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## ECONOMIC RECOVERY TAX ACT OF 1981

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AUGUST 1 (legislative day, JULY 8), 1981.—Ordered to be printed

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Mr. DOLE, from the committee of conference,  
submitted the following

### CONFERENCE REPORT

[To accompany H.R. 4242]

The committee of conference on the disagreeing votes of the two Houses on the amendment of the Senate to the bill (H.R. 4242) to amend the Internal Revenue Code of 1954 to encourage economic growth through reductions in individual income tax rates, the expensing of depreciable property, incentives for small businesses, and incentives for savings, and for other purposes, having met, after full and free conference, have agreed to recommend and do recommend to their respective Houses as follows:

That the House recede from its disagreement to the amendment of the Senate and agree to the same with an amendment as follows:

In lieu of the matter proposed to be inserted by the Senate amendment insert the following:

#### **SECTION 1. SHORT TITLE; TABLE OF CONTENTS; AMENDMENT OF 1954 CODE.**

(a) **SHORT TITLE.**—*This Act may be cited as the “Economic Recovery Tax Act of 1981”.*

(b) **TABLE OF CONTENTS.**—

*Sec. 1. Short title; table of contents; amendment of 1954 Code.*

#### **TITLE I—INDIVIDUAL INCOME TAX PROVISIONS**

##### **Subtitle A—Tax Reductions**

*Sec. 101. Rate cuts; rate reduction credit.*

*Sec. 102. 20-percent maximum rate on net capital gain for portion of 1981, decrease in holding period.*

*Sec. 103. Deduction for two-earner married couples.*

*Sec. 104. Adjustment to prevent inflation-caused tax increase.*

### Subtitle B—Income Earned Abroad

- Sec. 111. *Partial exclusion for earned income from sources without the United States and foreign housing costs.*
- Sec. 112. *Repeal of deduction for certain expenses of living abroad.*
- Sec. 113. *Employees living in camps.*
- Sec. 114. *Reports by Secretary.*
- Sec. 115. *Effective date.*

### Subtitle C—Miscellaneous Provisions

- Sec. 121. *Deduction for charitable contributions to be allowed for individuals who do not itemize deductions.*
- Sec. 122. *18-month period for rollover principal residence increased to 2 years.*
- Sec. 123. *One-time exclusion of gain increased to 2 years.*
- Sec. 124. *Increases in credit allowable for expenses for household and dependent care services necessary for gainful employment.*
- Sec. 125. *Deduction for adoption expenses paid by an individual.*
- Sec. 126. *Maximum rate of imputed interest for sale of land between related persons.*
- Sec. 127. *State legislators travel expenses away from home.*
- Sec. 128. *Rates of tax for principal campaign committees.*

## TITLE II—BUSINESS INCENTIVE PROVISIONS

### Subtitle A—Cost Recovery Provisions

- Sec. 201. *Accelerated cost recovery system.*
- Sec. 202. *Election to expense certain depreciable business assets.*
- Sec. 203. *Amendments related to depreciation.*
- Sec. 204. *Recapture on disposition of recovery property.*
- Sec. 205. *Minimum tax treatment.*
- Sec. 206. *Earnings and profits.*
- Sec. 207. *Extension of carryover period for net operating losses and certain credits.*
- Sec. 208. *Carryover of recovery attribute in section 381 transactions.*
- Sec. 209. *Effective dates.*

### Subtitle B—Investment Tax Credit Provisions

- Sec. 211. *Modification of investment tax credit to reflect accelerated cost recovery.*
- Sec. 212. *Increase in investment tax credit for qualified rehabilitation expenditures.*
- Sec. 213. *Investment credit for used property; increase in dollar limit.*
- Sec. 214. *Investment tax credit allowed for certain rehabilitated buildings leased to tax-exempt organizations or to governmental units.*

### Subtitle C—Incentives for Research and Experimentation

- Sec. 221. *Credit for increasing research activities.*
- Sec. 222. *Charitable contributions of scientific property used for research.*
- Sec. 223. *Suspension of regulations relating to allocation under section 861 of research and experimental expenditures.*

### Subtitle D—Small Business Provisions

- Sec. 231. *Reduction in corporate rate tax.*
- Sec. 232. *Increase in accumulated earnings credit.*
- Sec. 233. *Subchapter S shareholders.*
- Sec. 234. *Treatment of trusts as subchapter S shareholders.*
- Sec. 235. *Simplification of LIFO by use of Government indexes to be provided by regulations.*
- Sec. 236. *Three-year averaging permitted for increases in inventory value.*
- Sec. 237. *Election by small business to use one inventory pool when LIFO is elected.*

### Subtitle E—Savings and Loan Associations

- Sec. 241. *Reorganizations involving financially troubled thrift institutions.*
- Sec. 242. *Limitations on carryovers of financial institutions.*
- Sec. 243. *Reserves for losses on loans.*
- Sec. 244. *FSLIC financial assistance.*
- Sec. 245. *Mutual savings banks with capital stock.*
- Sec. 246. *Effective dates.*

*Subtitle F—Stock Options, Etc.*

- Sec. 251. Stock options.*  
*Sec. 252. Property transferred to employees subject to certain restrictions.*

*Subtitle G—Miscellaneous Provisions*

- Sec. 261. Adjustments to new jobs credit.*  
*Sec. 262. Section 189 made inapplicable to low-income housing.*  
*Sec. 263. Increase in deduction allowable to a corporation in any taxable year for charitable contributions.*  
*Sec. 264. Amortization of low-income housing.*  
*Sec. 265. Deductibility of gifts by employers to employees.*  
*Sec. 266. Deduction for motor carrier operating authority.*  
*Sec. 267. Limitation on additions to bank loss reserves.*

**TITLE III—SAVINGS PROVISIONS***Subtitle A—Interest Exclusion*

- Sec. 301. Exclusion of interest on certain savings certificates.*  
*Sec. 302. Partial exclusion of interest.*

*Subtitle B—Retirement Savings Provisions*

- Sec. 311. Retirement savings.*  
*Sec. 312. Increase in amount of self-employed retirement plan deduction.*  
*Sec. 313. Rollovers under bond purchase plans.*  
*Sec. 314. Miscellaneous provisions.*

*Subtitle C—Reinvestment of Dividends in Public Utilities*

- Sec. 321. Encouragement of reinvestment of dividends in the stock of public utilities.*

*Subtitle D—Employee Stock Ownership Provisions*

- Sec. 331. Payroll-based credit for establishing employee stock ownership plan.*  
*Sec. 332. Termination of the portion of the investment credit attributable to employee plan percentage.*  
*Sec. 333. Tax treatment of contributions attributable to principal and interest payments in connection with an employee stock ownership plan.*  
*Sec. 334. Cash distributions from an employee stock ownership plan.*  
*Sec. 335. Put option for stock bonus plans.*  
*Sec. 336. Put option requirements for banks; put option period.*  
*Sec. 337. Distribution of employer securities from a tax credit employee stock ownership plan in the case of a sale of employer assets or stock.*  
*Sec. 338. Pass through of voting rights on employer securities.*  
*Sec. 339. Effective date.*

**TITLE IV—ESTATE AND GIFT TAX PROVISIONS***Subtitle A—Increase in Unified Credit; Rate Reduction; Unlimited Marital Deduction*

- Sec. 401. Increase in unified credit.*  
*Sec. 402. Reduction in maximum rates of tax.*  
*Sec. 403. Unlimited marital deduction.*

*Subtitle B—Other Estate Tax Provisions*

- Sec. 421. Valuation of certain farm, etc., real property.*  
*Sec. 422. Coordination of extensions of time for payment of estate tax where estate consists largely of interest in closely held business.*  
*Sec. 423. Treatment of certain contributions of works of art, etc.*  
*Sec. 424. Gifts made within 3 years of decedent's death not included in gross estate.*  
*Sec. 425. Basis of certain appreciated property transferred to decedent by gift within one year of death.*  
*Sec. 426. Disclaimers.*  
*Sec. 427. Repeal of deduction for bequests, etc., to certain minor children.*  
*Sec. 428. Postponement of generation-skipping tax effective date.*  
*Sec. 429. Credit against estate tax for transfer to Smithsonian.*

*Subtitle C—Other Gift Tax Provisions*

- Sec. 441. Increase in annual gift tax exclusion; unlimited exclusion for certain transfers.*  
*Sec. 442. Time for payment of gift taxes.*

**TITLE V—TAX STRADDLES**

- Sec. 501. Postponement of recognition of losses, etc.*  
*Sec. 502. Capitalization of certain interest and carrying charges in the case of straddles.*  
*Sec. 503. Regulated futures contracts marked to market.*  
*Sec. 504. Carryback of losses from regulated futures contracts to offset prior gains from such contracts.*  
*Sec. 505. Certain governmental obligations issued at discount treated as capital assets.*  
*Sec. 506. Prompt identification of securities by dealers in securities.*  
*Sec. 507. Treatment of gain or loss from certain terminations.*  
*Sec. 508. Effective dates.*  
*Sec. 509. Election for extension of time for payment and application of section 1256 for the taxable year including June 23, 1981.*

**TITLE VI—ENERGY PROVISIONS**

*Subtitle A—Changes in Windfall Profit Tax*

- Sec. 601. \$22,500 royalty credit for 1981; exemption for 1982 and thereafter.*  
*Sec. 602. Reduction in tax imposed on newly discovered oil.*  
*Sec. 603. Exempt independent producer stripper well oil.*  
*Sec. 604. Exemption from windfall profit tax of oil produced from interests held by or for the benefit of residential child care agencies.*

*Subtitle B—Miscellaneous Provision*

- Sec. 611. Application of credit for producing natural gas from a nonconventional source with the Natural Gas Policy Act of 1978.*

**TITLE VII—ADMINISTRATIVE PROVISIONS**

*Subtitle A—Prohibition of Disclosure of Audit Methods*

- Sec. 701. Prohibition of disclosure of methods for selection of tax returns for audits.*

*Subtitle B—Changes in Interest Rate for Overpayments and Underpayments*

- Sec. 711. Changes in rate of interest for overpayments and underpayments.*

*Subtitle C—Changes in Certain Penalties and in Requirements Relating to Returns*

- Sec. 721. Changes in penalties for false information with respect to withholding.*  
*Sec. 722. Additions to tax in the case of valuation overstatements, increase in negligence penalty.*  
*Sec. 723. Changes in requirements relating to information returns.*  
*Sec. 724. Penalty for overstated deposit claims.*  
*Sec. 725. Declaration of estimated tax not required in certain cases.*

*Subtitle D—Cash Management*

- Sec. 731. Cash management.*

*Subtitle E—Financing of Railroad Retirement System.*

- Sec. 741. Increases in employer and employee taxes.*  
*Sec. 742. Advance transfer of amounts payable under social security financial interchange.*  
*Sec. 743. Amendments to section 3231 clarifying definition of compensation.*

*Subtitle F—Filing Fees*

- Sec. 751. Fees for filing petitions.*

**TITLE VIII—MISCELLANEOUS PROVISIONS**

**Subtitle A—Extensions**

*Sec. 801. Fringe benefits.*

*Sec. 802. Exclusion for prepaid legal services 3 years.*

**Subtitle B—Tax-Exemption Obligations**

*Sec. 811. Tax-exempt financing for vehicles used for mass commuting.*

*Sec. 812. Obligations of certain volunteer fire departments.*

**Subtitle C—Excise Taxes**

*Sec. 821. Extension of telephone excise tax.*

*Sec. 822. Exclusion of certain services from Federal Unemployment Tax Act.*

*Sec. 823. Private foundation distributions.*

*(c) AMENDMENT OF 1954 CODE.—Except as otherwise expressly provided, whenever in this Act an amendment or repeal is expressed in terms of an amendment to, or repeal of, a section or other provision, the reference shall be considered to be made to a section or other provision of the Internal Revenue Code of 1954.*

**TITLE I—INDIVIDUAL INCOME TAX PROVISIONS**

**Subtitle A—Tax Reductions**

**SEC. 101. RATE CUTS; RATE REDUCTION CREDIT.**

*(a) RATE REDUCTION.—Section 1 (relating to tax imposed) is amended to read as follows:*

**“SECTION 1. TAX IMPOSED.**

*“(a) MARRIED INDIVIDUALS FILING JOINT RETURNS AND SURVIVING SPOUSES.—There is hereby imposed on the taxable income of every married individual (as defined in section 143) who makes a single return jointly with his spouse under section 6013, and every surviving spouse (as defined in section 2(a)), a tax determined in accordance with the following tables:*

*“(1) FOR TAXABLE YEARS BEGINNING IN 1982.—*

<i>“If taxable income is:</i>	<i>The tax is:</i>
<i>Not over \$3,400 .....</i>	<i>No tax.</i>
<i>Over \$3,400 but not over \$5,500 .....</i>	<i>12% of the excess over \$3,400.</i>
<i>Over \$5,500 but not over \$7,600 .....</i>	<i>\$252, plus 14% of the excess over \$5,500.</i>
<i>Over \$7,600 but not over \$11,900 .....</i>	<i>\$546, plus 16% of the excess over \$7,600.</i>
<i>Over \$11,900 but not over \$16,000 .....</i>	<i>\$1,234, plus 19% of the excess over \$11,900.</i>
<i>Over \$16,000 but not over \$20,200 .....</i>	<i>\$2,013, plus 22% of the excess over \$16,000.</i>
<i>Over \$20,200 but not over \$24,600 .....</i>	<i>\$2,937, plus 25% of the excess over \$20,200.</i>
<i>Over \$24,600 but not over \$29,900 .....</i>	<i>\$4,037, plus 29% of the excess over \$24,600.</i>
<i>Over \$29,900 but not over \$35,200 .....</i>	<i>\$5,574, plus 33% of the excess over \$29,900.</i>
<i>Over \$35,200 but not over \$45,800 .....</i>	<i>\$7,323, plus 39% of the excess over \$35,200.</i>
<i>Over \$45,800 but not over \$60,000 .....</i>	<i>\$11,457, plus 44% of the excess over \$45,800.</i>
<i>Over \$60,000 but not over \$85,600 .....</i>	<i>\$17,705, plus 49% of the excess over \$60,000.</i>

<b>"If taxable income is:</b>	<b>The tax is:</b>
Over \$85,600.....	\$30,249, plus 50% of the excess over \$85,600.

**"(2) FOR TAXABLE YEARS BEGINNING IN 1983.—**

<b>"If taxable income is:</b>	<b>The tax is:</b>
Not over \$3,400.....	No tax.
Over \$3,400 but not over \$5,500.....	11% of the excess over \$3,400.
Over \$5,500 but not over \$7,600.....	\$231, plus 13% of the excess over \$5,500.
Over \$7,600 but not over \$11,900.....	\$504, plus 15% of the excess over \$7,600.
Over \$11,900 but not over \$16,000.....	\$1,149, plus 17% of the excess over \$11,900.
Over \$16,000 but not over \$20,200.....	\$1,846, plus 19% of the excess over \$16,000.
Over \$20,200 but not over \$24,600.....	\$2,644, plus 23% of the excess over \$20,200.
Over \$24,600 but not over \$29,900.....	\$3,656, plus 26% of the excess over \$24,600.
Over \$29,900 but not over \$35,200.....	\$5,034, plus 30% of the excess over \$29,900.
Over \$35,200 but not over \$45,800.....	\$6,624, plus 35% of the excess over \$35,200.
Over \$45,800 but not over \$60,000.....	\$10,334, plus 40% of the excess over \$45,800.
Over \$60,000 but not over \$85,600.....	\$16,014, plus 44% of the excess over \$60,000.
Over \$85,600 but not over \$109,400.....	\$27,278, plus 48% of the excess over \$85,600.
Over \$109,400.....	\$38,702, plus 50% of the excess over \$109,400.

**"(3) FOR TAXABLE YEARS BEGINNING AFTER 1983.—**

<b>"If taxable income is:</b>	<b>The tax is:</b>
Not over \$3,400.....	No tax.
Over \$3,400 but not over \$5,500.....	11% of the excess over \$3,400.
Over \$5,500 but not over \$7,600.....	\$231, plus 12% of the excess over \$5,500.
Over \$7,600 but not over \$11,900.....	\$483, plus 14% of the excess over \$7,600.
Over \$11,900 but not over \$16,000.....	\$1,085, plus 16% of the excess over \$11,900.
Over \$16,000 but not over \$20,200.....	\$1,741, plus 18% of the excess over \$16,000.
Over \$20,200 but not over \$24,600.....	\$2,497, plus 22% of the excess over \$20,200.
Over \$24,600 but not over \$29,900.....	\$3,465, plus 25% of the excess over \$24,600.
Over \$29,900 but not over \$35,200.....	\$4,790, plus 28% of the excess over \$29,900.
Over \$35,200 but not over \$45,800.....	\$6,274, plus 33% of the excess over \$35,200.
Over \$45,800 but not over \$60,000.....	\$9,772, plus 38% of the excess over \$45,800.
Over \$60,000 but not over \$85,600.....	\$15,168, plus 42% of the excess over \$60,000.
Over \$85,600 but not over \$109,400.....	\$25,920, plus 45% of the excess over \$85,600.
Over \$109,400 but not over \$162,400.....	\$36,630, plus 49% of the excess over \$109,400.
Over \$162,400.....	\$62,600, plus 50% of the excess over \$162,400.

**"(b) HEADS OF HOUSEHOLDS.—**There is hereby imposed on the taxable income of every individual who is the head of a household (as defined in section 2(b)) a tax determined in accordance with the following tables:

**"(1) FOR TAXABLE YEARS BEGINNING IN 1982.—**

<b><i>"If taxable income is:</i></b>	<b><i>The tax is:</i></b>
Not over \$2,300 .....	No tax.
Over \$2,300 but not over \$4,400 .....	12% of the excess over \$2,300.
Over \$4,400 but not over \$6,500 .....	\$252, plus 14% of the excess over \$4,400.
Over \$6,500 but not over \$8,700 .....	\$546, plus 16% of the excess over \$6,500.
Over \$8,700 but not over \$11,800 .....	\$898, plus 20% of the excess over \$8,700.
Over \$11,800 but not over \$15,000 .....	\$1,518, plus 22% of the excess over \$11,800.
Over \$15,000 but not over \$18,200 .....	\$2,222, plus 23% of the excess over \$15,000.
Over \$18,200 but not over \$23,500 .....	\$2,958, plus 28% of the excess over \$18,200.
Over \$23,500 but not over \$28,800 .....	\$4,442, plus 32% of the excess over \$23,500.
Over \$28,800 but not over \$34,100 .....	\$6,138, plus 38% of the excess over \$28,800.
Over \$34,100 but not over \$44,700 .....	\$8,152, plus 41% of the excess over \$34,100.
Over \$44,700 but not over \$60,600 .....	\$12,498, plus 49% of the excess over \$44,700.
Over \$60,600 .....	\$20,289, plus 50% of the excess over \$60,600.

