayers, property (stock or assets) purchased from a related person may, in some cases, qualify as property similar or related in service or use to the converted property.[27] Thus, in certain circumstances, related taxpayers may obtain significant (and possibly indefinite or permanent) tax deferral without any additional cash outlay to acquire new properties. In cases in which a taxpayer purchases stock as replacement property, section 1033 permits the taxpayer to reduce basis of stock, but does not require any reduction in the basis of the underlying assets. Thus, the reduction in basis of stock does not result in reduced depreciation deductions.

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[26] On January 17, 1995, House Committee on Ways and Means Chairman Archer issued a press release announcing that the Committee on Ways and Means would immediately review the operation of section 1071 to explore possible legislative changes to section 1071, including the possibility of repeal. The press release stated that any changes to section 1071 may apply to transactions completed, or certificates issued by the FCC, on or after the date of the announcement.

[27] See, e.g., PLR 8132072, PLR 8020069. Private letter rulings do not have precedential authority and may not be relied upon by any taxpayer other than the taxpayer receiving the ruling but are some indication of IRS administrative practice.

Reasons for Change

In the course of its deliberations, the Committee also became aware of problems with the operation of Code section 1033. Under interpretations issued by the IRS, taxpayers are able to purchase replacement property from a related party, thereby avoiding the need to buy "new" replacement property and, sometimes, effectively resulting in a total tax forgiveness for the transaction. The Committee intends that, in the future, corporate taxpayers be required to buy replacement property only from unrelated persons in order to receive the special tax treatment under section 1033.

In addition, the Committee sought to ensure tax-free treatment for transactions between PCS licensees and the incumbent microwave operators in connection with the relocation of the microwave operators from the 1850–1990MHz spectrum by reason of the FCC's reallocation of that spectrum for use for PCS. (See description of present law, Part III.B.) Thus, the Committee intends that such transactions constitute involuntary conversions under Code section 1033. However, no inference is intended with respect to the nature or appropriate tax treatment of any other transactions.

Explanation of Provision

Related-party transactions

Under the bill, subchapter C corporations are not entitled to defer gain under Code section 1033 if the replacement property or stock is purchased from a related person. A person is treated as related to another person if the person bears a relationship to the other person described in Code section 267(b) or 707(b)(1). An exception to the general rule provides that a taxpayer could purchase replacement property or stock from a related person and defer gain under Code section 1033 to the extent the related person acquired the replacement property or stock from an unrelated person within the period prescribed under Code section 1033. Thus, property acquired from outside the group within the period prescribed by section 1033 and retransferred to the taxpayer member of the group within the prescribed time period, will qualify in the hands of the taxpayer to the extent that the property's basis or other net tax consequences to the group do not change as a result of the transfer.

Microwave relocation transactions

The bill provides that sales or exchanges that are certified by the FCC as having been made by a taxpayer in connection with the relocation of the taxpayer from the 1850–1990MHz spectrum by reason of the FCC's reallocation of that spectrum for use for PCS would be treated as involuntary conversions to which Code section 1033 applies.

Effective Date

The provision prohibiting the purchase of qualified replacement property from a related party applies to involuntary conversions occurring on or after February 6, 1995.

The provision treating certain microwave relocation transactions as involuntary conversions applies to sales or exchanges occurring before January 1, 2000.

D. DENY EARNED INCOME TAX CREDIT FOR TAXPAYERS WITH MORE THAN $2,450 OF INVESTMENT INCOME (SEC. 4 OF THE BILL AND SEC. 32 OF THE CODE)

Present Law

Eligible low-income workers are able to claim a refundable earned income tax credit (EITC). The amount of the credit an eligible taxpayer may claim depends upon whether the taxpayer has one, more than one, or no qualifying children and is determined by multiplying the credit rate by the taxpayer's earned income up to an earned income threshold. The maximum amount of the credit is the product of the credit rate and the earned income threshold. For taxpayers with earned income (or adjusted gross income, if greater) in excess of the phaseout threshold, the credit amount is reduced by the phaseout rate multiplied by the amount of earned income (or adjusted gross income, if greater) in excess of the phaseout threshold. The credit is not allowed if earned income (or adjusted gross income, if greater) exceeds the phaseout limit. There is no additional limitation on the amount of unearned income that the taxpayer may receive.

The parameters for the EITC depend upon the number of qualifying children the taxpayer claims. For 1995 the parameters are as follows:

	Two or more qualifying children—	One qualifying child—	No qualifying children—
Credit rate (in percent)	36.00	34.00	7.65
Phaseout rate (in percent)	20.22	15.98	7.65
Earned income threshold	$8,640	$6,160	$4,100
Maximum credit	$3,110	$2,094	$314
Phaseout threshold	$11,290	$11,290	$5,130
Phaseout limit	$26,673	$24,396	$9,230

The earned income threshold and the phaseout threshold are indexed for inflation; because the phaseout limit depends on those amounts, the phaseout rate, and the credit rate, the phaseout limit will also increase if there is inflation. Earned income consists of wages, salaries, other employee compensation, and net self-employment income.

The credit rates and phaseout rates for the EITC change over time under present law. For 1996 and after, the credit rate will be 40.00 percent and the phaseout rate will be 21.06 percent for taxpayers with two or more qualifying children. The credit rate and the phaseout rate for taxpayers with one qualifying child or no qualifying children will be the same as those listed in the table above.

To claim the EITC, a taxpayer must either have a qualifying child or must meet other requirements. A qualifying child must meet a relationship test, an age test, and a residence test. In order to claim the EITC without a qualifying child, a taxpayer must not be a dependent and must be over age 24 and under age 65.

Reasons for Change

Under present law, a taxpayer may have relatively low earned income, and therefore may be eligible for the EITC, despite also having significant unearned income. The Committee believes that the EITC should be targeted to families with the greatest need. Therefore, the Committee believes that it is inappropriate to allow an EITC to taxpayers with significant unearned income.

Explanation of Provision

Under the bill, a taxpayer is not eligible for the EITC if the aggregate amount of disqualified income of the taxpayer for the taxable year exceeds $2,450. Disqualified income is the sum of:

(1) interest (whether or not subject to tax) received or accrued in the taxable year,

(2) dividends to the extent includible in gross income for the taxable year, and

(3) net income (if greater than zero) from rents and royalties not derived in the ordinary course of business.

Disqualified income would not include interest accrued during the taxable year on a United States savings bond issued at discount under 31 U.S.C. 3105 for which a cash-basis taxpayer has not made the election under Code section 454(a) to treat such accrued interest as received in the taxable year.

Effective Date

The provision is effective for taxable years beginning after December 31, 1995.

E. IMPOSE TAX ON U.S. CITIZENS WHO RELINQUISH CITIZENSHIP (SEC. 5 OF THE BILL AND SEC. 877A OF THE CODE)

Present Law

U.S. citizens and residents generally are subject to U.S. income taxation on their worldwide income (sec. 61 of the Code and Treas. Reg. sec. 1–1.1(b)). The U.S. tax may be reduced or offset by a credit allowed for foreign income taxes paid with respect to foreign income (secs. 901–907). Nonresident aliens are taxed at a flat rate of 30 percent (or a lower treaty rate) on certain types of passive income derived from U.S. sources, and at regular graduated rates on net profits derived from a U.S. business (sec. 871).

The United States imposes tax on gains recognized by foreign persons that are attributable to dispositions of interests in U.S. real property (secs. 897, 1445, 6039C, and 6652(f), known as the Foreign Investment in Real Property Tax Act ("FIRPTA")).[28] Such

[28] Under the FIRPTA provisions, tax is imposed on gains from the disposition of an interest (other than an interest solely as a creditor) in real property (including an interest in a mine, well, or other natural deposit) located in the United States or the U.S. Virgin Islands. Also included in the definition of a U.S. real property interest is any interest (other than an interest solely as a creditor) in any domestic corporation unless the taxpayer establishes that the corporation was not a U.S. real property holding corporation (USRPHC) at any time during the five year period ending on the date of the disposition of the interest (sec. 897(c)(1)(A)(ii)). A USRPHC is any corporation, the fair market value of whose U.S. real property interests equals or exceeds 50 percent of the sum of the fair market values of (i) its U.S. real property interests,

Continued

gains generally are subject to tax at the same rates that apply to similar income received by U.S. persons. The Code imposes a withholding obligation when a U.S. real property interest is acquired from a foreign person (sec. 1445). The amount required to be withheld on the sale by a foreign investor of a U.S. real property interest is generally 10 percent of the amount realized (gross sales price) (sec. 1445(a)). However, the amount withheld generally will not exceed the transferor's maximum tax liability if a certificate for reduced withholding is issued by the Internal Revenue Service (IRS) (sec. 1445(c)(1)).

Distributions, including lump-sum distributions, that foreign persons receive from qualified U.S. retirement plans generally are subject to U.S. tax at a 30-percent rate. However, to the extent these distributions represent contributions with respect to services performed in the United States after 1986, the distributions are subject to U.S. tax at graduated rates. The U.S. tax is frequently reduced or eliminated under applicable U.S. income tax treaties.

A U.S. citizen who relinquishes U.S. citizenship with a principal purpose to avoid Federal tax may be subjected to an alternative taxing method for 10 years after expatriation (sec. 877). A special rule applies with respect to the burden of proving the existence or nonexistence of U.S. tax avoidance as one of the principal purposes of the expatriation. Under this provision, the Treasury Department may establish that it is reasonable to believe that the expatriate's loss of U.S. citizenship would, but for the application of this provision, result in a substantial reduction in the U.S. tax based on the expatriate's probable income for the taxable year (sec. 877(e)) . If this reasonable belief is established, then the expatriate must carry the burden of proving that the loss of citizenship did not have as one of its principal purposes the avoidance of U.S. income, estate or gift taxes.

Under this alternative method, the expatriate generally is taxed on his U.S. source income (net of certain deductions), as well as on certain business profits, at rates applicable to U.S. citizens and residents. Solely for this purpose, gains on the sale of property located in the United States and stocks and securities issued by U.S. persons also are treated as U.S. source income (sec. 877(c)). The alternative method applies only if it results in a higher U.S. tax liability than the amount otherwise determined for nonresident aliens.