***"(2) FOR TAXABLE YEARS BEGINNING IN 1983.—***

<b><i>"If taxable income is:</i></b>	<b><i>The tax is:</i></b>
Not over \$2,300 .....	No tax.
Over \$2,300 but not over \$4,400 .....	11% of the excess over \$2,300.
Over \$4,400 but not over \$6,500 .....	\$231, plus 13% of the excess over \$4,400.
Over \$6,500 but not over \$8,700 .....	\$504, plus 15% of the excess over \$6,500.
Over \$8,700 but not over \$11,800 .....	\$834, plus 18% of the excess over \$8,700.
Over \$11,800 but not over \$15,000 .....	\$1,392, plus 19% of the excess over \$11,800.
Over \$15,000 but not over \$18,200 .....	\$2,000, plus 21% of the excess over \$15,000.
Over \$18,200 but not over \$23,500 .....	\$2,672, plus 25% of the excess over \$18,200.
Over \$23,500 but not over \$28,800 .....	\$3,997, plus 29% of the excess over \$23,500.
Over \$28,800 but not over \$34,100 .....	\$5,534, plus 34% of the excess over \$28,800.
Over \$34,100 but not over \$44,700 .....	\$7,336, plus 37% of the excess over \$34,100.
Over \$44,700 but not over \$60,600 .....	\$11,258, plus 44% of the excess over \$44,700.
Over \$60,600 but not over \$81,800 .....	\$18,254, plus 48% of the excess over \$60,600.
Over \$81,800 .....	\$28,430, plus 50% of the excess over \$81,800.

***"(3) FOR TAXABLE YEARS BEGINNING AFTER 1983.—***

<b><i>"If taxable income is:</i></b>	<b><i>The tax is:</i></b>
Not over \$2,300 .....	No tax.
Over \$2,300 but not over \$4,400 .....	11% of the excess over \$2,300.
Over \$4,400 but not over \$6,500 .....	\$231, plus 12% of the excess over \$4,400.
Over \$6,500 but not over \$8,700 .....	\$483, plus 14% of the excess over \$6,500.
Over \$8,700 but not over \$11,800 .....	\$791, plus 17% of the excess over \$8,700.
Over \$11,800 but not over \$15,000 .....	\$1,318, plus 18% of the excess over \$11,800.
Over \$15,000 but not over \$18,200 .....	\$1,894, plus 20% of the excess over \$15,000.

<b><i>"If taxable income is:</i></b>	<b><i>The tax is:</i></b>
Over \$18,200 but not over \$23,500.....	\$2,534, plus 24% of the excess over \$18,200.
Over \$23,500 but not over \$28,800.....	\$3,806, plus 28% of the excess over \$23,500.
Over \$28,800 but not over \$34,100.....	\$5,290, plus 32% of the excess over \$28,800.
Over \$34,100 but not over \$44,700.....	\$6,986, plus 35% of the excess over \$34,100.
Over \$44,700 but not over \$60,600.....	\$10,696, plus 42% of the excess over \$44,700.
Over \$60,600 but not over \$81,800.....	\$17,374, plus 45% of the excess over \$60,600.
Over \$81,800 but not over \$108,300.....	\$26,914, plus 48% of the excess over \$81,800.
Over \$108,300.....	\$39,634, plus 50% of the excess over \$108,300.

***"(c) UNMARRIED INDIVIDUALS (OTHER THAN SURVIVING SPOUSES AND HEADS OF HOUSEHOLDS).—There is hereby imposed on the taxable income of every individual (other than a surviving spouse as defined in section 2(a) or the head of a household as defined in section 2(b)) who is not a married individual (as defined in section 143) a tax determined in accordance with the following tables:***

***"(1) FOR TAXABLE YEARS BEGINNING IN 1982.—***

<b><i>"If taxable income is:</i></b>	<b><i>The tax is:</i></b>
Not over \$2,300.....	No tax.
Over \$2,300 but not over \$3,400.....	12% of the excess over \$2,300.
Over \$3,400 but not over \$4,400.....	\$132, plus 14% of the excess over \$3,400.
Over \$4,400 but not over \$6,500.....	\$272, plus 16% of the excess over \$4,400.
Over \$6,500 but not over \$8,500.....	\$608, plus 17% of the excess over \$6,500.
Over \$8,500 but not over \$10,800.....	\$948, plus 19% of the excess over \$8,500.
Over \$10,800 but not over \$12,900.....	\$1,385, plus 22% of the excess over \$10,800.
Over \$12,900 but not over \$15,000.....	\$1,847, plus 23% of the excess over \$12,900.
Over \$15,000 but not over \$18,200.....	\$2,330, plus 27% of the excess over \$15,000.
Over \$18,200 but not over \$23,500.....	\$3,194, plus 31% of the excess over \$18,200.
Over \$23,500 but not over \$28,800.....	\$4,837, plus 35% of the excess over \$23,500.
Over \$28,800 but not over \$34,100.....	\$6,692, plus 40% of the excess over \$28,800.
Over \$34,100 but not over \$41,500.....	\$8,812, plus 44% of the excess over \$34,100.
Over \$41,500.....	\$12,068, plus 50% of the excess over \$41,500.

***"(2) FOR TAXABLE YEARS BEGINNING IN 1983.—***

<b><i>"If taxable income is:</i></b>	<b><i>The tax is:</i></b>
Not over \$2,300.....	No tax.
Over \$2,300 but not over \$3,400.....	11% of the excess over \$2,300.
Over \$3,400 but not over \$4,400.....	\$121, plus 13% of the excess over \$3,400.
Over \$4,400 but not over \$8,500.....	\$251, plus 15% of the excess over \$4,400.
Over \$8,500 but not over \$10,800.....	\$866, plus 17% of the excess over \$8,500.
Over \$10,800 but not over \$12,900.....	\$1,257, plus 19% of the excess over \$10,800.
Over \$12,900 but not over \$15,000.....	\$1,656, plus 21% of the excess over \$12,900.



<i><b>"If taxable income is:</b></i>	<i><b>The tax is:</b></i>
Over \$15,000 but not over \$18,200 .....	\$2,097, plus 24% of the excess over \$15,000.
Over \$18,200 but not over \$23,500 .....	\$2,865, plus 28% of the excess over \$18,200.
Over \$23,500 but not over \$28,800 .....	\$4,349, plus 32% of the excess over \$23,500.
Over \$28,800 but not over \$34,100 .....	\$6,045, plus 36% of the excess over \$28,800.
Over \$34,100 but not over \$41,500 .....	\$7,953, plus 40% of the excess over \$34,100.
Over \$41,500 but not over \$55,300 .....	\$10,913, plus 45% of the excess over \$41,500.
Over \$55,300 .....	\$17,123, plus 50% of the excess over \$55,300.

**"(3) FOR TAXABLE YEARS BEGINNING AFTER 1983.—**

<i><b>"If taxable income is:</b></i>	<i><b>The tax is:</b></i>
Not over \$2,300 .....	No tax.
Over \$2,300 but not over \$3,400 .....	11% of the excess over \$2,300.
Over \$3,400 but not over \$4,400 .....	\$121, plus 12% of the excess over \$3,400.
Over \$4,400 but not over \$6,500 .....	\$241, plus 14% of the excess over \$4,400.
Over \$6,500 but not over \$8,500 .....	\$535, plus 15% of the excess over \$6,500.
Over \$8,500 but not over \$10,800 .....	\$835, plus 16% of the excess over \$8,500.
Over \$10,800 but not over \$12,900 .....	\$1,203, plus 18% of the excess over \$10,800.
Over \$12,900 but not over \$15,000 .....	\$1,581, plus 20% of the excess over \$12,900.
Over \$15,000 but not over \$18,200 .....	\$2,001, plus 23% of the excess over \$15,000.
Over \$18,200 but not over \$23,500 .....	\$2,737, plus 26% of the excess over \$18,200.
Over \$23,500 but not over \$28,800 .....	\$4,115, plus 30% of the excess over \$23,500.
Over \$28,800 but not over \$34,100 .....	\$5,705, plus 34% of the excess over \$28,800.
Over \$34,100 but not over \$41,500 .....	\$7,507, plus 38% of the excess over \$34,100.
Over \$41,500 but not over \$55,300 .....	\$10,319, plus 42% of the excess over \$41,500.
Over \$55,300 but not over \$81,800 .....	\$16,115, plus 48% of the excess over \$55,300.
Over \$81,800 .....	\$28,835, plus 50% of the excess over \$81,800.

**"(d) MARRIED INDIVIDUALS FILING SEPARATE RETURNS.—**There is hereby imposed on the taxable income of every married individual (as defined in section 143) who does not make a single return jointly with his spouse under section 6013 a tax determined in accordance with the following tables:

**"(1) FOR TAXABLE YEARS BEGINNING IN 1982.—**

<i><b>"If taxable income is:</b></i>	<i><b>The tax is:</b></i>
Not over \$1,700 .....	No tax.
Over \$1,700 but not over \$2,750 .....	12% of the excess over \$1,700.
Over \$2,750 but not over \$3,800 .....	\$126, plus 14% of the excess over \$2,750.
Over \$3,800 but not over \$5,950 .....	\$273, plus 16% of the excess over \$3,800.
Over \$5,950 but not over \$8,000 .....	\$617, plus 19% of the excess over \$5,950.
Over \$8,000 but not over \$10,100 .....	\$1,006, plus 22% of the excess over \$8,000.
Over \$10,100 but not over \$12,300 .....	\$1,468, plus 25% of the excess over \$10,100.

<i><b>"If taxable income is:</b></i>	<i><b>The tax is:</b></i>
Over \$12,300 but not over \$14,950 .....	\$2,018, plus 29% of the excess over \$12,300.
Over \$14,950 but not over \$17,600 .....	\$2,787, plus 33% of the excess over \$14,950.
Over \$17,600 but not over \$22,900 .....	\$3,661, plus 39% of the excess over \$17,600.
Over \$22,900 but not over \$30,000 .....	\$5,728, plus 44% of the excess over \$22,900.
Over \$30,000 but not over \$42,800 .....	\$8,852, plus 49% of the excess over \$30,000.
Over \$42,800 .....	\$15,124, plus 50% of the excess over \$42,800.

**"(2) FOR TAXABLE YEARS BEGINNING IN 1983.—**

<i><b>"If taxable income is:</b></i>	<i><b>The tax is:</b></i>
Not over \$1,700 .....	No tax.
Over \$1,700 but not over \$2,750 .....	11% of the excess over \$1,700.
Over \$2,750 but not over \$3,800 .....	\$115, plus 13% of the excess over \$2,750.
Over \$3,800 but not over \$5,950 .....	\$252, plus 15% of the excess over \$3,800.
Over \$5,950 but not over \$8,000 .....	\$574, plus 17% of the excess over \$5,950.
Over \$8,000 but not over \$10,100 .....	\$923, plus 19% of the excess over \$8,000.
Over \$10,100 but not over \$12,300 .....	\$1,322, plus 23% of the excess over \$10,100.
Over \$12,300 but not over \$14,950 .....	\$1,828, plus 26% of the excess over \$12,300.
Over \$14,950 but not over \$17,600 .....	\$2,517, plus 30% of the excess over \$14,950.
Over \$17,600 but not over \$22,900 .....	\$3,312, plus 35% of the excess over \$17,600.
Over \$22,900 but not over \$30,000 .....	\$5,167, plus 40% of the excess over \$22,900.
Over \$30,000 but not over \$42,800 .....	\$8,007, plus 44% of the excess over \$30,000.
Over \$42,800 but not over \$54,700 .....	\$13,639, plus 48% of the excess over \$42,800.
Over \$54,700 .....	\$19,351, plus 50% of the excess over \$54,700.

**"(3) FOR TAXABLE YEARS BEGINNING AFTER 1983.—**

<i><b>"If taxable income is:</b></i>	<i><b>The tax is:</b></i>
Not over \$1,700 .....	No tax.
Over \$1,700 but not over \$2,750 .....	11% of the excess over \$1,700.
Over \$2,750 but not over \$3,800 .....	\$115, plus 12% of the excess over \$2,750.
Over \$3,800 but not over \$5,950 .....	\$241, plus 14% of the excess over \$3,800.
Over \$5,950 but not over \$8,000 .....	\$542, plus 16% of the excess over \$5,950.
Over \$8,000 but not over \$10,100 .....	\$870, plus 18% of the excess over \$8,000.
Over \$10,100 but not over \$12,300 .....	\$1,248, plus 22% of the excess over \$10,100.
Over \$12,300 but not over \$14,950 .....	\$1,732, plus 25% of the excess over \$12,300.
Over \$14,950 but not over \$17,600 .....	\$2,395, plus 28% of the excess over \$14,950.
Over \$17,600 but not over \$22,900 .....	\$3,137, plus 33% of the excess over \$17,600.
Over \$22,900 but not over \$30,000 .....	\$4,886, plus 38% of the excess over \$22,900.
Over \$30,000 but not over \$42,800 .....	\$7,584, plus 42% of the excess over \$30,000.
Over \$42,800 but not over \$54,700 .....	\$12,960, plus 45% of the excess over \$42,800.

<i>"If taxable income is:</i>	<i>The tax is:</i>
Over \$54,700 but not over \$81,200 .....	\$18,915, plus 49% of the excess over \$54,700.
Over \$81,200 .....	\$31,300, plus 50% of the excess over \$81,200.

**"(e) ESTATES AND TRUSTS.**—There is hereby imposed on the taxable income of every estate and trust taxable under this subsection a tax determined in accordance with the following tables:

**"(1) FOR TAXABLE YEARS BEGINNING IN 1982.—**

<i>"If taxable income is:</i>	<i>The tax is:</i>
Not over \$1,050 .....	12% of taxable income.
Over \$1,050 but not over \$2,100 .....	\$126, plus 14% of the excess over \$1,050.
Over \$2,100 but not over \$4,250 .....	\$273, plus 16% of the excess over \$2,100.
Over \$4,250 but not over \$6,300 .....	\$617, plus 19% of the excess over \$4,250.
Over \$6,300 but not over \$8,400 .....	\$1,006, plus 22% of the excess over \$6,300.
Over \$8,400 but not over \$10,600 .....	\$1,468, plus 25% of the excess over \$8,400.
Over \$10,600 but not over \$13,250 .....	\$2,018, plus 29% of the excess over \$10,600.
Over \$13,250 but not over \$15,900 .....	\$2,787, plus 33% of the excess over \$13,250.
Over \$15,900 but not over \$21,200 .....	\$3,661, plus 39% of the excess over \$15,900.
Over \$21,200 but not over \$28,300 .....	\$5,728, plus 44% of the excess over \$21,200.
Over \$28,300 but not over \$41,100 .....	\$8,852, plus 49% of the excess over \$28,300.
Over \$41,100 .....	\$15,124, plus 50% of the excess over \$41,100.

**"(2) FOR TAXABLE YEARS BEGINNING IN 1983.—**

<i>"If taxable income is:</i>	<i>The tax is:</i>
Not over \$1,050 .....	11% of taxable income.
Over \$1,050 but not over \$2,100 .....	\$115, plus 13% of the excess over \$1,050.
Over \$2,100 but not over \$4,250 .....	\$252, plus 15% of the excess over \$2,100.
Over \$4,250 but not over \$6,300 .....	\$574, plus 17% of the excess over \$4,250.
Over \$6,300 but not over \$8,400 .....	\$923, plus 19% of the excess over \$6,300.
Over \$8,400 but not over \$10,600 .....	\$1,322, plus 23% of the excess over \$8,400.
Over \$10,600 but not over \$13,250 .....	\$1,828, plus 26% of the excess over \$10,600.
Over \$13,250 but not over \$15,900 .....	\$2,517, plus 30% of the excess over \$13,250.
Over \$15,900 but not over \$21,200 .....	\$3,312, plus 35% of the excess over \$15,900.
Over \$21,200 but not over \$28,300 .....	\$5,167, plus 40% of the excess over \$21,200.
Over \$28,300 but not over \$41,100 .....	\$8,007, plus 44% of the excess over \$28,300.
Over \$41,100 but not over \$53,000 .....	\$13,639, plus 48% of the excess over \$41,100.
Over \$53,000 .....	\$19,351, plus 50% of the excess over \$53,000.

**"(3) FOR TAXABLE YEARS BEGINNING AFTER 1983.—**

<i>"If taxable income is:</i>	<i>The tax is:</i>
Not over \$1,050 .....	11% of taxable income.
Over \$1,050 but not over \$2,100 .....	\$115, plus 12% of the excess over \$1,050.
Over \$2,100 but not over \$4,250 .....	\$241, plus 14% of the excess over \$2,100.

<i><b>"If taxable income is:</b></i>	<i><b>The tax is:</b></i>
Over \$4,250 but not over \$6,300.....	\$542, plus 16% of the excess over \$4,250.
Over \$6,300 but not over \$8,400.....	\$870, plus 18% of the excess over \$6,300.
Over \$8,400 but not over \$10,600.....	\$1,248, plus 22% of the excess over \$8,400.
Over \$10,600 but not over \$13,250.....	\$1,732, plus 25% of the excess over \$10,600.
Over \$13,250 but not over \$15,900.....	\$2,395, plus 28% of the excess over \$13,250.
Over \$15,900 but not over \$21,200.....	\$3,137, plus 33% of the excess over \$15,900.
Over \$21,200 but not over \$28,300.....	\$4,886, plus 38% of the excess over \$21,200.
Over \$28,300 but not over \$41,100.....	\$7,584, plus 42% of the excess over \$28,300.
Over \$41,100 but not over \$53,000.....	\$12,960, plus 45% of the excess over \$41,100.
Over \$53,000 but not over \$79,500.....	\$18,315, plus 49% of the excess over \$53,000.
Over \$79,500.....	\$31,300, plus 50% of the excess over \$79,500."

**(b) CREDIT TO REFLECT EQUIVALENT 1981 RATE REDUCTION.—**

**(1) IN GENERAL.—**Section 6428 (relating to refund of 1974 individual income taxes) is amended to read as follows:

**"SEC. 6428. 1981 RATE REDUCTION TAX CREDIT.**

**"(a) ALLOWANCE OF CREDIT.—**There shall be allowed as a credit against the tax imposed by section 1, or against a tax imposed in lieu of the tax imposed by section 1, for any taxable year beginning in 1981, an amount equal to the product of—

"(1) 1.25 percent, multiplied by

"(2) the amount of tax imposed by section 1 (or in lieu thereof) for such taxable year.

**"(b) SPECIAL RULES FOR APPLICATION OF THIS SECTION.—**

**"(1) APPLICATION WITH OTHER CREDITS.—**In determining any credit allowed under subpart A of part IV of subchapter A of chapter 1 (other than under sections 31, 39, and 43), the tax imposed by chapter 1 shall (before any other reductions) be reduced by the credit allowed under subsection (a).

**"(2) CREDIT TREATED AS SUBPART A CREDIT.—**For purposes of this title, the credit allowed under subsection (a) shall be treated as a credit allowed under subpart A of part IV of subchapter A of chapter 1.

**"(c) TABLES TO REFLECT CREDIT.—**

**"(1) SECTION 3 TABLES.—**The tables prescribed by the Secretary under section 3 shall reflect the credit allowed under subsection (a).

**"(2) OTHER TABLES.—**In order to reflect the amount of the credit under subsection (a) for different levels of tax or taxable income, the Secretary may—

"(A) modify the tables under section 1, or

"(B) prescribe such other tables as he determines necessary."

**(2) CONFORMING AMENDMENTS.—**

**(A)** The table of sections for subchapter B of chapter 65 is amended by striking out the item relating to section 6428 and inserting in lieu thereof the following new item:

"Sec. 6428. 1981 rate reduction tax credit."

(B) Paragraph (1) of section 3(a) (relating to imposition of tax table tax) is amended by inserting "and which shall be in such form as he determines appropriate" after "Secretary".

(C) Subsection (a) of section 3 (relating to tax tables for individuals) is amended by adding at the end thereof the following new paragraph:

"(5) SECTION MAY BE APPLIED ON THE BASIS OF TAXABLE INCOME.—The Secretary may provide that this section shall be applied for any taxable year on the basis of taxable income in lieu of tax table income."

(c) REPEAL OF MAXIMUM TAX ON PERSONAL SERVICE INCOME.—

(1) IN GENERAL.—Part VI of subchapter Q of chapter 1 (relating to maximum rate on personal service income) is repealed.

(2) CONFORMING AMENDMENTS.—

(A) Paragraph (1) of section 3(b) (relating to tax tables for individuals) is amended to read as follows:

"(1) an individual to whom section 1301 (relating to income averaging) applies for the taxable year,"

(B) Subsection (b) of section 1304 (relating to special rules for income averaging) is amended—

(i) by inserting "and" at the end of paragraph (1),

(ii) by striking out ", and" at the end of paragraph (2) and inserting in lieu thereof a period, and

(iii) by striking out paragraph (3).

(C) The table of parts for subchapter Q of chapter 1 is amended by striking out the item relating to part VI.

(d) CONFORMING AMENDMENTS.—

(1) ALTERNATIVE MINIMUM TAX.—Paragraph (1) of section 55(a) (relating to alternative minimum tax) is amended—

(A) by striking out all that follows "\$60,000" in subparagraph (B) and inserting in lieu thereof ", exceeds", and

(B) by striking out subparagraph (C).

(2) PERSONAL HOLDING COMPANY TAX.—Section 541 (relating to personal holding company tax) is amended by striking out "70 percent" and inserting in lieu thereof "50 percent".

(3) AMENDMENT TO SECTION 21.—Section 21 (relating to effect of changes in rates during taxable year) is amended by striking out subsections (d), (e), and (f) and inserting in lieu thereof the following:

"(d) SECTION NOT TO APPLY TO SECTION 1 RATE CHANGES MADE BY ECONOMIC RECOVERY TAX ACT OF 1981.—This section shall not apply to any change in rates under section 1 attributable to the amendments made by section 1010 of the Economic Recovery Tax Act of 1981 or subsection (f) of section 1 (relating to adjustments in tax tables so that inflation will not result in tax increases)."

(e) WITHHOLDING TABLES.—

(1) DETERMINATION OF WITHHOLDING.—Section 3402(a) (relating to requirement of withholding income tax at source) is amended to read as follows:

"(a) REQUIREMENT OF WITHHOLDING.—

"(1) IN GENERAL.—Except as otherwise provided in this section, every employer making payment of wages shall deduct and withhold upon such wages a tax determined in accordance with tables or computational procedures prescribed by the Secretary.

Any tables or procedures prescribed under this paragraph shall—

“(A) apply with respect to the amount of wages paid during such periods as the Secretary may prescribe, and

“(B) be in such form, and provide for such amounts to be deducted and withheld, as the Secretary determines to be most appropriate to carry out the purposes of this chapter and to reflect the provisions of chapter 1 applicable to such periods.

“(2) AMOUNT OF WAGES.—For purposes of applying tables or procedures prescribed under paragraph (1), the term ‘the amount of wages’ means the amount by which the wages exceed the number of withholding exemptions claimed multiplied by the amount of one such exemption. The amount of each withholding exemption shall be equal to the amount of one personal exemption provided in section 151(b), prorated to the payroll period. The maximum number of withholding exemptions permitted shall be calculated in accordance with regulations prescribed by the Secretary under this section, taking into account any reduction in withholding to which an employee is entitled under this section.

“(3) CHANGES MADE BY SECTION 101 OF THE ECONOMIC RECOVERY TAX ACT OF 1981.—Notwithstanding the provisions of this subsection, the Secretary shall modify the tables and procedures under paragraph (1) to reflect—

“(A) the amendments made by section 101(b) of the Economic Recovery Tax Act of 1981, and such modification shall take effect on October 1, 1981, as if such amendments made a 5-percent reduction effective on such date, and

“(B) the amendments made by section 101(a) of such Act, and such modifications shall take effect—

“(i) on July 1, 1982, as if the reductions in the rate of tax under section 1 (as amended by such section) were attributable to a 10-percent reduction effective on such date, and

“(ii) on July 1, 1983, as if such reductions were attributable to a 10-percent reduction effective on such date.”

(2) WAGES PAID FOR PERIOD LESS THAN 1 WEEK.—Section 3402(b) (relating to the percentage method of withholding) is amended—

(A) by striking out paragraph (1), and redesignating paragraphs (2) through (5) as paragraphs (1) through (4), respectively; and

(B) by striking out paragraph (3), as redesignated by subparagraph (A), and inserting in lieu thereof the following:

“(3) In any case in which the period, or the time described in paragraph (2), in respect of any wages is less than one week, the Secretary, under regulations prescribed by him, may authorize an employer to compute the tax to be deducted and withheld as if the aggregate of the wages paid to the employee during the calendar week were paid for a weekly payroll period.”

(3) ZERO BRACKET AMOUNT.—Paragraph (1)(G) of section 3402(f) (relating to withholding exemptions) is amended by in-

serting "(or more than one exemption if so prescribed by the Secretary)" after "one exemption".

(4) **CHANGES IN WITHHOLDING.**—Section 3402(i) (relating to additional withholding) is amended to read as follows:

"(i) **CHANGES IN WITHHOLDING.**—

"(1) **IN GENERAL.**—The Secretary may by regulations provide for increases or decreases in the amount of withholding otherwise required under this section in cases where the employee requests such changes.

"(2) **TREATMENT AS TAX.**—Any increased withholding under paragraph (1) shall for all purposes be considered tax required to be deducted and withheld under this chapter."

(5) **WITHHOLDING ALLOWANCES.**—Subsection (m) of section 3402 (relating to withholding allowances based on itemized deductions) is amended to read as follows:

"(m) **WITHHOLDING ALLOWANCES.**—Under regulations prescribed by the Secretary, an employee shall be entitled to additional withholding allowances or additional reductions in withholding under this subsection. In determining the number of additional withholding allowances or the amount of additional reductions in withholding under this subsection, the employee may take into account (to the extent and in the manner provided by such regulations)—

"(1) estimated itemized deductions allowable under chapter 1 (other than the deductions referred to in section 151 and other than the deductions required to be taken into account in determining adjusted gross income under section 62) (other than paragraph (13) thereof),

"(2) estimated tax credits allowable under chapter 1, and

"(3) such additional deductions and other items as may be specified by the Secretary in regulations."

(f) **EFFECTIVE DATES.**—

(1) **IN GENERAL.**—The amendments made by subsections (a), (c), and (d) shall apply to taxable years beginning after December 31, 1981.

(2) **WITHHOLDING AMENDMENTS.**—The amendments made by subsection (e) shall apply to remuneration paid after September 30, 1981; except that the amendment made by subsection (e)(5) shall apply to remuneration paid after December 31, 1981.

**SEC. 102. 20-PERCENT MAXIMUM RATE ON NET CAPITAL GAIN FOR PORTION OF 1981, DECREASE IN HOLDING PERIOD.**

(a) **IN GENERAL.**—If for any taxable year ending after June 9, 1981, and beginning before January 1, 1982, a taxpayer other than a corporation has qualified net capital gain, then the tax imposed under section 1 of the Internal Revenue Code of 1954 for such taxable year shall be equal to the lesser of—

(1) the tax imposed under such section determined without regard to this subsection, or

(2) the sum of—

(A) the tax imposed under such section on the excess of—

(i) the taxable income of the taxpayer, over

(ii) 40 percent of the qualified net capital gain of the taxpayer, and

(B) 20 percent of the qualified net capital gain.

(b) **APPLICATION WITH ALTERNATIVE MINIMUM TAX.**—

(1) **IN GENERAL.**—If subsection (a) applies to any taxpayer for any taxable year, then the amount determined under section 55(a)(1) of the Internal Revenue Code of 1954 for such taxable year shall be equal to the lesser of—

(A) the amount determined under such section 55(a)(1) determined without regard to this subsection, or

(B) the sum of—

(i) the amount which would be determined under such section 55(a)(1) if the alternative minimum taxable income was the excess of—

(I) the alternative minimum taxable income (within the meaning of section 55(b)(1) of such Code) of the taxpayer, over

(II) the qualified net capital gain of the taxpayer, and

(ii) 20 percent of the qualified net capital gain.

(2) **NO CREDITS ALLOWABLE.**—For purposes of section 55(c) of such Code, no credit allowable under subpart A of part IV of subchapter A of chapter 1 of such Code (other than section 33(a) of such Code) shall be allowable against the amount described in paragraph (1)(B)(ii).

(c) **QUALIFIED NET CAPITAL GAIN.**—

(1) **IN GENERAL.**—For purposes of this section, the term “qualified net capital gain” means the lesser of—

(A) the net capital gain for the taxable year, or

(B) the net capital gain for the taxable year taking into account only gain or loss from sales or exchanges occurring after June 9, 1981.

(2) **NET CAPITAL GAIN.**—For purposes of this subsection, the term “net capital gain” has the meaning given such term by section 1222(11) of the Internal Revenue Code of 1954.

(d) **SPECIAL RULE FOR PASS-THRU ENTITIES.**—

(1) **IN GENERAL.**—In applying subsections (a), (b), and (c) with respect to any pass-thru entity, the determination of when a sale or exchange has occurred shall be made at the entity level.

(2) **PASS-THRU ENTITY DEFINED.**—For purposes of paragraph (1), the term “pass-thru entity” means—

(A) a regulated investment company,

(B) a real estate investment trust,

(C) an electing small business corporation,

(D) a partnership,

(E) an estate or trust, and

(F) a common trust fund.

#### **SEC. 103. DEDUCTION FOR TWO-EARNER MARRIED COUPLES.**

(a) **IN GENERAL.**—Part VII of subchapter B of chapter 1 (relating to additional itemized deductions for individuals) is amended by redesignating section 221 as section 222 and by inserting after section 220 the following new section:

#### **“SEC. 221. DEDUCTION FOR TWO-EARNER MARRIED COUPLES.**

**“(a) DEDUCTION ALLOWED.**—

**“(1) IN GENERAL.**—In the case of a joint return under section 6013 for the taxable year, there shall be allowed as a deduction an amount equal to 10 percent of the lesser of—

**“(A) \$30,000, or**



“(B) the qualified earned income of the spouse with the lower qualified earned income for such taxable year.

“(2) SPECIAL RULE FOR 1982.—In the case of a taxable year beginning during 1982, paragraph (1) shall be applied by substituting ‘5 percent’ for ‘10 percent’.

“(b) QUALIFIED EARNED INCOME DEFINED.—

“(1) IN GENERAL.—For purposes of this section, the term ‘qualified earned income’ means an amount equal to the excess of—

“(A) the earned income of the spouse for the taxable year, over

“(B) an amount equal to the sum of the deductions described in paragraphs (1), (2), (7), (9), (10), and (15) of section 62 to the extent such deductions are properly allocable to or chargeable against earned income described in subparagraph (A).

The amount of qualified earned income shall be determined without regard to any community property laws.

“(2) EARNED INCOME.—For purposes of paragraph (1), the term ‘earned income’ means income which is earned income within the meaning of section 911(d)(2) or 401(c)(2)(C), except that—

“(A) such term shall not include any amount—

“(i) not includible in gross income,

“(ii) received as a pension or annuity,

“(iii) paid or distributed out of an individual retirement plan (within the meaning of section 7701(a)(37)),

“(iv) received as deferred compensation, or

“(v) received for services performed by an individual in the employ of his spouse (within the meaning of section 3121(b)(3)(A)), and

“(B) section 911(d)(2)(B) shall be applied without regard to the phrase ‘not in excess of 30 percent of his share of net profits of such trade or business’.

“(c) DEDUCTION DISALLOWED FOR INDIVIDUAL CLAIMING BENEFITS OF SECTION 911 OR 931.—No deduction shall be allowed under this section for any taxable year if either spouse claims the benefits of section 911 or 931 for such taxable year.”

(b) DEDUCTION ALLOWED IN COMPUTING ADJUSTED GROSS INCOME.—Section 62 (defining adjusted gross income), as amended by section 112(b)(2) of this Act, is amended by inserting after paragraph (15) the following new paragraph:

“(16) DEDUCTION FOR TWO-EARNER MARRIED COUPLES.—The deduction allowed by section 221.”

(c) OTHER CONFORMING AMENDMENTS.—

(1) Subsection (a) of section 85 (relating to unemployment compensation) is amended by striking out “and without regard to section 105(d)” and inserting in lieu thereof “, section 105(d), and section 221”.

(2) Subsection (d)(3) of section 105 (relating to amounts received under accident and health plans) is amended by inserting “and section 221” after “subsection” the first place it appears.

(3) The table of sections for such part VII is amended by striking out the item relating to section 221 and inserting in lieu thereof the following new items:

"Sec. 221. Deduction for two-earner married couples.

"Sec. 222. Cross references."

(d) **EFFECTIVE DATES.**—The amendments made by this section shall apply to taxable years beginning after December 31, 1981.

**SEC. 104. ADJUSTMENT TO PREVENT INFLATION-CAUSED TAX INCREASE.**

(a) **ADJUSTMENTS TO INDIVIDUAL INCOME TAX BRACKETS.**—Section 1 (relating to tax imposed) is amended by adding at the end thereof the following new subsection:

"(f) **ADJUSTMENTS IN TAX TABLES SO THAT INFLATION WILL NOT RESULT IN TAX INCREASES.**—

"(1) **IN GENERAL.**—Not later than December 15 of 1984 and each subsequent calendar year, the Secretary shall prescribe tables which shall apply in lieu of the tables contained in paragraph (3) of subsections (a), (b), (c), (d), and (e) with respect to taxable years beginning in the succeeding calendar year.

"(2) **METHOD OF PRESCRIBING TABLES.**—The table which under paragraph (1) is to apply in lieu of the table contained in paragraph (3) of subsection (a), (b), (c), (d), or (e), as the case may be, with respect to taxable years beginning in any calendar year shall be prescribed—

"(A) by increasing—

"(i) the maximum dollar amount on which no tax is imposed under such table, and

"(ii) the minimum and maximum dollar amounts for each rate bracket for which a tax is imposed under such table, by the cost-of-living adjustment for such calendar year,

"(B) by not changing the rate applicable to any rate bracket as adjusted under subparagraph (A)(ii), and

"(C) by adjusting the amounts setting forth the tax to the extent necessary to reflect the adjustments in the rate brackets.

If any increase determined under subparagraph (A) is not a multiple of \$10, such increase shall be rounded to the nearest multiple of \$10 (or if such increase is a multiple of \$5, such increase shall be increased to the next highest multiple of \$10).

"(3) **COST-OF-LIVING ADJUSTMENT.**—For purposes of paragraph (2), the cost-of-living adjustment for any calendar year is the percentage (if any) by which—

"(A) the CPI for the preceding calendar year, exceeds

"(B) the CPI for the calendar year 1983.

"(4) **CPI FOR ANY CALENDAR YEAR.**—For purposes of paragraph (3), the CPI for any calendar year is the average of the Consumer Price Index as of the close of the 12-month period ending on September 30 of such calendar year.

"(5) **CONSUMER PRICE INDEX.**—For purposes of paragraph (4), the term 'Consumer Price Index' means the last Consumer Price Index for all-urban consumers published by the Department of Labor."

(b) **DEFINITION OF ZERO BRACKET AMOUNT.**—Subsection (d) of section 63 (defining zero bracket amount) is amended to read as follows:

“(d) **ZERO BRACKET AMOUNT.**—For purposes of this subtitle, the term ‘zero bracket amount’ means—

“(1) in the case of an individual to whom subsection (a), (b), (c), or (d) of section 1 applies, the maximum amount of taxable income on which no tax is imposed by the applicable subsection of section 1, or

“(2) zero in any other case.”

(c) **PERSONAL EXEMPTIONS.**—

(1) **GENERAL RULE.**—Section 151 (relating to allowance of deductions for personal exemptions) is amended by striking out “\$1,000” each place it appears and inserting in lieu thereof “the exemption amount”.

(2) **EXEMPTION AMOUNT.**—Section 151 is amended by adding at the end thereof the following new subsection:

“(f) **EXEMPTION AMOUNT.**—For purposes of this section, the term ‘exemption amount’ means, with respect to any taxable year, \$1,000 increased by an amount equal to \$1,000 multiplied by the cost-of-living adjustment (as defined in section 1(f)(3)) for the calendar year in which the taxable year begins. If the amount determined under the preceding sentence is not a multiple of \$10, such amount shall be rounded to the nearest multiple of \$10 (or if such amount is a multiple of \$5, such amount shall be increased to the next highest multiple of \$10).”

(d) **RETURN REQUIREMENTS.**—

(1) **AMENDMENTS TO SECTION 6012.**—

(A) Clause (i) of section 6012(a)(1)(A) is amended by striking out “\$3,300” and inserting in lieu thereof “the sum of the exemption amount plus the zero bracket amount applicable to such an individual”.

(B) Clause (ii) of section 6012(a)(i)(A) is amended by striking out “\$4,400” and inserting in lieu thereof “the sum of the exemption amount plus the zero bracket amount applicable to such an individual”.

(C) Clause (iii) of section 6012(a)(1)(A) is amended by striking out “\$5,400” and inserting in lieu thereof “the sum of twice the exemption amount plus the zero bracket amount applicable to a joint return”.

(D) Paragraph (1) of section 6012(a) is amended by striking out “\$1,000” each place it appears and inserting in lieu thereof “the exemption amount”.

(E) Paragraph (1) of section 6012(a) is amended by adding at the end thereof the following new subparagraph:

“(D) For purposes of this paragraph—

“(i) The term ‘zero bracket amount’ has the meaning given to such term by section 63(d).

“(ii) The term ‘exemption amount’ has the meaning given to such term by section 151(f).”

(2) **AMENDMENTS TO SECTION 6013.**—Subparagraph (A) of section 6013(b)(3) is amended—

(A) by striking out “\$1,000” each place it appears and inserting in lieu thereof “the exemption amount”,

(B) by striking out "\$2,000" each place it appears and inserting in lieu thereof "twice the exemption amount", and  
 (C) by adding at the end thereof the following new sentence: "For purposes of this subparagraph, the term 'exemption amount' has the meaning given to such term by section 151(f)."

(e) **EFFECTIVE DATE.**—The amendments made by this section shall apply to taxable years beginning after December 31, 1984.

## **Subtitle B—Income Earned Abroad**

### **SEC. 111. PARTIAL EXCLUSION FOR EARNED INCOME FROM SOURCES WITHOUT THE UNITED STATES AND FOREIGN HOUSING COSTS.**

(a) **IN GENERAL.**—Section 911 (relating to income earned by individuals in certain camps) is amended to read as follows:

#### **"SEC. 911. CITIZENS OR RESIDENTS OF THE UNITED STATES LIVING ABROAD.**

"(a) **EXCLUSION FROM GROSS INCOME.**—At the election of a qualified individual (made separately with respect to paragraphs (1) and (2)), there shall be excluded from the gross income of such individual, and exempt from taxation under this subtitle, for any taxable year—

"(1) the foreign earned income of such individual, and  
 (2) the housing cost amount of such individual.

"(b) **FOREIGN EARNED INCOME.**—

"(1) **DEFINITION.**—For purposes of this section—

"(A) **IN GENERAL.**—The term 'foreign earned income' with respect to any individual means the amount received by such individual from sources within a foreign country or countries which constitute earned income attributable to services performed by such individual during the period described in subparagraph (A) or (B) of subsection (d)(1), whichever is applicable.

"(B) **CERTAIN AMOUNTS NOT INCLUDED IN FOREIGN EARNED INCOME.**—The foreign earned income for an individual shall not include amounts—

"(i) received as a pension or annuity,

"(ii) paid by the United States or an agency thereof to an employee of the United States or an agency thereof,

"(iii) included in gross income by reason of section 402(b) (relating to taxability of beneficiary of nonexempt trust) or section 403(c) (relating to taxability of beneficiary under a nonqualified annuity), or

"(iv) received after the close of the taxable year following the taxable year in which the services to which the amounts are attributable are performed.