The United States imposes its estate tax on the worldwide estates of persons who were citizens or domiciliaries of the United States at the time of death (secs. 2001, 2031), and on certain property belonging to nondomiciliaries of the United States which is located in the United States at the time of their death (secs. 2101, 2103). The U.S. gift tax is imposed on all gifts made by U.S. citizens and domiciliaries, and on gifts of property made by nondomiciliaries where the property is located in the United States at the time of the gift (sec. 2501).

(ii) its interests in foreign real property, plus (iii) any other of its assets which are used or held for use in a trade or business (sec. 897(c)(2)).

Reasons for Change

The Committee has been informed that a small number of very wealthy individuals each year relinquish their U.S. citizenship for the purpose of avoiding U.S. income, estate, and gift taxes. By so doing, such individuals reduce their annual U.S. income tax liability and eliminate their eventual U.S. estate tax liability.

The Committee recognizes that citizens of the United States have a basic right not only to physically leave the United States to live elsewhere, but also to relinquish their U.S. citizenship. The Committee does not believe that the Internal Revenue Code should be used to stop U.S. citizens from expatriating; however, the Committee also does not believe that the Code should provide a tax incentive for expatriating.

The Committee is concerned that present law, which bases the application of the alternative method of taxation under section 877 on proof of a tax-avoidance purpose, has proven difficult to administer. In addition, the Committee is concerned that the alternative method can be avoided by postponing the realization of U.S. source income for 10 years. The Committee believes that section 877 is largely ineffective to tax U.S. citizens who expatriate with a principal purpose to avoid tax.

The Committee believes that the alternative tax system of section 877 should be replaced by a tax regime that applies to expatriates who remove large amounts of appreciated assets out of U.S. tax jurisdiction, but does not rely on establishing a tax-avoidance motive. Inasmuch as U.S. citizens who retain their citizenship are subject to income tax on accrued appreciation when they dispose of their assets, as well as estate tax on the full value of assets that are held until death, the Committee believes it fair and equitable to tax expatriates on the appreciation of their assets when they relinquish their U.S. citizenship. The Committee is informed, however, that most U.S. citizens who relinquish their U.S. citizenship do not avoid large amounts of U.S. tax by so doing. Therefore, the Committee believes that an expatriation tax should not apply to expatriates who remove only modest amounts of appreciated assets out of U.S. tax jurisdiction.

The Committee approved the provision in order to reduce the Federal budget deficit. The Committee does not intend that the revenue raised from this provision be used to offset the tax-relief provisions of the bill or of any subsequent legislation.

Explanation of Provision

In general

Under the bill, a U.S. citizen who relinquishes citizenship generally is treated as having sold all of his property at fair market value immediately prior to the expatriation. Gain or loss from the deemed sale is recognized at that time, generally without regard to other provisions of the Code.[29]

[29] See the discussion of the application of the Code's income exclusions under "Other special rules" below.

Net gain on the deemed sale is recognized under the bill only to the extent it exceeds $600,000 ($1.2 million in the case of married individuals filing a joint return, both of whom expatriate).

Property taken into account

Property treated as sold by an expatriating citizen under the provision includes all items that would be included in the individual's gross estate under the Federal estate tax if such individual were to die on the day of the deemed sale, plus certain trust interests that are not otherwise includible in the gross estate (discussed below under "Interests in trusts"), and other interests that may be specified by the Treasury Department in order to carry out the purposes of the provision.

The bill provides that certain types of property, although includable in the gross estate were the expatriate to die while subject to U.S. estate tax, are not taken into account for purposes of determining the expatriation tax. U.S. real property interests, which remain subject to U.S. taxing jurisdiction in the hands of nonresident aliens, generally are not taken into account.[30] Also not taken into account are interests in qualified retirement plans, other than interests attributable to excess contributions or contributions that violate any condition for tax-favored treatment. In addition, under regulations, interests in foreign pension plans and similar retirement plans or programs are not taken into account up to a maximum amount of $500,000.

Interests in trusts

Under the bill, an expatriate who is a beneficiary of a trust is deemed to own a separate trust consisting of the assets allocable to his share of the trust, in accordance with his interest in the trust (discussed below). The separate trust is treated as selling its assets for fair market value immediately before the beneficiary relinquishes his citizenship, and distributing all resulting income and corpus to the beneficiary. The beneficiary is treated as subsequently recontributing the assets to the trust. Consequently, the separate trust's basis in the assets will be stepped up and all assets held by the separate trust will be treated as corpus.

The bill provides that a beneficiary's interest in a trust is determined on the basis of all facts and circumstances. These include the terms of the trust instrument itself, any letter of wishes or similar document, historical patterns of trust distributions, the role of any trust protector or similar advisor, and anything else of relevance. The Committee expects that the Treasury Department will issue regulations to provide guidance as to the determination of trust interests for purposes of the expatriation tax. The Committee intends that such regulations disregard de minimis interests in trusts, such as an interest of less than a certain percentage of the trust as determined on an actuarial basis, or a contingent remainder interest that has less than a certain likelihood of occurrence.