"(2) **LIMITATION ON FOREIGN EARNED INCOME.**—

"(A) **IN GENERAL.**—The foreign earned income of an individual which may be excluded under subsection (a)(1) for any taxable year shall not exceed the amount of foreign earned income computed on a daily basis at the annual rate set forth in the following table for each day of the taxable year within the applicable period described in subparagraph (A) or (B) of subsection (d)(1):

**"In the case of taxable years beginning in:**

	<i>The annual rate is:</i>
1982.....	\$75,000
1983.....	80,000
1984.....	85,000
1985.....	90,000
1986 and thereafter.....	95,000.

**"(B) CONTRIBUTION TO YEAR IN WHICH SERVICES ARE PERFORMED.—**For purposes of applying subparagraph (A), amounts received shall be considered received in the taxable year in which the services to which the amounts are attributable are performed.

**"(C) TREATMENT OF COMMUNITY INCOME.—**In applying subparagraph (A) with respect to amounts received from services performed by a husband or wife which are community income under community property laws applicable to such income, the aggregate amount which may be excludable from the gross income of such husband and wife under subsection (a)(1) for any taxable year shall equal the amount which would be so excludable if such amounts did not constitute community income.

**"(c) HOUSING COST AMOUNT.—**For purposes of this section—

**"(1) IN GENERAL.—**The term 'housing cost amount' means an amount equal to the excess of—

**"(A)** the housing expenses of an individual for the taxable year, over

**"(B)** an amount equal to the product of—

**"(i)** 16 percent of the salary (computed on a daily basis) of an employee of the United States who is compensated at a rate equal to the annual rate paid for step 1 of grade GS-14, multiplied by

**"(ii)** the number of days of such taxable year within the applicable period described in subparagraph (A) or (B) of subsection (d)(1).

**"(2) HOUSING EXPENSES.—**

**"(A) IN GENERAL.—**The term 'housing expenses' means the reasonable expenses paid or incurred during the taxable year by or on behalf of an individual for housing for the individual (and, if they reside with him, for his spouse and dependents) in a foreign country. The term—

**"(i)** includes expenses attributable to the housing (such as utilities and insurance), but

**"(ii)** does not include interest and taxes of the kind deductible under section 163 or 164 or any amount allowable as a deduction under section 216(a).

Housing expenses shall not be treated as reasonable to the extent such expenses are lavish or extravagant under the circumstances.

**"(B) SECOND FOREIGN HOUSEHOLD.—**

**"(i) IN GENERAL.—**Except as provided in clause (ii), only housing expenses incurred with respect to that abode which bears the closest relationship to the tax home of the individual shall be taken into account under paragraph (1).

**"(ii) SEPARATE HOUSEHOLD FOR SPOUSE AND DEPENDENTS.—**If an individual maintains a separate abode

outside the United States for his spouse and dependents and they do not reside with him because of living conditions which are dangerous, unhealthful, or otherwise adverse, then—

“(I) the words ‘if they reside with him’ in subparagraph (A) shall be disregarded, and

“(II) the housing expenses incurred with respect to such abode shall be taken into account under paragraph (1).

**“(3) SPECIAL RULES WHERE HOUSING EXPENSES NOT PROVIDED BY EMPLOYER.—**

“(A) **IN GENERAL.**—To the extent the housing cost amount of any individual for any taxable year is not attributable to employer provided amounts, such amount shall be treated as a deduction allowable in computing adjusted gross income to the extent of the limitation of subparagraph (B).

“(B) **LIMITATION.**—For purposes of subparagraph (A), the limitation of this subparagraph is the excess of—

“(i) the foreign earned income of the individual for the taxable year, over

“(ii) the amount of such income excluded from gross income under subsection (a)(1) for the taxable year.

**“(C) 1-YEAR CARRYOVER OF HOUSING AMOUNTS NOT ALLOWED BY REASON OF SUBPARAGRAPH (B).—**

“(i) **IN GENERAL.**—The amount not allowable as a deduction for any taxable year under subparagraph (A) by reason of the limitation of subparagraph (B) shall be treated as a deduction allowable in computing adjusted gross income for the succeeding taxable year (and only for the succeeding taxable year) to the extent of the limitation of clause (ii) for such succeeding taxable year.

“(ii) **LIMITATION.**—For purposes of clause (i), the limitation of this clause for any taxable year is the excess of—

“(I) the limitation of subparagraph (B) for such taxable year, over

“(II) amounts treated as a deduction under subparagraph (A) for such taxable year.

“(D) **EMPLOYER PROVIDED AMOUNTS.**—For purposes of this paragraph, the term ‘employer provided amounts’ means any amount paid or incurred on behalf of the individual by the individual’s employer which is foreign earned income included in the individual’s gross income for the taxable year (without regard to this section).

“(E) **FOREIGN EARNED INCOME.**—For purposes of this paragraph, an individual’s foreign earned income for any taxable year shall be determined without regard to the limitation of subparagraph (A) of subsection (b)(2).

**“(d) DEFINITIONS AND SPECIAL RULES.**—For purposes of this section—

“(1) **QUALIFIED INDIVIDUAL.**—The term ‘qualified individual’ means an individual whose tax home is in a foreign country and who is—

“(A) a citizen of the United States and establishes to the satisfaction of the Secretary that he has been a bona fide resident of a foreign country or countries for an uninterrupted period which includes an entire taxable year, or

“(B) a citizen or resident of the United States and who, during any period of 12 consecutive months, is present in a foreign country or countries during at least 330 full days in such period.

“(2) EARNED INCOME.—

“(A) IN GENERAL.—The term ‘earned income’ means wages, salaries, or professional fees, and other amounts received as compensation for personal services actually rendered, but does not include that part of the compensation derived by the taxpayer for personal services rendered by him to a corporation which represents a distribution of earnings or profits rather than a reasonable allowance as compensation for the personal services actually rendered.

“(B) TAXPAYER ENGAGED IN TRADE OR BUSINESS.—In the case of a taxpayer engaged in a trade or business in which both personal services and capital are material income-producing factors, under regulations prescribed by the Secretary, a reasonable allowance as compensation for the personal services rendered by the taxpayer, not in excess of 30 percent of his share of the net profits of such trade or business, shall be considered as earned income.

“(3) TAX HOME.—The term ‘tax home’ means, with respect to any individual, such individual’s home for purposes of section 162(a)(2) (relating to traveling expenses while away from home). An individual shall not be treated as having a tax home in a foreign country for any period for which his abode is within the United States.

“(4) WAIVER OF PERIOD OF STAY IN FOREIGN COUNTRY.—Notwithstanding paragraph (1), an individual who—

“(A) is a bona fide resident of, or is present in, a foreign country for any period,

“(B) leaves such foreign country after August 31, 1978—

“(i) during any period during which the Secretary determines, after consultation with the Secretary of State or his delegate, that individuals were required to leave such foreign country because of war, civil unrest, or similar adverse conditions in such foreign country which precluded the normal conduct of business by such individuals, and

“(ii) before meeting the requirements of such paragraph (1), and

“(C) establishes to the satisfaction of the Secretary that such individual could reasonably have been expected to have met such requirements but for the conditions referred to in clause (i) of subparagraph (B),

shall be treated as a qualified individual with respect to the period described in subparagraph (A) during which he was a bona fide resident of, or was present in, the foreign country, and in applying subsections (b)(2)(A) and (c)(1)(B)(ii) with respect to such individual, only the days within such period shall be taken into account.

**“(5) TEST OF BONA FIDE RESIDENCE.—If—**

**“(A) an individual who has earned income from sources within a foreign country submits a statement to the authorities of that country that he is not a resident of that country, and**

**“(B) such individual is held not subject as a resident of that country to the income tax of that country by its authorities with respect to such earnings,**  
**then such individual shall not be considered a bona fide resident of that country for purposes of paragraph (1)(A).**

**“(6) DENIAL OF DOUBLE BENEFITS.—No deduction or exclusion from gross income under this subtitle or credit against the tax imposed by this chapter (including any credit or deduction for the amount of taxes paid or accrued to a foreign country or possession of the United States) shall be allowed to the extent such deduction, exclusion, or credit is properly allocable to or chargeable against amounts excluded from gross income under subsection (a).**

**“(7) REGULATIONS.—The Secretary shall prescribe such regulations as may be necessary or appropriate to carry out the purposes of this section, including regulations providing rules—**

**“(A) for cases where a husband and wife each have earned income from sources outside the United States, and**

**“(B) for married individuals filing separate returns.**

**“(e) ELECTION.—**

**“(1) IN GENERAL.—An election under subsection (a) shall apply to the taxable year for which made and to all subsequent taxable years unless revoked under paragraph (2).**

**“(2) REVOCATION.—A taxpayer may revoke an election made under paragraph (1) for any taxable year after the taxable year for which such election was made. Except with the consent of the Secretary, any taxpayer who makes such a revocation for any taxable year may not make another election under this section for any subsequent taxable year before the 6th taxable year after the taxable year for which such revocation was made.**

**“(f) CROSS REFERENCES.—**

**“For administrative and penal provisions relating to the exclusions provided for in this section, see sections 6001, 6011, 6012(c), and the other provisions of subtitle F.”**

**(b) CONFORMING AMENDMENTS.—**

**(1) The table of sections for subpart B of part III of subchapter N of chapter 1 is amended by striking out the item relating to section 911 and inserting in lieu thereof the following:**

**“Sec. 911. Citizens or residents of the United States living abroad.”**

**(2) Section 43(c)(1)(C)(i) is amended by striking out “relating to income earned by individuals in certain camps outside the United States” and inserting in lieu thereof “relating to citizens or residents of the United States living abroad”.**

**(3) Sections 1302(b)(2)(A)(i), 1304(b)(1), 1402(a)(8), 6012(c), and 6091(b)(1)(B)(iii) are each amended by striking out “relating to income earned by employees in certain camps” and inserting in lieu thereof “relating to citizens or residents of the United States living abroad”.**



(4) Sections 37(e)(9)(B), 63(e)(2), 105(h)(3)(B)(v), 410(b)(3)(C), 879(a)(1), 1303(c)(2), and 1304(c)(3) are each amended by striking out "section 911(b)" each place it appears and inserting in lieu thereof "section 911(d)(2)".

(5) Paragraph (11) of section 1402(a) is amended to read as follows:

"(11) in the case of an individual described in section 911(d)(1)(B), the exclusion from gross income provided by section 911(a)(1) shall not apply; and".

**SEC. 112. REPEAL OF DEDUCTION FOR CERTAIN EXPENSES OF LIVING ABROAD.**

(a) **IN GENERAL.**—Section 913 (relating to deduction for certain expenses of living abroad) is hereby repealed.

(b) **CONFORMING AMENDMENTS.**—

(1) The table of sections for subpart B of part III of subchapter N of chapter 1 is amended by striking out the item relating to section 913.

(2) Section 62 (relating to definition of adjusted gross income) is amended by striking out paragraph (14) and redesignating paragraphs (15) and (16) as paragraphs (14) and (15), respectively.

(3) Subparagraph (C) of section 43(c)(1) (relating to earned income) is amended—

(A) by striking out "913," in the caption thereof,

(B) by striking out clause (ii), and

(C) by redesignating clause (iii) as clause (ii).

(4) Subsection (k) of section 1034 (relating to rollover of gain on sale of principal residence) is amended by striking out "section 913(j)(1)(B)" and inserting in lieu thereof "section 911(d)(3)".

(5) Section 3401 (relating to the definition of wages) is amended by striking out paragraph (18) and redesignating paragraphs (19) and (20) as paragraphs (18) and (19), respectively.

(6) Subparagraph (B) of section 6091(b)(1) (relating to place for filing returns and other documents) is amended by striking out "section 913 (relating to deduction for certain expenses of living abroad)".

**SEC. 113. EMPLOYEES LIVING IN CAMPS.**

Section 119 (relating to meals or lodging furnished for the convenience of the employer) is amended by adding at the end thereof the following new subsection:

"(c) **EMPLOYEES LIVING IN CERTAIN CAMPS.**—

"(1) **IN GENERAL.**—In the case of an individual who is furnished lodging in a camp located in a foreign country by or on behalf of his employer, such camp shall be considered to be part of the business premises of the employer.

"(2) **CAMP.**—For purposes of this section, a camp constitutes lodging which is—

"(A) provided by or on behalf of the employer for the convenience of the employer because the place at which such individual renders services is in a remote area where satisfactory housing is not available on the open market,

"(B) located, as near as practicable, in the vicinity of the place at which such individual renders services, and

“(C) furnished in a common area (or enclave) which is not available to the public and which normally accommodates 10 or more employees.”

**SEC. 114. REPORTS BY SECRETARY.**

Section 208 of the Foreign Earned Income Act of 1978 is amended to read as follows:

**“SEC. 208. REPORTS BY SECRETARY.**

“(a) **GENERAL RULE.**—As soon as practicable after the date of the enactment of the Economic Recovery Tax Act of 1981, and as soon as practicable after the close of each fourth calendar year thereafter, the Secretary of the Treasury shall transmit a report to the Committee on Ways and Means of the House of Representatives and to the Committee on Finance of the Senate on the operation and effects of sections 911 and 912 of the Internal Revenue Code of 1954.

“(b) **INFORMATION FROM FEDERAL AGENCIES.**—Each agency of the Federal Government which pays allowances excludable from gross income under section 912 of such Code shall furnish to the Secretary of the Treasury such information as he determines to be necessary to carry out his responsibility under subsection (a).”

**SEC. 115. EFFECTIVE DATE.**

The amendments made by this subtitle (other than section 114) shall apply with respect to taxable years beginning after December 31, 1981.

## **Subtitle C—Miscellaneous Provisions**

**SEC. 121. DEDUCTION FOR CHARITABLE CONTRIBUTIONS TO BE ALLOWED FOR INDIVIDUALS WHO DO NOT ITEMIZE DEDUCTIONS.**

(a) **IN GENERAL.**—Section 170 (relating to charitable, etc., contributions and gifts) 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) RULE FOR NONITEMIZATION OF DEDUCTIONS.—**

“(1) **IN GENERAL.**—In the case of an individual who does not itemize his deductions for the taxable year, the applicable percentage of the amount allowable under subsection (a) for the taxable year shall be taken into account as a direct charitable deduction under section 63.

“(2) **APPLICABLE PERCENTAGE.**—For purposes of paragraph (1), the applicable percentage shall be determined under the following table:

<b>“For taxable years beginning in—</b>	<b>The applicable percentage is—</b>
1982, 1983 or 1984 .....	25
1985.....	50
1986 or thereafter .....	100.

“(3) **LIMITATION FOR TAXABLE YEARS BEGINNING BEFORE 1985.**—In the case of a taxable year beginning before 1985, the portion of the amount allowable under subsection (a) to which the applicable percentage shall be applied—

“(A) shall not exceed \$100 for taxable years beginning in 1982 or 1983, and

“(B) shall not exceed \$300 for taxable years beginning in 1984.

*In the case of a married individual filing a separate return, the limit under subparagraph (A) shall be \$50, and the limit under subparagraph (B) shall be \$150.*

*“(4) TERMINATION.—The provisions of this subsection shall not apply to contributions made after December 31, 1986.”*

**(b) DEFINITION OF TAXABLE INCOME.—**

*(1) IN GENERAL.—Paragraph (1) of section 63(b) (relating to individuals) is amended—*

*(A) by striking out “and” at the end of subparagraph (A), and*

*(B) by inserting after subparagraph (B) the following new subparagraph:*

*“(C) the direct charitable deduction, and”.*

*(2) DIRECT CHARITABLE DEDUCTION DEFINED.—Section 63 (defining taxable income) is amended by adding at the end thereof the following new subsection:*

*“(i) DIRECT CHARITABLE DEDUCTION.—For purposes of this section, the term ‘direct charitable deduction’ means that portion of the amount allowable under section 170(a) which is taken as a direct charitable deduction for the taxable year under section 170(i).”*

**(c) CONFORMING AMENDMENTS.—**

*(1) Paragraph (1) of section 57(b) (relating to adjusted itemized deductions) is amended by inserting “without regard to paragraph (3) thereof” after “section 63(f)”.*

*(2) Subsection (f) of section 63 (relating to itemized deductions) is amended—*

*(A) by striking out “and” at the end of paragraph (1),*

*(B) by striking out the period at the end of paragraph (2) and inserting in lieu thereof “, and”, and*

*(C) by adding at the end thereof the following new paragraph:*

*“(3) the direct charitable deduction.”*

*(3) Subparagraph (A) of section 3(a)(4) (relating to imposition of tax table tax) is amended to read as follows:*

*“(A) reduced by the sum of—*

*“(i) the excess itemized deductions, and*

*“(ii) the direct charitable deduction, and”.*

*(d) EFFECTIVE DATE.—The amendments made by this section shall apply to contributions made after December 31, 1981, in taxable years beginning after such date.*

**SEC. 122. 18-MONTH PERIODS FOR ROLLOVER OF PRINCIPAL RESIDENCE INCREASED TO 2 YEARS.**

*(a) IN GENERAL.—Section 1034 (relating to rollover of gain on sale of principal residence) is amended by striking out “18 months” each place it appears and inserting in lieu thereof “2 years”.*

**(b) CONFORMING AMENDMENTS.—**

*(1) Paragraph (4) of section 1034(c) is amended by striking out “18-month” and inserting in lieu thereof “2-year”.*

*(2) Paragraph (5) of section 1034(c) is hereby repealed.*

*(c) EFFECTIVE DATE.—The amendments made by this section shall apply to old residences (within the meaning of section 1034 of the Internal Revenue Code of 1954) sold or exchanged—*

*(1) after July 20, 1981, or*

(2) on or before such date, if the rollover period under such section (determined without regard to the amendments made by this section) expires on or after such date.

**SEC. 123. ONE-TIME EXCLUSION OF GAIN INCREASED TO \$125,000.**

(a) **IN GENERAL.**—Paragraph (1) of section 121(b) (relating to one-time exclusion of gain from sale of principal residence by individual who has attained age 55) is amended by striking out “\$100,000 (\$50,000” and inserting in lieu thereof “\$125,000 (\$62,500”.

(b) **EFFECTIVE DATE.**—The amendment made by this section shall apply to residences sold or exchanged after July 20, 1981.

**SEC. 124. INCREASES IN CREDIT ALLOWABLE FOR EXPENSES FOR HOUSEHOLD AND DEPENDENT CARE SERVICES NECESSARY FOR GAINFUL EMPLOYMENT.**

(a) **INCREASE IN PERCENTAGE OF EXPENSES ALLOWED AS CREDIT.**—Subsection (a) of section 44A (relating to expenses for household and dependent care services necessary for gainful employment) is amended to read as follows:

“(a) **ALLOWANCE OF CREDIT.**—

“(1) **IN GENERAL.**—In the case of an individual who maintains a household which includes as a member one or more qualifying individuals (as defined in subsection (c)(1)), there shall be allowed as a credit against the tax imposed by this chapter for the taxable year an amount equal to the applicable percentage of the employment-related expenses (as defined in subsection (c)(2)) paid by such individual during the the taxable year.

“(2) **APPLICABLE PERCENTAGE DEFINED.**—For purposes of paragraph (1), the term ‘applicable percentage’ means 30 percent reduced (but not below 20 percent) by 1 percentage point for each \$2,000 (or fraction thereof) by which the taxpayer’s adjusted gross income for the taxable year exceeds \$10,000.”