In the event that any beneficiaries' interests in the trust cannot be determined on the basis of the facts and circumstances, the ben-

[30] The exception would apply to all U.S. real property interests, as defined in section 897(c)(1), except the stock of a U.S. real property holding corporation that does not satisfy the requirements of section 897(c)(2) on the date of the deemed sale.

eficiary with the closest degree of family relationship to the settlor would be presumed to hold the remaining interests in the trust. The beneficiaries would be required to disclose on their respective tax returns the methodology used to determine that beneficiary's interest in the trust, and whether that beneficiary knows (or has reason to know) that any other beneficiary of the trust uses a different method.

The Committee intends that the special rule for interests in a trust not apply to a grantor trust. The bill follows the grantor trust rules in treating a grantor of a grantor trust as the owner of the trust assets for tax purposes. Therefore, a grantor who expatriates is treated as directly selling the assets held by the trust for purposes of computing the tax on expatriation. Similarly, a beneficiary of a grantor trust who is not treated as an owner of a portion of the trust under the grantor trust rules is not considered to hold an interest in the trust for purposes of the expatriation tax.

Date of relinquishment of citizenship

Under the bill, a U.S. citizen who renounces his U.S. nationality before a diplomatic or consular officer of the United States pursuant to section 349(a)(5) of the Immigration and Nationality Act (8 U.S.C. section 1481(a)(5)) is treated as having relinquished his citizenship on that date, provided that the renunciation is later confirmed by the issuance of a certificate of loss of nationality by the U.S. Department of State. A U.S. citizen who furnishes to the State Department a signed statement of voluntary relinquishment of U.S. nationality confirming the performance of an expatriating act specified in section 349(a)(1)–(4) of the Immigration and Nationality Act (8 U.S.C. section 1481(a)(1)–(4)) is treated as having relinquished his citizenship on the date such statement is so furnished, provided that the voluntary relinquishment is later confirmed by the issuance of a certificate of loss of nationality by the U.S. Department of State. Any other U.S. citizen to whom the Department of State issues a certificate of loss of nationality is treated as having relinquished his citizenship on the date that such certificate is issued to the individual. A naturalized citizen is treated as having relinquished his citizenship on the date a court of the United States cancels his certificate of naturalization. If any individual is described in more than one of the above categories, the individual is treated as having relinquished his citizenship on the earliest of the applicable dates.

The Committee anticipates that an individual who has either renounced his citizenship or furnished a signed statement of voluntary relinquishment but has not received a certificate of loss of nationality from the Department of State by the date on which he is required to file a tax return covering the year of expatriation will file his U.S. tax return as if he expatriated. The Committee further anticipates that such an individual will amend his return for that year in the event that the Department of State fails to confirm the expatriation by issuing a certificate of loss of nationality.

Administrative requirements

Under the bill, an individual who is subject to the tax on expatriation is required to pay a tentative tax equal to the amount of

tax that would have been due based on a hypothetical short tax year that ended on the date the individual relinquished his citizenship.[31] The tentative tax is due on the 90th day after the date of relinquishment. The Committee expects that Treasury regulations (under the authority of sec. 6011) will require that the expatriate file a tax return at such time. The individual also is required to file a full-year tax return for the tax year during which he expatriated reporting all of his taxable income for the year, including gain attributable to the deemed sale of assets on the date of expatriation. The individual's U.S. Federal income tax liability for such year will be reduced by the tentative tax paid with the filing of the hypothetical short-year return.

The bill provides that the time for the payment of the tax on expatriation may be extended for a period not to exceed 10 years at the request of the taxpayer, as provided by section 6161. The Committee expects that a taxpayer's interest in non-liquid assets such as an interest in a closely-held business interest (as defined in sec. 6166(b)) will be taken into account in determining reasonable cause for the extension of time to pay the tax on expatriation.

In the event that the expatriating individual and the Treasury Department agree to defer payment of the tax on expatriation for a period that extends beyond the filing date for the full-year tax return for the year of expatriation, the bill provides that the individual would not be required to pay a tentative tax. The entire gain on the deemed sale of property on the date of expatriation would be included in the individual's full-year tax return for that year, and would be paid in accordance with the provisions of the deferred-tax agreement under section 6161. The Committee expects that the Treasury Department will not agree to defer payment of the tax on expatriation unless the taxpayer provides adequate assurance that all amounts due under the agreement will be paid.

The Committee expects that the Department of State will notify the IRS of the name and taxpayer identification number of any U.S. citizen who relinquishes U.S. citizenship promptly after the date of relinquishment, as defined in the provision.[32] In addition, the Committee anticipates that the Department of State will request of any expatriating citizen, at the time of relinquishment of citizenship, appropriate information to assist the IRS in enforcing the requirements of the provision.

Other special rules

As noted above, the tax on expatriation applies generally notwithstanding other provisions of the Code. For example, gain that would be eligible for nonrecognition treatment if the property were actually sold is treated as recognized for purposes of the tax on expatriation. In addition, for example, bona fide residence in a U.S. possession or commonwealth does not affect the application of the

[31] Thus, the tentative tax is based on all the income, gain, deductions, loss and credits of the individual for the year through the date of relinquishment, including amounts realized from the deemed sale of property. The tentative tax is treated as imposed immediately before the individual relinquishes citizenship.

[32] That is, without waiting for the issuance of a certificate of loss of nationality.

expatriation tax.[33] However, the bill provides that the portions of the gain treated as realized under the provisions of the expatriation tax are not recognized to the extent they are treated as excluded under the specific income exclusions of sections 101–137 (Subtitle A, Chapter 1B, Part III) of the Code.

Other special rules of the Code may affect the characterization of amounts treated as realized under the expatriation tax. For example, in the case of stock in a foreign corporation that was a controlled foreign corporation at any time during the five-year period ending on the date of the deemed sale, the gain recognized on the deemed sale is included in the shareholder's income as a dividend to the extent of certain earnings of the foreign corporation (see sec. 1248).

The bill provides that any period during which recognition of income or gain is deferred will terminate on the date of the relinquishment, causing any deferred U.S. tax to be due and payable at the time specified by the Treasury Department. For example, where an individual has disposed of certain property (e.g., property that qualifies for like-kind exchange under sec. 1031 or as a principal residence under sec. 1034) but has not yet acquired replacement property, the relevant period to acquire any replacement property is deemed to terminate and the individual is taxed on the gain from the original sale.

The bill authorizes the Treasury Department to issue regulations to permit a taxpayer to allocate the taxable gain (net of any applicable exclusion) to the basis of assets taxed under this provision, thereby preventing double taxation if the assets remain subject to U.S. tax jurisdiction.

Effective Date

The provision is effective for U.S. citizens who relinquish their U.S. citizenship (as determined under the bill) on or after February 6, 1995. The tentative tax will not be required to be paid until 90 days after the date of enactment of the bill.

Present law will continue to apply to U.S. citizens who relinquished their citizenship prior to February 6, 1995.

IV. BUDGET EFFECTS

A. COMMITTEE ESTIMATES

In compliance with paragraph 11(a) of rule XXVI of the Standing Rules of the Senate, the following statement is made concerning the estimated budget effects of the bill (H.R. 831) as amended and reported by the Committee on Finance.

The bill as amended is estimated to have the following effects on budget receipts and outlays for fiscal years 1995–2000:

[33] Because there is no meaningful concept of citizenship of a U.S. territory or possession, the Committee intends that the provision not be "mirrored" for application in the U.S. territories and possessions that employ the mirror code.

ESTIMATED REVENUE EFFECTS OF H.R. 831 AS REPORTED BY THE SENATE FINANCE COMMITTEE

[By fiscal years, in millions of dollars]

Provision	Effective	1995	1996	1997	1998	1999	2000	1995–00	2001–05	1995–05
1. Extend self-employed health deduction: 25% for 1994 and 30% thereafter	12/31/93	−514	−482	−527	−587	−649	−708	−3,467	−4,520	−7,987
2. Repeal section 1071 (FCC tax certificate program)	1/17/95	334	411	135	135	170	201	1,386	1,465	2,849
3. Modify section 1033 for corporations with transition rule for microwave relocation previously entitled to section 1071 (non-recognition of gain on involuntary conversions not to apply to acquisitions from related persons).	2/6/95	5	9	23	33	47	67	184	689	873
4. Deny earned income tax credit to individuals with interest, dividends, tax-exempt interest income and net rental and royalty income over $2,450 (the $2,450 threshold is not indexed for inflation)[1].	1/1/96	....	21	415	465	501	540	1,941	3,372	5,313
5. Revise tax treatment of renouncers of citizenship[2]	2/6/95	47	144	197	257	322	392	1,359	2,274	3,633
Net totals		−128	103	243	303	391	492	1,403	3,280	4,681

[1] Included in this estimate are decreases in EITC outlays of $17 million for FY 1996, $334 million for FY 1997, $375 million for FY 1998, $409 million for FY 1999, $439 million for FY 2000, $468 million for FY 2001, $504 million for FY 2002, $540 million for FY 2003, $579 million for FY 2004, and $622 million for FY 2005.

[2] Modified version of Administration's revenue proposal.

Note.—Details may not add to total due to rounding.

Source: Joint Committee on Taxation.

B. BUDGET AUTHORITY AND TAX EXPENDITURES

Budget authority

In compliance with Section 308(a)(1) of the Budget Act, the Committee states that the bill as reported involves decreased budget authority (reduction in outlays) for the reduction in the refundable portion of the earned income tax credit attributable to the change in eligibility relating to certain unearned income (amounts are shown above in the table in Part IV.A).

Tax expenditures

In compliance with Section 308(a)(2) of the Budget Act, the Committee states that the revenue reduction attributable to the extension of the deduction for health insurance costs for self-employed individuals involves increased tax expenditures, and that the revenue-increasing provisions of the bill involve a reduction in tax expenditures (amounts are shown above in the table in IV.A).

C. CONSULTATION WITH CONGRESSIONAL BUDGET OFFICE

In accordance with Section 403 of the Budget Act, the Committee advises that the Congressional Budget Office has reviewed the Committee's budget estimates. The Congressional Budget Office submitted the following statement:

U.S. CONGRESS,
CONGRESSIONAL BUDGET OFFICE,
Washington, DC, March 17, 1995.