(b) **INCREASES IN DOLLAR LIMITS ON AMOUNT CREDITABLE.**—

(1) **IN GENERAL.**—Subsection (d) of section 44A (relating to dollar limit on amount creditable) is amended—

(A) by striking out “\$2,000” and inserting in lieu thereof “\$2,400”, and

(B) by striking out “\$4,000” and inserting in lieu thereof “\$4,800”.

(2) **CONFORMING AMENDMENTS.**—Paragraph (2) of section 44A(e) (relating to earned income limitation) is amended—

(A) by striking out “\$166” and inserting in lieu thereof “\$200”, and

(B) by striking out “\$333” and inserting in lieu thereof “\$400”.

(c) **CREDIT ALLOWED FOR CERTAIN SERVICES OUTSIDE THE TAXPAYER’S HOUSEHOLD.**—Subparagraph (B) of section 44A(c)(2) is amended to read as follows:

“(B) **EXCEPTION.**—Employment-related expenses described in subparagraph (A) which are incurred for services outside the taxpayer’s household shall be taken into account only if incurred for the care of—

“(i) a qualifying individual described in paragraph (1)(A), or

“(ii) a qualifying individual (not described in paragraph (1)(A)) who regularly spends at least 8 hours each day in the taxpayer’s household.”

**(d) DAY CARE CENTERS MUST MEET STATE LAW REQUIREMENTS.**—Paragraph (2) of section 44A(c) (defining employment-related expenses) is amended by adding at the end thereof the following new subparagraphs:

“(C) **DEPENDENT CARE CENTERS.**—Employment-related expenses described in subparagraph (A) which are incurred for services provided outside the taxpayer’s household by a dependent care center (as defined in subparagraph (D)) shall be taken into account only if—

“(i) such center complies with all applicable laws and regulations of a State or unit of local government, and

“(ii) the requirements of subparagraph (B) are met.

“(D) **DEPENDENT CARE CENTER DEFINED.**—For purposes of this paragraph, the term ‘dependent care center’ means any facility which—

“(i) provides care for more than six individuals (other than individuals who reside at the facility), and

“(ii) receives a fee, payment, or grant for providing services for any of the individuals (regardless of whether such facility is operated for profit).”

**(e) EXCLUSION OF DEPENDENT CARE ASSISTANCE FROM THE INCOME OF EMPLOYEES.**

**(1) IN GENERAL.**—Part III of subchapter B of chapter 1 (as amended by section 301) is amended by redesignating section 129 as section 130 and inserting after section 128 the following new section:

**“SEC. 129. DEPENDENT CARE ASSISTANCE PROGRAMS.**

“(a) **IN GENERAL.**—Gross income of an employee does not include amounts paid or incurred by the employer for dependent care assistance provided to such employee if the assistance is furnished pursuant to a program which is described in subsection (d).

“(b) **EARNED INCOME LIMITATION.**—

“(1) **IN GENERAL.**—The amount excluded from the income of an employee under subsection (a) for any taxable year shall not exceed—

“(A) in the case of an employee who is not married at the close of such taxable year, the earned income of such employee for such taxable year, or

“(B) in the case of an employee who is married at the close of such taxable year, the lesser of—

“(i) the earned income of such employee for such taxable year, or

“(ii) the earned income of the spouse of such employee for such taxable year.

“(2) **SPECIAL RULE FOR CERTAIN SPOUSES.**—For purposes of paragraph (1), the provisions of section 44A(e)(2) shall apply in determining the earned income of a spouse who is a student or incapable of caring for himself.

“(c) **PAYMENTS TO RELATED INDIVIDUALS.**—No amount paid or incurred during the taxable year of an employee by an employer in providing dependent care assistance to such employee shall be ex-

cluded under subsection (a) if such amount was paid or incurred to an individual—

“(1) with respect to whom, for such taxable year, a deduction is allowable under section 151(e) (relating to personal exemptions for dependents) to such employee or the spouse of such employee, or

“(2) who is a child of such employee (within the meaning of section 151(e)(3)) under the age of 19 at the close of such taxable year.

“(d) **DEPENDENT CARE ASSISTANCE PROGRAM.**—

“(1) **IN GENERAL.**—For purposes of this section a dependent care assistance program is a separate written plan of an employer for the exclusive benefit of his employees to provide such employees with dependent care assistance which meets the requirements of paragraphs (2) through (6) of this subsection.

“(2) **ELIGIBILITY.**—The program shall benefit employees who qualify under a classification set up by the employer and found by the Secretary not to be discriminatory in favor of employees who are officers, owners, or highly compensated, or their dependents. For purposes of this paragraph, there shall be excluded from consideration employees not included in the program who are included in a unit of employees covered by an agreement which the Secretary of Labor finds to be a collective bargaining agreement between employee representatives and one or more employers, if there is evidence that dependent care benefits were the subject of good faith bargaining between such employee representatives and such employer or employers.

“(3) **PRINCIPAL SHAREHOLDERS OR OWNERS.**—Not more than 25 percent of the amounts paid or incurred by the employer for dependent care assistance during the year may be provided for the class of individuals who are shareholders or owners (or their spouses or dependents), each of whom (on any day of the year) owns more than 5 percent of the stock or of the capital or profits interest in the employer.

“(4) **NO FUNDING REQUIRED.**—A program referred to in the paragraph (1) is not required to be funded.

“(5) **NOTIFICATION OF ELIGIBLE EMPLOYEES.**—Reasonable notification of the availability and terms of the program shall be provided to eligible employees.

“(6) **STATEMENT OF EXPENSES.**—The plan shall furnish to an employee, on or before January 31, a written statement showing the amounts paid or expenses incurred by the employer in providing dependent care assistance to such employee during the previous calendar year.

“(e) **DEFINITIONS AND SPECIAL RULES.**—For purposes of this section—

“(1) **DEPENDENT CARE ASSISTANCE.**—The term ‘dependent care assistance’ means the payment of, or provision of, those services which if paid for by the employee would be considered employment-related expenses under section 44A(c)(2) (relating to expenses for household and dependent care services necessary for gainful employment).

“(2) **EARNED INCOME.**—The term ‘earned income’ shall have the meaning given such term in section 43(c)(2), but such term

shall not include any amounts paid or incurred by an employer for dependent care assistance to an employee.

“(3) **EMPLOYEE.**—The term ‘employee’ includes, for any year, an individual who is an employee within the meaning of section 401(c)(1) (relating to self-employed individuals).

“(4) **EMPLOYER.**—An individual who owns the entire interest in an unincorporated trade or business shall be treated as his own employer. A partnership shall be treated as the employer of each partner who is an employee within the meaning of paragraph (3).

“(5) **ATTRIBUTION RULES.**—

“(A) **OWNERSHIP OF STOCK.**—Ownership of stock in a corporation shall be determined in accordance with the rules provided under subsections (d) and (e) of section 1563 (without regard to section 1563(e)(3)(C)).

“(B) **INTEREST IN UNINCORPORATED TRADE OR BUSINESS.**—The interest of an employee in a trade or business which is not incorporated shall be determined in accordance with regulations prescribed by the Secretary, which shall be based on principles similar to the principles which apply in the case of subparagraph (A).

“(6) **UTILIZATION TEST NOT APPLICABLE.**—A dependent care assistance program shall not be held or considered to fail to meet any requirements of subsection (d) merely because of utilization rates for the different types of assistance made available under the program.

“(7) **DISALLOWANCE OF EXCLUDED AMOUNTS AS CREDIT OR DEDUCTION.**—No deduction or credit shall be allowed under any other section of this chapter for any amount excluded from income by reason of this section.”

(2) **EXCLUSION FROM WAGES.**—

(A) **EMPLOYMENT TAXES AND COLLECTION OF INCOME TAX.**—Subtitle C is amended by striking out “section 127” in section 3121(a)(18) (relating to the Federal Insurance Contributions Act), section 3306(b)(13) (relating to the Federal Unemployment Tax Act), and section 3401(a)(19) (relating to collection of income at source on wages) and inserting in lieu thereof “section 127 or 129”.

(B) **SOCIAL SECURITY ACT.**—Subsection (q) of section 209 of the Social Security Act (defining wages) is amended by striking out “section 127” and inserting in lieu thereof “section 127 or 129”.

(f) **EFFECTIVE DATE.**—

(1) Except as provided in paragraph (2), the amendments made by this section shall apply to taxable years beginning after December 31, 1981.

(2) The amendments made by subsection (e)(2) shall apply to remuneration paid after December 31, 1981.

**SEC. 125. DEDUCTION FOR ADOPTION EXPENSES PAID BY AN INDIVIDUAL.**

(a) **IN GENERAL.**—Part VII of subchapter B of chapter 1 (relating to additional itemized deductions for individuals), as amended by section 103, is amended by redesignating section 222 as section 223 and by inserting after section 221 the following new section:

**“SEC. 222. ADOPTION EXPENSES.**

**“(a) ALLOWANCE OF DEDUCTION.—***In the case of an individual, there shall be allowed as a deduction for the taxable year the amount of the qualified adoption expenses paid or incurred by the taxpayer during such taxable year.*

**“(b) LIMITATIONS.—**

**“(1) MAXIMUM DOLLAR AMOUNT.—***The aggregate amount of adoption expenses which may be taken into account under subsection (a) with respect to the adoption of a child shall not exceed \$1,500.*

**“(2) DENIAL OF DOUBLE BENEFIT.—**

**“(A) IN GENERAL.—***No deduction shall be allowable under subsection (a) for any expense for which a deduction or credit is allowable under any other provision of this chapter.*

**“(B) GRANTS.—***No deduction shall be allowable under subsection (a) for any expenses paid from any funds received under any Federal, State, or local program.*

**“(c) DEFINITIONS.—***For purposes of this section—*

**“(1) QUALIFIED ADOPTION EXPENSES.—***The term ‘qualified adoption expenses’ means reasonable and necessary adoption fees, court costs, attorney fees, and other expenses which are directly related to the legal adoption of a child with special needs by the taxpayer and which are not incurred in violation of State or Federal law.*

**“(2) CHILD WITH SPECIAL NEEDS.—***The term ‘child with special needs’ means a child with respect to whom adoption assistance payments are made under section 473 of the Social Security Act.”*

**(b) CONFORMING AMENDMENT.—***The table of sections for such part VII is amended by striking out the item relating to section 222 and inserting in lieu thereof the following:*

*“Sec. 222. Adoption expenses.*

*“Sec. 223. Cross references.”*

**(c) EFFECTIVE DATE.—***The amendments made by this section shall apply to taxable years beginning after December 31, 1980.*

**SEC. 126. MAXIMUM RATE OF IMPUTED INTEREST FOR SALE OF LAND BETWEEN RELATED PERSONS.**

**(a) GENERAL RULE.—***Section 483 (relating to interest on certain deferred payments) is amended by adding at the end thereof the following new subsection:*

**“(g) MAXIMUM RATE OF INTEREST ON CERTAIN TRANSFERS OF LAND BETWEEN RELATED PARTIES.—**

**“(1) IN GENERAL.—***In the case of any qualified sale, the maximum interest rate used in determining the total unstated interest rate under the regulations under subsection (b) shall not exceed 7 percent, compounded semiannually.*

**“(2) QUALIFIED SALE.—***For purposes of this subsection, the term ‘qualified sale’ means any sale or exchange of land by an individual to a member of such individual’s family (within the meaning of section (267(c)(4)).*

**“(3) \$500,000 LIMITATION.—***Paragraph (1) shall not apply to any qualified sale between individuals made during any calendar year to the extent that the sales price for such sale (when added to the aggregate sales price for prior qualified sales be-*



tween such individuals during the calendar year) exceeds \$500,000.

**"(4) NONRESIDENT ALIEN INDIVIDUALS.**—This section shall not apply to any sale or exchange if any party to such sale or exchange is a nonresident alien individual."

**(b) EFFECTIVE DATE.**—The amendment made by subsection (a) shall apply to payments made after June 30, 1981, pursuant to sales or exchanges after such date.

**SEC. 127. STATE LEGISLATORS TRAVEL EXPENSES AWAY FROM HOME.**

**(a) IN GENERAL.**—Section 162 (relating to trade or business expenses) is amended by redesignating subsection (h) as subsection (i) and by inserting after subsection (g) the following new subsection:

**"(h) STATE LEGISLATORS' TRAVEL EXPENSES AWAY FROM HOME.**—

**"(1) IN GENERAL.**—For purposes of subsection (a), in the case of any individual who is a State legislator at any time during the taxable year and who makes an election under this subsection for the taxable year—

**"(A)** the place of residence of such individual within the legislative district which he represented shall be considered his home,

**"(B)** he shall be deemed to have expended for living expenses (in connection with his trade or business as a legislator) an amount equal to the sum of the amounts determined by multiplying each legislative day of such individual during the taxable year by the greater of—

**"(i)** the amount generally allowable with respect to such day to employees of the State of which he is a legislator for per diem while away from home, to the extent such amount does not exceed 110 percent of the amount described in clause (ii) with respect to such day, or

**"(ii)** the amount generally allowable with respect to such day to employees of the executive branch of the Federal Government for per diem while away from home but serving in the United States, and

**"(C)** he shall be deemed to be away from home in the pursuit of a trade or business on each legislative day.

**"(2) LEGISLATIVE DAYS.**—For purposes of paragraph (1), a legislative day during any taxable year for any individual shall be any day during such year on which—

**"(A)** the legislature was in session (including any day in which the legislature was not in session for a period of 4 consecutive days or less), or

**"(B)** the legislature was not in session but the physical presence of the individual was formally recorded at a meeting of a committee of such legislature.

**"(3) ELECTION.**—An election under this subsection for any taxable year shall be made at such time and in such manner as the Secretary shall by regulations prescribe.

**"(4) SECTION NOT TO APPLY TO LEGISLATORS WHO RESIDE NEAR CAPITOL.**—For taxable years beginning after December 31, 1980, this subsection shall not apply to any legislator whose place of residence within the legislative district which he represents is 50 or fewer miles from the capitol building of the State."

(b) The amendment made by subsection (a) shall apply to taxable years beginning on or after January 1, 1976.

**SEC. 128. RATES OF TAX FOR PRINCIPAL CAMPAIGN COMMITTEES.**

(a) *IN GENERAL.*—Section 527 (relating to political organizations) is amended by adding at the end thereof the following new subsection:

“(h) **SPECIAL RULE FOR PRINCIPAL CAMPAIGN COMMITTEES.**—

“(1) *IN GENERAL.*—In the case of a political organization which is a principal campaign committee, paragraph (1) of subsection (b) shall be applied by substituting ‘the appropriate rates’ for ‘the highest rate’.

“(2) **PRINCIPAL CAMPAIGN COMMITTEE DEFINED.**—

“(A) *IN GENERAL.*—For purposes of this subsection, the term ‘principal campaign committee’ means the political committee designated by a candidate for Congress as his principal campaign committee for purposes of—

“(i) section 302(e) of the Federal Election Campaign Act of 1971 (2 U.S.C. 432(e)), and

“(ii) this subsection.

“(B) *DESIGNATION.*—A candidate may have only 1 designation in effect under subparagraph (A)(ii) at any time and such designation—

“(i) shall be made at such time and in such manner as the Secretary may prescribe by regulations, and

“(ii) once made, may be revoked only with the consent of the Secretary.”

(b) *EFFECTIVE DATE.*—The amendments made by this section shall apply to taxable years beginning after December 31, 1981.

## **TITLE II—BUSINESS INCENTIVE PROVISIONS**

### **Subtitle A—Cost Recovery Provisions**

**SEC. 201. ACCELERATED COST RECOVERY SYSTEM.**

(a) *IN GENERAL.*—Part VI of subchapter B of chapter 1 (relating to itemized deductions for individuals and corporations) is amended by inserting after section 167 the following new section:

**“SEC. 168. ACCELERATED COST RECOVERY SYSTEM.**

“(a) *ALLOWANCE OF DEDUCTION.*—There shall be allowed as a deduction for any taxable year the amount determined under this section with respect to recovery property.

“(b) *AMOUNT OF DEDUCTION.*—

“(1) *IN GENERAL.*—Except as otherwise provided in this section, the amount of the deduction allowable by subsection (a) for any taxable year shall be the aggregate amount determined by applying to the unadjusted basis of recovery property the applicable percentage determined in accordance with the following tables:

“(A) **FOR PROPERTY PLACED IN SERVICE AFTER DECEMBER 31, 1980, AND BEFORE JANUARY 1, 1985.**—

<i>"If the recovery year is.</i>	<i>The applicable percentage for the class of property is.</i>			
	<i>3-year</i>	<i>5-year</i>	<i>10-year</i>	<i>15-year public utility</i>
1 .....	25	15	8	5
2 .....	38	22	14	10
3 .....	37	21	12	9
4 .....		21	10	8
5 .....		21	10	7
6 .....			10	7
7 .....			9	6
8 .....			9	6
9 .....			9	6
10 .....			9	6
11 .....				6
12 .....				6
13 .....				6
14 .....				6
15 .....				6

**"(B) FOR PROPERTY PLACED IN SERVICE IN 1985.—**

<i>"If the recovery year is.</i>	<i>The applicable percentage for the class of property is:</i>			
	<i>3-year</i>	<i>5-year</i>	<i>10-year</i>	<i>15-year public utility</i>
1 .....	29	18	9	6
2 .....	47	33	19	12
3 .....	24	25	16	12
4 .....		16	14	11
5 .....		8	12	10
6 .....			10	9
7 .....			8	8
8 .....			6	7
9 .....			4	6
10 .....			2	5
11 .....				4
12 .....				4
13 .....				3
14 .....				2
15 .....				1

**"(C) FOR PROPERTY PLACED IN SERVICE AFTER DECEMBER 31, 1985.—**

<i>"If the recovery year is:</i>	<i>The applicable percentage for the class of property is.</i>			
	<i>3-year</i>	<i>5-year</i>	<i>10-year</i>	<i>15-year public utility</i>
1 .....	33	20	10	7
2 .....	45	32	18	12

"If the recovery year is:	The applicable percentage for the class of property is:			
	3-year	5-year	10-year	15-year public utility
3.....	22	24	16	12
4.....		16	14	11
5.....		8	12	10
6.....			10	9
7.....			8	8
8.....			6	7
9.....			4	6
10.....			2	5
11.....				4
12.....				3
13.....				3
14.....				2
15.....				1.

**"(2) 15-YEAR REAL PROPERTY.—**

**"(A) IN GENERAL.—**In the case of 15-year real property, the applicable percentage shall be determined in accordance with a table prescribed by the Secretary. In prescribing such table, the Secretary shall—

**"(i)** assign to the property a 15-year recovery period, and

**"(ii)** assign percentages generally determined in accordance with use of the 175 percent declining balance method (200 percent declining balance method in the case of low-income housing), switching to the method described in section 167(b)(1) at a time to maximize the deduction allowable under subsection (a).

For purposes of this subparagraph, the applicable percentage in the taxable year in which the property is placed in service shall be determined on the basis of the number of months in such year during which the property was in service. For purposes of this subparagraph, the term 'low-income housing' means property described in clause (i), (ii), (iii), or (iv) of section 1250(a)(1)(B).

**"(B) SPECIAL RULE FOR YEAR OF DISPOSITION.—**In the case of a disposition of 15-year real property, the deduction allowable under subsection (a) for the taxable year in which the disposition occurs shall reflect only the months during such year the property was in service.