Hon. BOB PACKWOOD,
Chairman, Committee on Finance,
U.S. Senate, Washington, DC.

DEAR MR. CHAIRMAN: The Congressional Budget Office and the Joint Committee on Taxation (JCT) have reviewed H.R. 831, as ordered reported by the Senate Committee on Finance on March 15, 1995. The JCT estimates that this bill would increase the deficit by $0.128 billion in fiscal year 1995 and decrease the deficit by $1.404 billion over fiscal years 1995 through 2000.

H.R. 831 would restore the 25 percent deduction for health insurance costs of self-employed individuals for 1994, and would increase it permanently to 30 percent thereafter. The 25 percent deduction expired after December 31, 1993.

The bill includes several provisions to offset the revenue loss from extending the deduction. First, H.R. 831 would repeal the provision of the Internal Revenue Code that permits nonrecognition of gain on sales and exchanges effectuating policies of the Federal Communications Commission and would prohibit nonrecognition of gain on involuntary conversions in certain related-party transactions. Also, the bill would deny the earned income tax credit (EITC) to individuals with interest, dividends, tax-exempt interest income and net rental and royalty income over $2,450. Finally, H.R. 831 should revise the tax treatment of individuals who renounce their citizenship. The budget effects of the bill are shown below:

BUDGET EFFECTS OF H.R. 831

[By fiscal years, in billions of dollars]

	1995	1996	1997	1998	1999	2000
Revenues:						
Projected revenues under current law	1355.213	1417.720	1475.496	1546.405	1618.306	1697.488
Proposed changes	−0.128	0.086	−0.091	−0.072	−0.018	0.053
Projected revenues under H.R. 831	1355.085	1417.806	1475.405	1546.333	1618.288	1697.541
Outlays:						
Projected EITC outlays under current law	17.260	20.392	22.904	23.880	24.938	25.982
Proposed changes	0	−0.017	−0.334	−0.375	−0.409	−0.439
Projected EITC outlays under H.R. 831	17.260	20.375	22.570	23.505	24.529	25.543

Section 252 of the Balanced Budget and Emergency Deficit Control Act of 1985 sets up pay-as-you-go procedures for legislation affecting receipts or direct spending through 1998. Because H.R. 831 would affect receipts, pay-as-you-go procedures would apply to the bill. These effects are summarized in the table below:

PAY-AS-YOU-GO CONSIDERATIONS

[By fiscal years, in billions of dollars]

	1995	1996	1997	1998
Changes in receipts	−0.128	0.086	−0.091	−0.072
Changes in outlays	0	−0.017	−0.334	−0.375

If you wish further details, please feel free to contact me or your staff may wish to contact Melissa Sampson.

Sincerely,

JAMES L. BLUM
(For June E. O'Neill, Director).

V. VOTES OF THE COMMITTEE

In compliance with paragraph 7(b) of rule XXVI of the Standing Rules of the Senate, the following is a tabulation of the votes taken during Committee markup of the bill (H.R. 831).

Motion to report the bill as amended

The bill (H.R. 831), as amended, was ordered favorably reported by a voice vote (13 Members were present for this voice vote).

Votes on amendments

The Committee approved a motion (12 yeas and 8 nays) by Senator Roth to (1) repeal Code section 1071, effective January 17, 1995 (as provided in the Chairman's mark), (2) modify the EITC, and (3) use the savings to increase the deduction for health insurance costs for self-employed individuals to 30 percent beginning in 1995. (This amendment was a second-degree substitute for an original amendment by Senator Moynihan, which would have (1) made the repeal of Code section 1071 effective on or after March 15, 1995, with exceptions for investors contributing start-up financing to a minority enterprise before March 15, 1995, (2) applied the section 1033 change effective for involuntary conversions occurring on or after March 15, 1995, and (3) set the limit on unearned income for EITC eligibility at $2,450.

Yeas—Packwood, Dole (proxy), Roth, Chafee, Grassley, Hatch, Simpson (proxy), Pressler (proxy), D'Amato, Murkowski, Nickles, Bradley.

Nays—Moynihan, Baucus, Pryor, Rockefeller (proxy) Breaux, Conrad, Graham, Moseley-Braun.

The Committee defeated a motion (9 yeas and 11 nays) by Senator Moynihan to: (1) strike repeal of section 1071 and provide for a 2-year moratorium on Code section 1071; (2) add a provision to preclude tax avoidance through renunciation of U.S. citizenship; (3) increase the self-employed health deduction to 30 percent in 1995 and thereafter; (4) permit the State of New York to continue operating inpatient hospital reimbursement system; (5) exempt from excise tax diesel dyeing rules those States exempt from the Clean Air Act diesel dyeing rules under EPA regulations; (6) provide special rules for marina operators that sell and recreational boaters who buy dyed diesel fuel; (7) apply the section 1033 change effective for involuntary conversions occurring on or after March 15, 1995; and (8) set the limit on unearned income for EITC eligibility at $2,450. The roll call vote was as follows:

Yeas—Moynihan, Baucus, Bradley, Pryor, Rockefeller (proxy), Breaux, Conrad, Graham, Moseley-Braun.

Nays—Packwood, Dole (proxy), Roth, Chafee, Grassley, Hatch, Simpson (proxy), Pressler (proxy), D'Amato, Murkowski, Nickles.

The Committee defeated a motion (10 yeas and 10 nays) by Senator Bradley to limit the deduction for health insurance costs for self-employed individuals to 25 percent and to use the savings for deficit reduction. The roll call vote was as follows:

Yeas—Packwood, Chafee, Simpson, Moynihan, Bradley, Rockefeller (proxy), Breaux, Conrad, Graham, Moseley-Braun.

Nays—Dole (proxy), Roth, Grassley, Hatch, Pressler, D'Amato, Murkowski, Nickles, Baucus, Pryor.

The Committee defeated a second-degree substitute motion (7 yeas and 13 nays) by Senator Moseley-Braun to the above Bradley amendment. The Moseley-Braun amendment would delete the retroactive dates in the previous Roth amendment, and make the dates prospective. The roll call vote was as follows:

Yeas—Moynihan, Pryor, Rockefeller (proxy), Breaux, Conrad, Graham, Moseley-Braun.

Nays—Packwood, Dole (proxy), Roth, Chafee, Grassley, Hatch (proxy), Simpson (proxy), Pressler (proxy), D'Amato (proxy), Murkowski (proxy), Nickles (proxy), Baucus, Bradley.

The Committee approved a motion (voice vote) by Senator Bradley (cosponsored by Senators Conrad and Moseley-Braun) to (1) impose a tax on people who relinquish their U.S. citizenship and (2) use the revenues for deficit reduction (13 Members were present for this voice vote.)

VI. REGULATORY IMPACT

Pursuant to paragraph 11(b) of rule XXVI of the Standing Rules of the Senate, the Committee makes the following statement concerning the regulatory impact that might be incurred in carrying out the bill (H.R. 831) as reported.

Impact on individuals and businesses

Section 1 of the bill as reported reinstates the 25-percent deduction for health insurance costs for self-employed individuals for 1994 and permanently extends the deduction at 30 percent for 1995 and thereafter. Expeditious enactment of this provision will allow self-employed individuals to be able to file their 1994 income tax returns with certainty concerning the deduction and not have to file amended tax returns.

Section 2 of the bill as reported repeals Code section 1071 (relating to nonrecognition of gain on certain broadcast properties under the FCC tax certificate program), generally effective for sales or exchanges on or after January 17, 1995, and for sales or exchanges before that date if the FCC tax certificate with respect to the sale or exchanges is issued on or after that date. Thus, a sale or exchange of broadcast properties is subject to the same general tax rules applicable to other taxpayers engaged in the sale or exchange of a business.

Section 3 of the bill as reported modifies Code section 1033 to provide that, in the case of a C corporation, deferral of gain is not available when replacement property or stock is purchased from a related party, effective for involuntary conversions occurring on or after February 6, 1995. Also, the bill provides that sales or exchanges involving microwave relocation transactions that are certified by the FCC as having been made in connection with the relocation of the taxpayer from the 1850–1990MHz spectrum by reason of the FCC's reallocation of that spectrum for use for personal communications services (PCS) will be treated as involuntary conversions under section 1033. The microwave relocation provision applies to sales or exchanges occurring before January 1, 2000.

Section 4 of the bill as reported denies the earned income tax credit (EITC) to taxpayers if the aggregate amount of interest income (taxable and exempt), dividend income, net rental income and royalties exceeds $2,450 for taxable years beginning after 1995.

Section 5 of the bill as reported provides that U.S. citizens who relinquish their citizenship will be required to recognize, and pay income tax on, unrealized and deferred gains with respect to property held immediately prior to the expatriation. The provision is effective for U.S. citizens relinquishing citizenship on or after February 6, 1995.

Impact on personal privacy and paperwork

Section 4 of the bill as reported will involve an additional calculation by taxpayers who may be eligible for the EITC to determine if they are subject to the $2,450 limit on unearned income.

Section 5 of the bill as reported will involve increased reporting of information to the Federal Government for U.S. citizens who relinquish their citizenship and the filing of additional tax forms to comply with the provision.

VII. CHANGES IN EXISTING LAW MADE BY THE BILL

In the opinion of the Committee, it is necessary in order to expedite the business of the Senate, to dispense with the requirements of paragraph 12 of rule XXVI of the Standing Rules of the Senate

(relating to the showing of changes in existing law made by the provision of H.R. 831 as reported by the Committee).

VIII. ADDITIONAL VIEWS

ADDITIONAL VIEWS OF SENATORS MOYNIHAN AND MOSELEY-BRAUN

During the Finance Committee's consideration of H.R. 831, Senator Moynihan offered amendments that would have eliminated the retroactive repeal of Internal Revenue Code section 1071 from the bill. Section 1071 authorizes the Federal Communications Commission to provide tax deferral to sellers of broadcast properties when such sales effectuate FCC policies, including sales to minority purchasers to foster program diversity. The Chairman's mark proposed to use the revenue generated from retroactive repeal of section 1071 to pay for the permanent extension of the 25 percent deduction for health insurance costs of the self-employed.