**"(3) ELECTION OF DIFFERENT RECOVERY PERCENTAGE.—**

**"(A) IN GENERAL.—**Except as provided in subsection (f)(2), in lieu of any applicable percentage under paragraphs (1) and (2), the taxpayer may elect, with respect to one or more classes of recovery property placed in service during the taxable year, the applicable percentage determined by use of the straight line method over the recovery period elected by the taxpayer in accordance with the following table:

<b>"In the case of:</b>	<b>The taxpayer may elect a recovery period of:</b>
3-year property.....	The present class life, 5 or 12 years.
5-year property.....	The present class life, 12 or 25 years.
10-year property.....	The present class life, 25 or 35 years.
15-year real property.....	35 or 45 years.
15-year public utility property.	The present class life, 35 or 45 years.

**“(B) OPERATING RULES.—**

**“(i) IN GENERAL.—**Except as provided in clause (ii), the taxpayer may elect under subparagraph (A) only a single percentage for property in any class of recovery property placed in service during the taxable year. The percentage so elected shall apply to all property in such class placed in service during such taxable year and shall apply throughout the recovery period elected for such property.

**“(ii) REAL PROPERTY.—**In the case of 15-year real property the taxpayer shall make the election under subparagraph (A) on a property-by-property basis.

**“(iii) CONVENTION.—**Under regulations prescribed by the Secretary, the half-year convention shall apply to any election with respect to any recovery property (other than 15-year real property) with respect to which an election is made under this paragraph.

**“(c) RECOVERY PROPERTY.—**For purposes of this title—

**“(1) RECOVERY PROPERTY DEFINED.—**Except as provided in subsection (e), the term ‘recovery property’ means tangible property of a character subject to the allowance for depreciation—

**“(A) used in a trade or business, or**

**“(B) held for the production of income.**

**“(2) CLASSES OF RECOVERY PROPERTY.—**Each item of recovery property shall be assigned to one of the following classes of property:

**“(A) 3-YEAR PROPERTY.—**The term ‘3-year property’ means section 1245 class property—

**“(i) with a present class life of 4 years or less; or**

**“(ii) used in connection with research and experimentation.**

**“(B) 5-YEAR PROPERTY.—**The term ‘5-year property’ means recovery property which is section 1245 class property and which is not 3-year property, 10-year property, or 15-year public utility property.

**“(C) 10-YEAR PROPERTY.—**The term ‘10-year property’ means—

**“(i) public utility property (other than section 1250 class property or 3-year property) with a present class life of more than 18 years but not more than 25 years; and**

**“(ii) section 1250 class property with a present class life of 12.5 years or less.**

**“(D) 15-YEAR REAL PROPERTY.—**The term ‘15-year real property’ means section 1250 class property which does not have a present class life of 12.5 years or less.

**“(E) 15-YEAR PUBLIC UTILITY PROPERTY.—**The term ‘15-year public utility property’ means public utility property (other than section 1250 class property or 3-year property) with a present class life of more than 25 years.

**“(d) UNADJUSTED BASIS; ADJUSTMENTS.—**

**“(1) UNADJUSTED BASIS DEFINED.—**

**“(A) IN GENERAL.—**For purposes of this section, the term ‘unadjusted basis’ means the excess of—

“(i) the basis of the property determined under part II of subchapter O of chapter 1 for purposes of determining gain (determined without regard to the adjustments described in paragraph (2) or (3) of section 1016(a)), over

“(ii) the sum of—

“(I) that portion of the basis for which the taxpayer properly elects amortization (including the deduction allowed under section 167(k)) in lieu of depreciation, and

“(II) that portion of the basis which the taxpayer properly elects to treat as an expense under section 179.

“(B) TIME FOR TAKING BASIS INTO ACCOUNT.—

“(i) IN GENERAL.—The unadjusted basis of property shall be first taken into account under subsection (b) for the taxable year in which the property is placed in service.

“(ii) REDETERMINATIONS.—The Secretary shall by regulation provide for the method of determining the deduction allowable under subsection (a) for any taxable year (and succeeding taxable years) in which the basis is redetermined (including any reduction under section 1017).

“(2) DISPOSITIONS.—

“(A) MASS ASSET ACCOUNTS.—In lieu of recognizing gain or loss under this chapter, a taxpayer who maintains one or more mass asset accounts of recovery property may, under regulations prescribed by the Secretary, elect to include in income all proceeds realized on the disposition of such property.

“(B) ADJUSTMENT TO BASIS.—Except as provided under regulations prescribed by the Secretary under subsection (f)(7), if any recovery property (other than 15-year real property or property with respect to which an election under subparagraph (A) is made) is disposed of, the unadjusted basis of such property shall cease to be taken into account in determining any recovery deduction allowable under subsection (a) as of the beginning of the taxable year in which such disposition occurs.

“(C) DISPOSITION INCLUDES RETIREMENT.—For purposes of this subparagraph, the term ‘disposition’ includes retirement.

“(e) PROPERTY EXCLUDED FROM APPLICATION OF SECTION.—For purposes of this section—

“(1) PROPERTY PLACED IN SERVICE BEFORE JANUARY 1, 1981.—The term ‘recovery property’ does not include property placed in service by the taxpayer before January 1, 1981.

“(2) CERTAIN METHODS OF DEPRECIATION.—The term ‘recovery property’ does not include property if—

“(A) the taxpayer elects to exclude such property from the application of this section, and

“(B) for the first taxable year for which a deduction would (but for this election) be allowable under this section with respect to such property in the hands of the taxpayer,

*the property is properly depreciated under the unit-of-production method or any method of depreciation not expressed in a term of years (other than the retirement-replacement-betterment method).*

**“(3) SPECIAL RULE FOR CERTAIN PUBLIC UTILITY PROPERTY.—**

**“(A) IN GENERAL.—***The term ‘recovery property’ does not include public utility property (within the meaning of section 167(l)(3)(A)) if the taxpayer does not use a normalization method of accounting.*

**“(B) USE OF NORMALIZATION METHOD DEFINED.—***For purposes of subparagraph (A), in order to use a normalization method of accounting with respect to any public utility property—*

*“(i) the taxpayer must, in computing its tax expense for purposes of establishing its cost of service for rate-making purposes and reflecting operating results in its regulated books of account, use a method of depreciation with respect to such property that is the same as, and a depreciation period for such property that is no shorter than, the method and period used to compute its depreciation expense for such purposes; and*

*“(ii) if the amount allowable as a deduction under this section with respect to such property differs from the amount that would be allowable as a deduction under section 167 (determined without regard to section 167(l)) using the method (including the period, first and last year convention, and salvage value) used to compute regulated tax expense under subparagraph (B)(i), the taxpayer must make adjustments to a reserve to reflect the deferral of taxes resulting from such difference.*

**“(C) PUBLIC UTILITY PROPERTY WHICH IS NOT RECOVERY PROPERTY.—***In the case of public utility property which, by reason of this paragraph, is not treated as recovery property, the allowance for depreciation under section 167(a) shall be an amount computed using the method and period referred to in subparagraph (B)(i).*

**“(4) CERTAIN TRANSACTIONS IN PROPERTY PLACED IN SERVICE BEFORE 1986.—**

**“(A) SECTION 1245 CLASS PROPERTY.—***The term ‘recovery property’ does not include section 1245 class property acquired by the taxpayer after December 31, 1980, if—*

*“(i) the property was owned or used at any time during 1980 by the taxpayer or a related person,*

*“(ii) the property is acquired from a person who owned such property at any time during 1980, and, as part of the transaction, the user of such property does not change,*

*“(iii) the taxpayer leases such property to a person (or a person related to such person) who owned or used such property at any time during 1980, or*

*“(iv) the property is acquired in a transaction as part of which the user of such property does not change and the property is not recovery property in the hands of the*

person from which the property is so acquired by reason of clause (ii) or (iii).

For purposes of this subparagraph and subparagraph (B), property shall not be treated as owned before it is placed in service. For purposes of this subparagraph, whether the user of property changes as part of a transaction shall be determined in accordance with regulations prescribed by the Secretary.

**“(B) SECTION 1250 CLASS PROPERTY.**—The term ‘recovery property’ does not include section 1250 class property acquired by the taxpayer after December 31, 1980, if—

“(i) such property was owned by the taxpayer or by a related person at any time during 1980;

“(ii) the taxpayer leases such property to a person (or a person related to such person) who owned such property at any time during 1980; or

“(iii) such property is acquired in an exchange described in section 1031, 1033, 1038, or 1039 to the extent that the basis of such property includes an amount representing the adjusted basis of other property owned by the taxpayer or a related person during 1980.

**“(C) CERTAIN NONRECOGNITION TRANSACTIONS.**—The term ‘recovery property’ does not include property placed in service by the transferor or distributor before January 1, 1981, which is acquired by the taxpayer after December 31, 1980, in a transaction described in section 332, 351, 361, 371(a), 374(a), 721, or 731 (or such property acquired from the transferee or acquiring corporation in a transaction described in such section), to the extent that the basis of the property is determined by reference to the basis of the property in the hands of the transferor or distributor. In the case of property to which this subparagraph applies, rules similar to the rules described in section 381(c)(6) shall apply.

**“(D) RELATED PERSON DEFINED.**—Except as provided in subparagraph (E), for purposes of this paragraph a person (hereinafter referred to as the related person) is related to any person if—

“(i) the related person bears a relationship to such person specified in section 267(b) or section 707(b)(1), or

“(ii) the related person and such person are engaged in trades or businesses under common control (within the meaning of subsections (a) and (b) of section 52).

For purposes of clause (i), in applying section 267(b) and section 707(b)(1) ‘10 percent’ shall be substituted for ‘50 percent’. The determination of whether a person is related to another person shall be made as of the time the taxpayer acquires the property involved.

**“(E) LIQUIDATION OF SUBSIDIARY, ETC.**—For purposes of this paragraph, a corporation is not a related person to the taxpayer—

“(i) if such corporation is a distributing corporation in a transaction to which section 334(b)(2)(B) applies and the stock of such corporation referred to in such



subparagraph (B) was acquired by the taxpayer by purchase after December 31, 1980, or

“(ii) if such corporation is liquidated in a liquidation to which section 331(a) applies and the taxpayer (or a related person) by himself or together with 1 or more other persons acquires the stock of the liquidated corporation by purchase (meeting the requirements of section 334(b)(2)(B)) after December 31, 1980.

“(F) ANTI-AVOIDANCE RULE.—The term ‘recovery property’ does not include property acquired by the taxpayer after December 31, 1980, which, under regulations prescribed by the Secretary, is acquired in a transaction one of the principal purposes of which is to avoid the principles of paragraph (1) and this paragraph.

“(G) REDUCTION IN UNADJUSTED BASIS.—In the case of an acquisition of property described in subparagraph (B) or (C), the unadjusted basis of the property under subsection (d) shall be reduced to the extent that such property acquired is not recovery property.

“(H) SPECIAL RULES FOR PROPERTY PLACED IN SERVICE BEFORE CERTAIN PERCENTAGES TAKE EFFECT.—Under regulations prescribed by the Secretary—

“(i) rules similar to the rules of this paragraph shall be applied in determining whether the tables contained in subparagraph (B) or (C) of subsection (b)(1) apply with respect to recovery property, and

“(ii) if the tables contained in subparagraph (B) or (C) of subsection (b)(1) do not apply to such property by reason of clause (i), the deduction allowable under subsection (a) shall be computed—

“(I) In the case of a transaction described in subparagraph (C), under rules similar to the rules described in section 381(c)(6); and

“(II) in the case of a transaction otherwise described in this paragraph, under the recovery period and method (including rates prescribed under subsection (b)(1)) used by the person from whom the taxpayer acquired such property (or, where such person had no recovery method and period for such property, under the recovery period and method (including rates prescribed under subsection (b)(1)) used by the person which transferred such property to such person).

“(f) SPECIAL RULES FOR APPLICATION OF THIS SECTION.—For purposes of this section—

“(1) COMPONENTS OF SECTION 1250 CLASS PROPERTY.—

“(A) IN GENERAL.—Except as otherwise provided in this paragraph—

“(i) the deduction allowable under subsection (a) with respect to any component (which is section 1250 class property) of a building shall be computed in the same manner as the deduction allowable with respect to such building, and

“(ii) the recovery period for such component shall begin on the later of—

*“(I) the date such component is placed in service,  
or*

*“(II) the date on which the building is placed in service.*

*“(B) TRANSITIONAL RULE.—In the case of any building placed in service by the taxpayer before January 1, 1981, for purposes of applying subparagraph (A) to components of such buildings placed in service after December 31, 1980, the deduction allowable under subsection (a) with respect to such components shall be computed in the same manner as the deduction allowable with respect to the first such component placed in service after December 31, 1980. For purposes of the preceding sentence, the method of computing the deduction allowable with respect to such first component shall be determined as if it were a separate building.*

*“(C) EXCEPTION FOR SUBSTANTIAL IMPROVEMENTS.—*

*“(i) IN GENERAL.—For purposes of this paragraph, a substantial improvement shall be treated as a separate building.*

*“(ii) SUBSTANTIAL IMPROVEMENT.—For purposes of clause (i), the term ‘substantial improvement’ means the improvements added to capital account with respect to any building during any 24-month period, but only if the sum of the amounts added to such account during such period equals or exceeds 25 percent of the adjusted basis of the building (determined without regard to the adjustments provided in paragraphs (2) and (3) of section 1016(a)) as of the first day of such period.*

*“(iii) IMPROVEMENTS MUST BE MADE AFTER BUILDING IN SERVICE FOR 3 YEARS.—For purposes of this paragraph, the term ‘substantial improvement’ shall not include any improvement made before the date 3 years after the building was placed in service.*

*“(2) RECOVERY PROPERTY USED PREDOMINANTLY OUTSIDE THE UNITED STATES.—*

*“(A) IN GENERAL.—Except as provided in subparagraphs (B) and (C), in the case of recovery property which, during the taxable year, is used predominantly outside the United States, the recovery deduction for the taxable year shall be, in lieu of the amount determined under subsection (b), the amount determined by applying to the unadjusted basis of such property the applicable percentage determined under tables prescribed by the Secretary. For purposes of the preceding sentence, in prescribing such tables, the Secretary shall—*

*“(i) assign the property described in this subparagraph to classes in accordance with the present class life (or 12 years in the case of personal property with no present class life) of such property; and*

*“(ii) assign percentages (taking into account the half-year convention) determined in accordance with use of the method of depreciation described in section 167(b)(2), switching to the method described in section*

167(b)(1) at a time to maximize the deduction allowable under subsection (a).

**“(B) REAL PROPERTY.—**

**“(i) IN GENERAL.—**Except as provided in subparagraph (C), in the case of 15-year real property which, during the taxable year, is predominantly used outside the United States, the recovery deduction for the taxable year shall be, in lieu of the amount determined under subsection (b), the amount determined by applying to the unadjusted basis of such property the applicable percentage determined under tables prescribed by the Secretary. For purposes of the preceding sentence in prescribing such tables, the Secretary shall—

**“(I) assign to the property described in this subparagraph a 35-year recovery period; and**

**“(II) assign percentages (taking into account the last sentence of subsection (b)(2)(A)) determined in accordance with use of the method of depreciation described in section 167(j)(1)(B), switching to the method described in section 167(b)(1) at a time to maximize the deduction allowable under subsection (a).**

**“(ii) SPECIAL RULE FOR DISPOSITION.—**In the case of a disposition of 15-year real property described in clause (i), subsection (b)(2)(B) shall apply.

**“(C) ELECTION OF DIFFERENT RECOVERY PERCENTAGE.—**

**“(i) GENERAL RULE.—**The taxpayer may elect, with respect to one or more classes of recovery property described in this paragraph, to determine the applicable percentage under this paragraph by use of the straight-line method over the recovery period determined in accordance with the following table:

<b>“In the case of:</b>	<b>The taxpayer may elect a recovery period of:</b>
3-year property.....	The present class life, 5 or 12 years.
5-year property.....	The present class life, 12 or 25 years.
10-year property.....	The present class life, 25 or 35 years.
15-year real property.....	35 or 45 years.
15-year public utility property.	The present class life, 35 or 45 years.

**“(ii) OPERATING RULES.—**

**“(I) PERIOD ELECTED BY TAXPAYER.—**Except as provided in subclause (II), the taxpayer may elect under clause (i) for any taxable year only a single recovery period for recovery property described in this paragraph which is placed in service during such taxable year, which has the same present

class life, and which is in the same class under subsection (c)(2). The period so elected shall not be shorter than such present class life.

“(II) REAL PROPERTY.—In the case of 15-year real property, the election under clause (i) shall be made on a property-by-property basis.

“(D) DETERMINATION OF PROPERTY USED PREDOMINANTLY OUTSIDE THE UNITED STATES.—For purposes of this paragraph, under regulations prescribed by the Secretary, rules similar to the rules under section 48(a)(2) (including the exceptions under subparagraph (B)) shall be applied in determining whether property is used predominantly outside the United States.

“(E) CONVENTION.—Under regulations prescribed by the Secretary, the half year convention shall apply for purposes of any determination under subparagraph (C) (other than any determination with respect to 15-year real property).

“(3) RRB REPLACEMENT PROPERTY.—

“(A) IN GENERAL.—In the case of RRB replacement property placed in service before January 1, 1985, the recovery deduction for the taxable year shall be, in lieu of the amount determined under subsection (b), the amount determined by applying to the unadjusted basis of such property the applicable percentage determined under tables prescribed by the Secretary. For purposes of the preceding sentence, in prescribing such tables, the Secretary shall—

“(i) use the recovery period determined in accordance with the following table:

<i>“If the year property is placed in service is:</i>	<i>The recovery period is:</i>
1981.....	1
1982.....	2
1983.....	3
1984.....	4

and

“(ii) assign percentages determined in accordance with use of the method of depreciation described in section 167(b)(2), switching to the method described in section 167(b)(3) at a time to maximize the deduction allowable under subsection (a) (taking into account the half-year convention).

“(B) RRB REPLACEMENT PROPERTY DEFINED.—For purposes of this section, the term ‘RRB replacement property’ means replacement track material (including rail, ties, other track material, and ballast) installed by a railroad (including a railroad switching or terminal company) if—

“(i) the replacement is made pursuant to a scheduled program for replacement,

“(ii) the replacement is made pursuant to observations by maintenance-of-way personnel or specific track material needing replacement,

“(iii) the replacement is made pursuant to the detection by a rail-test car of specific track material needing replacement, or

“(iv) the replacement is made as a result of a casualty.

*Replacements made as a result of a casualty shall be RRB replacement property only to the extent that, in the case of each casualty, the replacement cost with respect to the replacement track material exceeds \$50,000.*

**“(4) MANNER AND TIME FOR MAKING ELECTIONS.—**

**“(A) IN GENERAL.—**Any election under this section shall be made for the taxable year in which the property is placed in service.

**“(B) MADE ON RETURN.—**Any election under this section shall be made on the taxpayer’s return of the tax imposed by this chapter for the taxable year concerned.

**“(C) REVOCATION ONLY WITH CONSENT.—**Any election under this section, once made, may be revoked only with the consent of the Secretary.

**“(5) SHORT TAXABLE YEARS.—**In the case of a taxable year that is less than 12 months, the amount of the deduction under this section shall be an amount which bears the same relationship to the amount of the deduction, determined without regard to this paragraph, as the number of months in the short taxable year bears to 12. In such case, the amount of the deduction for subsequent taxable years shall be appropriately adjusted in accordance with regulations prescribed by the Secretary. The determination of when a taxable year begins shall be made in accordance with regulations prescribed by the Secretary. This paragraph shall not apply to any deduction with respect to any property for the first taxable year of the lessor for which an election under paragraph (8) is in effect with respect to such property.

**“(6) LEASEHOLD IMPROVEMENTS.—**For purposes of determining whether a leasehold improvement which is recovery property shall be amortized over the term of the lease, the recovery period (taking into account any election under paragraph (2)(C) of this subsection or under subsection (b)(3) with respect to such property) of such property shall be taken into account in lieu of its useful life.