Senator Moynihan's amendment proposed instead an alternative source to raise the same revenue: a proposal from the Administration's Fiscal Year 1996 Budget designed to prevent tax avoidance by U.S. citizens who renounce their citizenship. This amendment accomplished the primary objective of H.R. 831, that is, to act expeditiously on the 25 percent health insurance deduction for the self-employed prior to the filing deadline for the 1994 tax year. Retroactive repeal of section 1071 was not necessary to accomplish this objective. With modest changes to the earned income tax credit (EITC) provision in the Chairman's mark, the amendment provided sufficient revenue to allow a permanent extension of the self-employed health insurance deduction at an increased level of 30 percent.

Valid questions have been raised about the way that section 1071 is currently being administered. Recognizing this fact, the amendment would have provided a moratorium of up to two years on the provision. The Administration is undertaking a comprehensive review of all federal affirmative action programs. The moratorium would provide adequate time for the Congress to review section 1071 and affirmative action policies generally, consider the Administration's recommendations and develop a reform proposal. During the moratorium period, no FCC tax certificates would be issued and applications for tax certificates would not be processed by the FCC. Section 1071 was enacted more than 50 years ago, in 1943, and its application to sales to minority purchasers has been in place for 17 years, since 1978. It is only reasonable to expend more than a few weeks when making significant changes to the provision. The necessity of acting quickly on the extension of the self-employed health insurance deduction precludes that kind of deliberation.

The amendment would also have eliminated the retroactive aspect of the repeal of section 1071. The Committee is aware of at least 19 transactions that were negotiated in reliance on the exist-

ence of section 1071 and had FCC tax certificate applications pending at the time the House voted to retroactively repeal the provision. In many of these cases, the parties had signed definitive purchase agreements (subject only to issuance of an FCC tax certificate), filed applications for FCC tax certificates, and expended hundreds of thousands (in some cases, millions) of dollars in negotiation costs. All done in reliance on an FCC policy that had been in place for 17 years and had been expressly reaffirmed by Congress in each annual appropriations bill for the FCC since 1987, most recently in appropriations legislation passed in August 1994. In the case of the sale of certain cable TV systems by Viacom, a transaction that has received much press attention, we are advised that negotiations with the buyer had commenced in July 1994, more than 6 months before there was any indication that section 1071 might be modified. The Chairman of the Ways & Means Committee announced in a press release on January 17, 1995 that section 1071 might be modified, and that any changes later decided on by the Ways & Means Committee would be retroactive to the date of the press release. By the time of the press release, we are advised that the parties to the Viacom transaction had expended more than $15 million in negotiation costs, and that the definitive terms of the $2.3 billion transaction had been settled—which is amply evidenced by the signing of the agreement on January 20, 1995, a mere three days after the release. Eighteen other transactions were proceeding in similar reliance on the law in effect on January 17—at least that is the number of which we are currently aware.

Businesses cannot plan, cannot negotiate, and cannot compete on a fair basis under the threat of this kind of retroactive reversal of the law. The critical issues are adequate notice and justified reliance. We believe that the affected parties justifiably relied on the law in effect when they entered into their transactions, and that the notice they received was not adequate. This kind of retroactive legislating should not be done.

In addition to paying for an extension of the self-employed health insurance deduction without resort to a retroactive repeal of section 1071, the amendment contained two additional time sensitive provisions.

First, the amendment included a measure providing that the diesel fuel dyeing requirements for tax administration purposes, enacted in 1993, would not apply in any State that is exempted from the fuel dyeing requirements of the Clean Air Act. Alaska currently has such an exemption, due to the fact that over 90 percent of the diesel fuel used in that state is used off-road and not subject to the Clean Air Act requirements. Similarly, over 90 percent of the diesel fuel used in Alaska is used for nontaxable purposes. Conforming the fuel dyeing rules for environmental and tax purposes is justified, and needs to be accomplished expeditiously. In addition, the amendment would have permitted the use of dyed diesel fuel for recreational boating purposes during calendar year 1995, so long as the diesel tax is collected at the retail level.

Second, the amendment contained another provision of a time-sensitive nature related to health care. The amendment would have permitted the State of New York to continue operating an inpatient hospital reimbursement system that has been in place since

1983. The reimbursement system, in which all payers except Medicare participate, provides substantial support to hospitals for the cost of care to the uninsured by imposing a surcharge on each inpatient hospital bill. This reimbursement system is being challenged in the Federal courts as impermissible state regulation of employer group health plans. A statutory provision covering this reimbursement system was added by Senator Moynihan to the Omnibus Budget Reconciliation Act of 1993, but will expire on May 12 of this year. The amendment would have provided an exemption for the reimbursement system through 1996.

In summary, the Moynihan amendments addressed the time-sensitive need to extend the self-employed health insurance deduction in advance of the 1994 tax filing deadline without embroiling that issue in the twin controversies of precipitous repeal of the minority broadcast tax preference program or of retroactive tax provisions. We regret that it did not pass.

DANIEL PATRICK MOYNIHAN.
CAROL MOSELEY-BRAUN.