**“(7) SPECIAL RULE FOR ACQUISITIONS AND DISPOSITIONS IN NONRECOGNITION TRANSACTIONS.—**Notwithstanding any other provision of this section, the deduction allowed under this section in the taxable year in which recovery property is acquired or is disposed of in a transaction in which gain or loss is not recognized in whole or in part shall be determined in accordance with regulations prescribed by the Secretary.

**“(8) SPECIAL RULE FOR LEASES.—**

**“(A) IN GENERAL.—**In the case of an agreement with respect to qualified leased property, if all of the parties to the agreement characterize such agreement as a lease and elect to have the provisions of this paragraph apply with respect to such agreement, and if the requirements of subparagraph (B) are met, then, for purposes of this subtitle—

**“(i)** such agreement shall be treated as a lease entered into by the parties (and any party which is a corporation described in subparagraph (B)(i)(I) shall be deemed to have entered into the lease in the course of carrying on a trade or business), and

*“(ii) the lessor shall be treated as the owner of the property and the lessee shall be treated as the lessee of the property.*

*“(B) CERTAIN REQUIREMENTS MUST BE MET.—The requirements of this subparagraph are met if—*

*“(i) the lessor is—*

*“(I) a corporation (other than an electing small business corporation (within the meaning of section 1371(b)) or a personal holding company (within the meaning of section 542(a))),*

*“(II) a partnership all of the partners of which are corporations described in subclause (I), or*

*“(III) a grantor trust with respect to which the grantor and all beneficiaries of the trust are described in subclause (I) or (II),*

*“(ii) the minimum investment of the lessor—*

*“(I) at the time the property is first placed in service under the lease, and*

*“(II) at all times during the term of the lease, is not less than 10 percent of the adjusted basis of such property, and*

*“(iii) the term of the lease (including any extensions) does not exceed the greater of—*

*“(I) 90 percent of the useful life of such property for purposes of section 167, or*

*“(II) 150 percent of the present class life of such property.*

*“(C) NO OTHER FACTORS TAKEN INTO ACCOUNT.—If the requirements of subparagraphs (A) and (B) are met with respect to any transaction described in subparagraph (A), no other factors shall be taken into account in making a determination as to whether subparagraph (A) (i) or (ii) applies with respect to such transaction.*

*“(D) QUALIFIED LEASED PROPERTY DEFINED.—For purposes of subparagraph (A), the term ‘qualified leased property’ means recovery property (other than a qualified rehabilitated building within the meaning of section 48(g)(1)) which is—*

*“(i) new section 38 property (as defined in section 48(b)) of the lessor which is leased within 3 months after such property was placed in service and which, if acquired by the lessee, would have been new section 38 property of the lessee,*

*“(ii) property—*

*“(I) which was new section 38 property of the lessee,*

*“(II) which was leased within 3 months after such property was placed in service by the lessee, and*

*“(III) with respect to which the adjusted basis of the lessor does not exceed the adjusted basis of the lessee at the time of the lease, or*

*“(iii) property which is a qualified mass commuting vehicle (as defined in section 103(b)(9)) and which is financed in whole or in part by obligations the interest*

on which is excludable from income under section 103(a).

For purposes of this title (other than this subparagraph), any property described in clause (i) or (ii) to which subparagraph (A) applies shall be deemed originally placed in service not earlier than the date such property is used under the lease. In the case of property placed in service after December 31, 1980, and before the date of the enactment of this subparagraph, this subparagraph shall be applied by submitting 'the date of the enactment of this subparagraph' for 'such property was placed in service'.

**"(E) MINIMUM INVESTMENT.—**

**"(i) IN GENERAL.—**For purposes of subparagraph (A), the term 'minimum investment' means the amount the lessor has at risk with respect to the property (other than financing from the lessee or a related party of the lessee).

**"(ii) SPECIAL RULE FOR PURCHASE REQUIREMENT.—**For purposes of clause (i), an agreement between the lessor and lessee requiring either or both parties to purchase or sell the qualified leased property at some price (whether or not fixed in the agreement) at the end of the lease term shall not affect the amount the lessor is treated as having at risk with respect to the property.

**"(F) CHARACTERIZATION BY PARTIES.—**For purposes of this paragraph, any determination as to whether a person is a lessor or lessee or property is leased shall be made on the basis of the characterization of such person or property under the agreement described in subparagraph (A).

**"(G) REGULATIONS.—**The Secretary shall prescribe such regulations as may be necessary to carry out the purposes of this paragraph, including (but not limited to) regulations consistent with such purposes which limit the aggregate amount of (and timing of) deductions and credits in respect of qualified leased property to the aggregate amount (and the timing) allowable without regard to this paragraph.

**"(H) CROSS REFERENCE.—**

*"For special recapture in cases where lessee acquires qualified leased property, see section 1245.*

**"(9) SALVAGE VALUE.—**No salvage value shall be taken into account in determining the deduction allowable under subsection (a).

**"(10) TRANSFEREE BOUND BY TRANSFEROR'S PERIOD AND METHOD IN CERTAIN CASES.—**

**"(A) IN GENERAL.—**In the case of recovery property transferred in a transaction described in subparagraph (B), the transferee shall be treated as the transferor for purposes of computing the deduction allowable under subsection (a) with respect to so much of the basis in the hands of the transferee as does not exceed the adjusted basis in the hands of the transferor.

**"(B) TRANSFERS COVERED.—**The transactions described in this subparagraph are—

**"(i)** a transaction described in section 332 (other than a transaction with respect to which the basis is deter-

mined under section 334(b)(2)), 351, 361, 371(a), 374(a), 721, or 731;

“(ii) an acquisition (other than described in clause (i)) from a related person (as defined in subparagraph (D) of subsection (e)(4)); and

“(iii) an acquisition followed by a leaseback to the person from whom the property is acquired.

“(C) **PROPERTY REACQUIRED BY THE TAXPAYER.**—Under regulations prescribed by the Secretary, recovery property which is disposed of and then reacquired by the taxpayer shall be treated for purposes of computing the deduction allowable under subsection (a) as if such property had not been disposed of.

“(D) **EXCEPTION.**—This paragraph shall not apply to any transaction to which subsection (e)(4) applies.

“(11) **SPECIAL RULES FOR COOPERATIVES.**—In the case of a cooperative organization described in section 1381(a), the Secretary may by regulations provide—

“(A) for allowing allocation units to make separate elections under this section with respect to recovery property, and

“(B) for the allocation of the deduction allowable under subsection (a) among allocation units.

“(g) **DEFINITIONS.**—For purposes of this section—

“(1) **PUBLIC UTILITY PROPERTY.**—The term ‘public utility property’ means property described in section 167(l)(3)(A).

“(2) **PRESENT CLASS LIFE.**—The term ‘present class life’ means the class life (if any) which would be applicable with respect to any property as of January 1, 1981, under subsection (m) of section 167 (determined without regard to paragraph (4) thereof and as if the taxpayer had made an election under such subsection).

“(3) **SECTION 1245 CLASS PROPERTY.**—The term ‘section 1245 class property’ means tangible property described in section 1245(a)(3) other than subparagraphs (C) and (D).

“(4) **SECTION 1250 CLASS PROPERTY.**—The term ‘section 1250 class property’ means property described in section 1250(c) and property described in section 1245(a)(3)(C).

“(5) **RESEARCH AND EXPERIMENTATION.**—The term ‘research and experimentation’ has the same meaning as the term research or experimental has under section 174.

“(6) **RRB PROPERTY DEFINED.**—For purposes of this section, the term ‘RRB property’ means property which under the taxpayer’s method of depreciation before January 1, 1981, would have been depreciated using the retirement-replacement-betterment method.

“(7) **MANUFACTURED HOMES.**—The term ‘manufactured home’ has the same meaning as in section 603(6) of the Housing and Community Development Act of 1974, which is 1250 class property used as a dwelling unit.

“(8) **QUALIFIED COAL UTILIZATION PROPERTY.**—

“(A) **IN GENERAL.**—The term ‘qualified coal utilization property’ means that portion of the unadjusted basis of coal utilization property which bears the same ratio (but not greater than 1) to such unadjusted basis as—



“(i) the Btu’s of energy produced by the powerplant or major fuel-burning installation before the conversion or replacement involving coal utilization property, bears to

“(ii) the Btu’s of energy produced by such powerplant or installation after such conversion or replacement.

“(B) IN GENERAL.—The term ‘coal utilization property’ means—

“(i) a boiler or burner—

“(I) the primary fuel for which is coal (including lignite), and

“(II) which replaces an existing boiler or burner which is part of a powerplant or major fuel-burning installation and the primary fuel for which is oil or natural gas or any product thereof, and

“(ii) equipment for converting an existing boiler or burner described in clause (i)(II) to a boiler or burner the primary fuel for which will be coal.

“(C) POWERPLANT AND MAJOR FUEL-BURNING INSTALLATION.—The terms ‘powerplant’ and ‘major fuel-burning installation’ have the meanings given such terms by paragraphs (7) and (10) of section 103(a) of the Powerplant and Industrial Fuel Use Act of 1978, respectively.

“(D) EXISTING BOILER OR BURNER.—The term ‘existing boiler or burner’ means a boiler or burner which was placed in service before January 1, 1981.

“(E) REPLACEMENT OF EXISTING BOILER OR BURNER.—A boiler or burner shall be treated as replacing a boiler or burner if the taxpayer certifies that the boiler or burner which is to be replaced—

“(i) was used during calendar year 1980 for more than 2,000 hours of full load peak use (or equivalent thereof), and

“(ii) will not be used for more than 2,000 hours of such use during any 12-month period after the boiler or burner which is to replace such boiler or burner is placed in service.

“(h) SPECIAL RULES FOR RECOVERY PROPERTY CLASSES.—For purposes of this section—

“(1) CERTAIN HORSES.—The term ‘3-year property’ includes—

“(A) any race horse which is more than 2 years old at the time such horse is placed in service; or

“(B) any other horse which is more than 12 years old at such time.

“(2) RAILROAD TANK CARS.—The term ‘10-year property’ includes railroad tank cars.

“(3) MANUFACTURED HOMES.—The term ‘10-year property’ includes manufactured homes.

“(4) QUALIFIED COAL UTILIZATION PROPERTY.—The term ‘10-year property’ includes qualified coal utilization property which is not 3-year property, 5-year property, or 10-year property (determined without regard to this paragraph).

“(5) APPLICATION WITH OTHER CLASSES.—Any property which is treated as included in a class or property by reason of this

subsection shall not be treated as property included in any other class.

**“(i) CROSS REFERENCE.—**

*For special rules with respect to certain gain derived from disposition of recovery property, see sections 1245 and 1250.”*

**(b) SINGLE PURPOSE AGRICULTURAL OR HORTICULTURAL STRUCTURES AND PETROLEUM PRODUCT STORAGE FACILITIES TREATED AS SECTION 1245 PROPERTY.—**Paragraph (3) of section 1245(a) (defining section 1245 property) is amended by striking out “or” at the end of subparagraph (C), by striking out the period at the end of subparagraph (D), and by adding at the end thereof the following new subparagraphs:

*“(E) a single purpose agricultural or horticultural structure (as defined in section 48(p)), or*

*“(F) a storage facility used in connection with the distribution of petroleum or any primary product of petroleum.”*

**(c) REPEAL OF SECTION 263(e).—**Subsection (e) of section 263 is hereby repealed.

**(d) CLERICAL AMENDMENT.—**The table of sections for part VI of subchapter B of chapter 1 is amended by inserting after the item relating to section 167 the following new item:

*“Sec. 168. Accelerated cost recovery system.”*

**SEC. 202. ELECTION TO EXPENSE CERTAIN DEPRECIABLE BUSINESS ASSETS.**

**(a) IN GENERAL.—**Section 179 (relating to additional first-year depreciation allowance for small business) is amended to read as follows:

**“SEC. 179. ELECTION TO EXPENSE CERTAIN DEPRECIABLE BUSINESS ASSETS.**

**“(a) TREATMENT AS EXPENSES.—**A taxpayer may elect to treat the cost of any section 179 property as an expense which is not chargeable to capital account. Any cost so treated shall be allowed as a deduction for the taxable year in which the section 179 property is placed in service.

**“(b) DOLLAR LIMITATION.—**

**“(1) IN GENERAL.—**The aggregate cost which may be taken into account under subsection (a) for any taxable year shall not exceed the following applicable amount:

<b>“If the taxable year begins in:</b>	<b>The applicable amount is:</b>
1981.....	\$0
1982.....	\$5,000
1983.....	\$5,000
1984.....	\$7,500
1985.....	\$7,500
1986 or thereafter .....	\$10,000.

**“(2) MARRIED INDIVIDUALS FILING SEPARATELY.—**In the case of a husband and wife filing separate returns for a taxable year, the applicable amount under paragraph (1) shall be equal to 50 percent of the amount otherwise determined under paragraph (1).

**“(c) ELECTION.—**

**“(1) IN GENERAL.—**An election under this section for any taxable year shall—

“(A) specify the items of section 179 property to which the election applies and the portion of the cost of each of such items which is to be taken into account under subsection (a), and

“(B) be made on the taxpayer’s return of the tax imposed by this chapter for the taxable year.

Such election shall be made in such manner as the Secretary may by regulations prescribe.

“(2) **ELECTION IRREVOCABLE.**—Any election made under this section, and any specification contained in any such election, may not be revoked except with the consent of the Secretary.

“(d) **DEFINITIONS AND SPECIAL RULES.**—

“(1) **SECTION 179 PROPERTY.**—For purposes of this section, the term ‘section 179 property’ means any recovery property which is section 38 property and which is acquired by purchase for use in a trade or business.

“(2) **PURCHASE DEFINED.**—For purposes of paragraph (1), the term ‘purchase’ means any acquisition of property, but only if—

“(A) the property is not acquired from a person whose relationship to the person acquiring it would result in the disallowance of losses under section 267 or 707(b) (but, in applying section 267 (b) and (c) for purposes of this section, paragraph (4) of section 267(c) shall be treated as providing that the family of an individual shall include only his spouse, ancestors, and lineal descendants),

“(B) the property is not acquired by one component member of a controlled group from another component member of the same controlled group, and

“(C) the basis of the property in the hands of the person acquiring it is not determined—

“(i) in whole or in part by reference to the adjusted basis of such property in the hands of the person from whom acquired, or

“(ii) under section 1014(a) (relating to property acquired from a decedent).

“(3) **COST.**—For purposes of this section, the cost of property does not include so much of the basis of such property as is determined by reference to the basis of other property held at any time by the person acquiring such property.

“(4) **SECTION NOT TO APPLY TO ESTATES AND TRUSTS.**—This section shall not apply to estates and trusts.

“(5) **SECTION NOT TO APPLY TO CERTAIN NONCORPORATE LESSORS.**—This section shall not apply to any section 179 property purchased by any person described in section 46(e)(3) unless the credit under section 38 is allowable with respect to such person for such property (determined without regard to this section).

“(6) **DOLLAR LIMITATION OF CONTROLLED GROUP.**—For purposes of subsection (b) of this section—

“(A) all component members of a controlled group shall be treated as one taxpayer, and

“(B) the Secretary shall apportion the dollar limitation contained in subsection (b)(1) among the component members of such controlled group in such manner as he shall by regulations prescribe.

**“(7) CONTROLLED GROUP DEFINED.**—For purposes of paragraphs (2) and (6), the term ‘controlled group’ has the meaning assigned to it by section 1563(a), except that, for such purposes, the phrase ‘more than 50 percent’ shall be substituted for the phrase ‘at least 80 percent’ each place it appears in section 1563(a)(1).

**“(8) DOLLAR LIMITATION IN CASE OF PARTNERSHIPS.**—In the case of a partnership, the dollar limitation contained in subsection (b)(1) shall apply with respect to the partnership and with respect to each partner.

**“(9) COORDINATION WITH SECTION 38.**—No credit shall be allowed under section 38 with respect to any amount for which a deduction is allowed under subsection (a).”

**(b) RECAPTURE RULE.**—Subsection (a) of section 1245 (relating to gains from dispositions from certain depreciable property) is amended—

(1) by striking out “169, 184” each place it appears in paragraph (2) and inserting in lieu thereof “169, 179, 184”,

(2) by striking out “section 190” in paragraph (2) and inserting in lieu thereof “section 179, 190”, and

(3) by striking out “169, 185” in paragraphs (2)(D) and (3)(D) and inserting in lieu thereof “169, 179, 185”.

**(c) INSTALLMENT SALES.**—Section 453 (relating to the installment method) is amended by redesignating subsection (i) as subsection (j) and by inserting after subsection (h) the following new subsection:

**“(i) APPLICATION WITH SECTION 179.**—

**“(1) IN GENERAL.**—In the case of an installment sale of section 179 property, subsection (a) shall not apply, and for purposes of this title, all payments to be received shall be deemed received in the year of disposition.

**“(2) LIMITATION.**—Paragraph (1) shall apply only to the extent of the amount allowed as a deduction under section 179 with respect to the section 179 property.”

**(d) TECHNICAL AMENDMENTS.**—

(1) Paragraph (1) of section 263(a) (relating to capital expenditures) is amended—

(A) by striking “or” at the end of subparagraph (F);

(B) by striking out the period at the end of subparagraph (G) and inserting in lieu thereof a semicolon and “or”, and

(C) by adding at the end thereof the following new subparagraph:

**“(H) expenditures for which a deduction is allowed under section 179.”**

(2) Subparagraph (A) of section 1033(g)(3) (relating to condemnation of real property held for productive use in trade or business or for investment) is amended by striking out “(relating to additional first-year depreciation allowance for small business)” and inserting in lieu thereof “(relating to election to expense certain depreciable business assets)”.

(3) The table of sections for part VI of subchapter B of chapter 1 is amended by striking out the item relating to section 179 and inserting in lieu thereof the following:

**“Sec. 179. Election to expense certain depreciable business assets.”**

**SEC. 203. AMENDMENTS RELATED TO DEPRECIATION.**

(a) **RECOVERY DEDUCTION TREATED AS DEPRECIATION.**—Subsection (a) of section 167 (relating to depreciation) is amended by adding at the end thereof the following new sentence: “In the case of recovery property (within the meaning of section 168), the deduction allowable under section 168 shall be deemed to constitute the reasonable allowance provided by this section, except with respect to that portion of the basis of such property to which subsection (k) applies.”

(b) **TERMINATION OF CLASS LIFE SYSTEM.**—Subsection (m) of section 167 (relating to class lives) is amended by adding at the end thereof the following new paragraph:

“(4) **TERMINATION.**—This subsection shall not apply with respect to recovery property (within the meaning of section 168) placed in service after December 31, 1980.”

(c) **RETIREMENT—REPLACEMENT—BETTERMENT METHOD OF DEPRECIATION.**—

(1) **REPEAL OF SECTION 167(r).**—Section 167 (relating to depreciation) is amended by striking out subsection (r) and redesignating subsection (s) as subsection (r).

(2) **CHANGE IN METHOD OF ACCOUNTING.**—Sections 446 and 481 of the Internal Revenue Code of 1954 shall not apply to the change in the method of depreciation to comply with the provisions of this subsection.

(3) **TRANSITIONAL RULE.**—The adjusted basis of RRB property (as defined in section 168(g)(6) of such Code) as of December 31, 1980, shall be depreciated using a useful life of no less than 5 years and no more than 50 years and a method described in section 167(b) of such Code, including the method described in section 167(b)(2) of such Code, switching to the method described in section 167(b)(3) of such Code at a time to maximize the deduction.

(d) **AGREEMENT AS TO USEFUL LIFE ON WHICH DEPRECIATION RATE IS BASED.**—Subsection (d) of section 167 is amended by adding at the end thereof the following: “This subsection shall not apply with respect to recovery property defined in section 168.”

(e) **CONFORMING AMENDMENT.**—The Secretary of Health and Human Services is not required to apply any provision of the Internal Revenue Code of 1954, as amended, in calculating depreciation (for the purpose of determining any cost under a program administered by the Secretary), unless a provision of law requires so expressly.

**SEC. 204. RECAPTURE ON DISPOSITION OF RECOVERY PROPERTY.**

(a) **GENERAL RULE.**—Paragraph (1) of section 1245(a) (relating to ordinary income) is amended by inserting after “December 31, 1962,” the following “or section 1245 recovery property is disposed of after December 31, 1980,”

(b) **RECOMPUTED BASIS.**—Paragraph (2) of section 1245(a) (relating to recomputed basis) is amended—

- (1) by striking out “or” at the end of subparagraph (C),
- (2) by inserting “, or” at the end of subparagraph (D), and
- (3) by inserting immediately after subparagraph (D) the following new subparagraph:

“(E) with respect to any section 1245 recovery property, the adjusted basis of such property recomputed by adding thereto all adjustments attributable to periods for which a

deduction is allowed under section 168(a) (as added by the Economic Recovery Tax Act of 1981) with respect to such property.”

(c) **SECTION 1245 RECOVERY PROPERTY DEFINED.**—Subsection (a) of section 1245 is amended by adding at the end thereof the following new paragraph:

“(5) **SECTION 1245 RECOVERY PROPERTY.**—For purposes of this section, the term ‘section 1245 recovery property’ means recovery property (within the meaning of section 168) other than—

“(A) 15-year real property which is residential rental property (as defined in section 167(j)(2)(B)),

“(B) 15-year real property which is described in section 168(f)(2),

“(C) 15-year real property with respect to which an election under subsection (b)(3) of section 168 to use a different recovery percentage is in effect, and

“(D) 15-year real property which is described in clause (i), (ii), (iii), or (iv) of section 1250(a)(1)(B).

If only a portion of a building (or other structure) is section 1245 recovery property, gain from any disposition of such building (or other structure) shall be allocated first to the portion of the building (or other structure) which is section 1245 recovery property (to the extent of the amount which may be treated as ordinary income under this section) and then to the portion of the building or other structure which is not section 1245 recovery property.”

(d) **QUALIFIED LEASED PROPERTY.**—Subsection (a) of section 1245 (relating to recomputed basis) is amended by adding at the end thereof the following new paragraph:

“(6) **SPECIAL RULE FOR QUALIFIED LEASED PROPERTY.**—In any case in which—

“(A) the lessor of qualified leased property (within the meaning of section 168(f)(8)(D)) is treated as the owner of such property for purposes of this subtitle under section 168(f)(8), and

“(B) the lessee acquires such property, the recomputed basis of the lessee under this subsection shall be determined by taking into account any adjustments which would be taken into account in determining the recomputed basis of the lessor.”

(e) **APPLICATION WITH SECTION 1250.**—Subsection (d) of section 1250 (relating to exceptions and limitations) is amended by adding at the end thereof the following new paragraph:

“(11) **SECTION 1245 RECOVERY PROPERTY.**—Subsection (a) shall not apply to the disposition of property which is section 1245 recovery property (as defined in section 1245(a)(5)).”

#### **SEC. 205. MINIMUM TAX TREATMENT.**

(a) **IN GENERAL.**—Subsection (a) of section 57 (defining items of tax preference) is amended by inserting immediately after paragraph (11) the following new paragraph:

“(12) **ACCELERATED COST RECOVERY DEDUCTION.**—

“(A) **IN GENERAL.**—With respect to each recovery property (other than 15-year real property) which is subject to a lease, the amount (if any) by which the deduction allowed under section 168(a) for the taxable year exceeds the deduc-

tion which would have been allowable for the taxable year had the property been depreciated using the straight-line method (with a half-year convention and without regard to salvage value) and a recovery period determined in accordance with the following table:

<i>"In the case of:</i>	<i>The recovery period is:</i>
3-year property.....	5 years.
5-year property.....	8 years.
10-year property.....	15 years.
15-year public utility property.....	22 years.

**"(B) 15-YEAR REAL PROPERTY.**—With respect to each recovery property which is 15-year real property, the amount (if any) by which the deduction allowed under section 168(a) for the taxable year exceeds the deduction which would have been allowable for the taxable year had the property been depreciated using a 15-year period and the straight-line method (without regard to salvage value).

**"(C) PARAGRAPHS (2) AND (3) SHALL NOT APPLY.**—Paragraphs (2) and (3) shall not apply to recovery property.

**"(D) DEFINITIONS.**—For purposes of this paragraph, the terms '3-year property', '5-year property', '10-year property', '15-year public utility property', '15-year real property', and 'recovery property', shall have the same meanings given such terms under section 168."

(b) **CONFORMING AMENDMENT.**—The next to the last sentence of section 57(a) is amended by striking out "and (11)" and inserting in lieu thereof ", (11), and (12)".

#### **SEC. 206. EARNINGS AND PROFITS.**

(a) **IN GENERAL.**—Subsection (k) of section 312 (relating to earnings and profits) is amended by redesignating paragraph (3) as paragraph (4) and by inserting after paragraph (2) the following new paragraph:

**"(3) EXCEPTION FOR RECOVERY AND SECTION 179 PROPERTY.**—

**"(A) RECOVERY PROPERTY.**—Except as provided in subparagraphs (B) and (C), in the case of recovery property (within the meaning of section 168), the adjustment to earnings and profits for depreciation for any taxable year shall be the amount determined under the straight-line method (using a half year convention in the case of property other than the 15-year real property and without regard to salvage value) and using a recovery period determined in accordance with the following table:

<i>"In the case of:</i>	<i>The applicable recovery period is:</i>
3-year property.....	5 years.
5-year property.....	12 years.
10-year property.....	25 years.
15-year real property.....	35 years.
15-year public utility property.....	35 years.

For purposes of this subparagraph, no adjustment shall be allowed in the year of disposition (except with respect to 15-year real property), and rules similar to the rules under the last sentence of section 168(b)(2)(A) and section 168(b)(2)(B) shall apply.

**“(B) TREATMENT OF AMOUNTS DEDUCTIBLE UNDER SECTION 179.**—For purposes of computing the earnings and profits of a corporation, any amount deductible under section 179 shall be allowed as a deduction ratably over the period of 5 years (beginning with the year for which such amount is deductible under section 179).

**“(C) FLEXIBILITY.**—In any case where a different recovery percentage is elected under section 168(b)(3) or (f)(2)(C) based on a recovery period longer than the recovery period provided in subparagraph (A), the adjustment to earnings and profits shall be based on such longer period under rules similar to those provided in subparagraph (A).”

**(b) FOREIGN CORPORATIONS.**—Paragraph (4) of section 312(k), as redesignated by subsection (a), is amended—

(1) by striking out “paragraph (1)” and inserting in lieu thereof “paragraphs (1) and (3)”, and

(2) by adding at the end thereof the following new sentence: “In determining the earnings and profits of such corporation in the case of recovery property (within the meaning of section 168), the rules of section 168(f)(2) shall apply.”

**(c) CONFORMING AMENDMENT.**—Subsection (a) of section 964 (relating to miscellaneous provisions involving controlled foreign corporations) is amended by striking out “section 312(k)(3)” and inserting in lieu thereof “section 312(k)(4)”.

**SEC. 207. EXTENSION OF CARRYOVER PERIOD FOR NET OPERATING LOSSES AND CERTAIN CREDITS.**

**(a) NET OPERATING LOSS.**—

(1) **IN GENERAL.**—Subparagraph (B) of section 172(b)(1) (relating to net operating loss carryovers) is amended by striking out “7” and inserting in lieu thereof “15”.

(2) **CONFORMING AMENDMENTS.**—

**(A) Subparagraph (C) of section 172(b)(1) is amended—**

(i) by inserting “and before January 1, 1976,” after “1955,” and

(ii) by striking out the last sentence thereof.

**(B)(i) Subparagraph (E)(i)(II) of section 172(b)(1) is amended by striking out “8” and inserting in lieu thereof “15”.**

**(ii) Clause (ii) of section 172(b)(1)(E) is amended to read as follows:**

“(ii) In the case of any net operating loss for a taxable year which is not a REIT year, such loss shall not be carried back to any taxable year which is a REIT year.”

**(C) Paragraph (3) of section 172(g) (relating to certain regulated transportation corporations) is amended—**

(i) by inserting “and” at the end of subparagraph (A),

(ii) by striking out “; and” at the end of subparagraph (B) and inserting in lieu thereof a period, and

(iii) by striking out subparagraph (C).

**(b) CERTAIN LOSSES OF LIFE INSURANCE COMPANIES.**—Paragraph (1) of section 812(b) (relating to operations loss carrybacks and carryovers of life insurance companies) and paragraph (1) of section 825(d) (relating to unused loss carrybacks and carryovers of mutual



life insurance companies) are each amended by striking out "7" and inserting in lieu thereof "15".

**(c) CARRYOVER OF TAX CREDITS.—**

**(1) INVESTMENT CREDIT AND WIN CREDIT.—**Paragraph (1) of section 46(b) (relating to carryback and carryovers of unused investment credits) and paragraph (1) of section 50A(b) (relating to carryback and carryover of unused work incentive program credit) are each amended by adding at the end thereof the following new sentence: "In the case of an unused credit for an unused credit year ending after December 31, 1973, this paragraph shall be applied by substituting '15' for '7' in subparagraph (B), and by substituting '18' for '10', and '17' for '9' in the second sentence."

**(2) NEW EMPLOYEE CREDIT.—**Paragraph (1) of section 53(c) (relating to carrybacks and carryovers of new employee credit) is amended—

(A) by striking out "7" in subparagraph (B) and inserting in lieu thereof "15",

(B) by striking out "10" and inserting in lieu thereof "18", and

(C) by striking out "9" and inserting in lieu thereof "17".

**(3) ALCOHOL FUELS CREDIT.—**Subparagraph (A) of section 44E(e)(2) (relating to carryover of unused credit) is amended—

(A) by striking out "7" each place it appears and inserting in lieu thereof "15", and

(B) by striking out "6" and inserting in lieu thereof "14".

**SEC. 208. CARRYOVER OF RECOVERY ATTRIBUTE IN SECTION 381 TRANSACTIONS.**

Subsection (c) of section 381 is amended by adding at the end thereof the following new paragraph:

"(28) **METHOD OF COMPUTING RECOVERY ALLOWANCE FOR RECOVERY PROPERTY.—**The acquiring corporation shall be treated as the distributor or transferor corporation for purposes of computing the deduction allowable under section 168(a) on property acquired in a distribution or transfer with respect to so much of the basis in the hands of the acquiring corporation as does not exceed the adjusted basis in the hands of the distributor or transferor corporation."

**SEC. 209. EFFECTIVE DATES.**

**(a) GENERAL RULE.—**Except as otherwise provided in this section, the amendments made by this subtitle shall apply to property placed in service after December 31, 1980, in taxable years ending after such date.

**(b) SPECIAL RULE FOR RRB PROPERTY.—**The amendment made by subsection (c) of section 203 shall take effect on January 1, 1981, and shall apply with respect to taxable years ending after such date.

**(c) SPECIAL RULE FOR CARRYOVERS.—**

**(1)(A)** Except as provided in subparagraph (B), the amendments made by subsections (a) and (b) of section 207 shall apply to net operating losses in taxable years ending after December 31, 1975.

**(B)** The amendments made by subparagraph (B) of section 207(a)(2) shall take effect as if they had been included in the amendments made by section 1(a) of Public Law 96-595; except that the amendments made by such subparagraph shall apply

only to net operating losses in taxable years ending after December 31, 1972.

(2)(A) The amendments made by subsection (c)(1) of section 207 shall apply to unused credit years ending after December 31, 1973.

(B) The amendment made by subsection (c)(2) of section 207 shall apply to unused credit years beginning after December 31, 1976.

(C) The amendments made by subsection (c)(3) of section 207 shall apply to unused credit years ending after September 30, 1980.

**(d) SPECIAL RULE FOR PUBLIC UTILITIES.—**

**(1) TRANSITIONAL RULE FOR NORMALIZATION REQUIREMENTS.—** If, by the terms of the applicable rate order last entered before the date of the enactment of this Act by a regulatory commission having appropriate jurisdiction, a regulated public utility would (but for this provision) fail to meet the requirements of section 168(e)(3) of the Internal Revenue Code of 1954 with respect to property because, for an accounting period ending after December 31, 1980, such public utility used a method of accounting other than a normalization method of accounting, such regulated public utility shall not fail to meet such requirements if, by the terms of its first rate order determining cost of service with respect to such property which becomes effective after the date of the enactment of this Act and on or before January 1, 1983, such regulated public utility uses a normalization method of accounting. This provision shall not apply to any rate order which, under the rules in effect before the date of the enactment of this Act, required a regulated public utility to use a method of accounting with respect to the deduction allowable by section 167 which, under section 167(l), it was not permitted to use.

**(2) TRANSITIONAL RULE FOR REQUIREMENTS OF SECTION 46(f).—** If, by the terms of the applicable rate order last entered before the date of the enactment of this Act by a regulatory commission having appropriate jurisdiction, a regulated public utility would (but for this provision) fail to meet the requirements of paragraph (1) or (2) of section 46(f) of the Internal Revenue Code of 1954 with respect to property for an accounting period ending after December 31, 1980, such regulated public utility shall not fail to meet such requirements if, by the terms of its first rate order determining cost of service with respect to such property which becomes effective after the date of the enactment of this Act and on or before January 1, 1983, such regulated public utility meets such requirements. This provision shall not apply to any rate order which, under the rules in effect before the date of the enactment of this Act, was inconsistent with the requirements of paragraph (1) or (2) of section 46(f) of such Code (whichever would have been applicable).

**(3) CLARIFICATION.—** Subparagraph (C) of section 167(l)(3) is amended by inserting "and which is placed in service before January 1, 1981" immediately before the period at the end thereof.

**(4) AUTHORITY TO PRESCRIBE INTERIM REGULATIONS WITH RESPECT TO NORMALIZATION.—** Until Congress acts further, the Sec-

retary of the Treasury or his delegate may prescribe such interim regulations as may be necessary or appropriate to determine whether the requirements of section 168(e)(3)(B) of the Internal Revenue Code of 1954 have been met with respect to property placed in service after December 31, 1980.

## **Subtitle B—Investment Tax Credit Provisions**

### **SEC. 211. MODIFICATION OF INVESTMENT TAX CREDIT TO REFLECT ACCELERATED COST RECOVERY.**

#### **(a) APPLICABLE PERCENTAGE.—**

(1) **IN GENERAL.**—Subsection (c) of section 46 (relating to qualified investment) is amended by adding at the end thereof the following new paragraph:

“(7) **APPLICABLE PERCENTAGE FOR RECOVERY PROPERTY.**—Notwithstanding paragraph (2), the applicable percentage for purposes of paragraph (1) shall be—

“(A) in the case of 15-year public utility, 10-year, or 5-year property (within the meaning of section 168(c)), 100 percent, and

“(B) in the case of 3-year property (within the meaning of section 168(c)), 60 percent.

For purposes of subparagraph (A), RRB replacement property (within the meaning of section 168(f)(3)(B)) shall be treated as 5-year property.”

(2) Subsection (a) of section 48 (defining section 38 property) is amended by striking out paragraph (9).

#### **(b) REVISION OF PROGRESS EXPENDITURE RULES.—**

(1) **IN GENERAL.**—Paragraph (1) of section 46(d) (defining qualified progress expenditures) is amended to read as follows:

“(1) **INCREASE IN QUALIFIED INVESTMENT.**—

“(A) **IN GENERAL.**—In the case of any taxpayer who has made an election under paragraph (6), the amount of the qualified investment of such taxpayer for the taxable year (determined under subsection (c) without regard to this subsection) shall be increased by an amount equal to the aggregate of the applicable percentage of each qualified progress expenditure for the taxable year with respect to progress expenditure property.

“(B) **APPLICABLE PERCENTAGE.**—

“(i) **RECOVERY PROPERTY.**—For purposes of subparagraph (A), the applicable percentage for recovery property (within the meaning of section 168) shall be determined under subsection (c)(7) based on a reasonable expectation of what the character of the property will be when it is placed in service.

“(ii) **NONRECOVERY PROPERTY.**—For purposes of subparagraph (A), the applicable percentage for property which is not recovery property (within the meaning of section 168) shall be determined under subsection (c)(2) based on a reasonable expectation of what the useful life of the property will be when it is placed in service.

“(iii) **APPLICATION ON BASIS OF FACTS KNOWN.**—Clauses (i) and (ii) shall be applied on the basis of the

facts known at the close of the taxable year of the taxpayer in which the expenditure is made.”

(2) **CONFORMING AMENDMENT.**—Clause (ii) of section 46(d)(2)(A) (defining progress expenditure property) is amended by striking out “having a useful life of 7 years or more”.

(c) **PETROLEUM PRODUCT STORAGE FACILITIES.**—Paragraph (1) of section 48(a) (defining section 38 property) is amended—

(1) by striking out the period at the end of subparagraph (F) and inserting in lieu thereof “, or”; and

(2) by inserting immediately after subparagraph (F) the following new subparagraph:

“(G) a storage facility used in connection with the distribution of petroleum or any primary product of petroleum.”

(d) **TECHNICAL AMENDMENT RELATING TO NONCORPORATE LESSORS.**—Paragraph (3) of section 46(e) (relating to limitations on non-corporate lessors) is amended by adding at the end thereof the following new sentence: “For purposes of subparagraph (B), in the case of any recovery property (within the meaning of section 168), the useful life shall be the present class life for such property (as defined in section 168(g)(2)).”

(e) **CONFORMING AMENDMENTS.**—

(1) The heading and so much of paragraph (2) of section 46(c) as precedes the table is amended to read as follows:

“(2) **APPLICABLE PERCENTAGE IN CERTAIN CASES.**—Except as provided in paragraphs (3), (6), and (7), the applicable percentage for purposes of paragraph (1) for any property shall be determined under the following table:”

(2) Subparagraph (A) of section 46(c)(6) (relating to special rules for commuter highway vehicles) is amended to read as follows:

“(A) **IN GENERAL.**—Notwithstanding paragraph (2) or (3), in the case of a commuter highway vehicle the useful life of which is 3 years or more, or which is recovery property (within the meaning of section 168), the applicable percentage for purposes of paragraph (1) shall be 100 percent.”

(3) Subparagraph (C) of section 48(l)(2) (defining energy property) is amended by inserting before the period at the end thereof “or which is recovery property (within the meaning of section 168)”.

(4) The second sentence of section 48(a)(1) (defining section 38 property) is amended by striking out “includes only property” and inserting in lieu thereof “includes only recovery property (within the meaning of section 168 without regard to any useful life) and any other property”.

(f) **APPLICATION OF AT RISK RULES TO INVESTMENT CREDIT.**—

(1) **IN GENERAL.**—Subsection (c) of section 46 (relating to qualified investment) is amended by adding at the end thereof the following new paragraphs:

“(8) **LIMITATION TO AMOUNT AT RISK.**—

“(A) **IN GENERAL.**—In the case of new or used section 38 property which—

“(i) is placed in service during the taxable year by a taxpayer described in section 465(a)(1), and

“(ii) is used in connection with an activity with respect to which any loss is subject to limitation under section 465, the basis of such property for purposes of paragraph (1) shall not exceed the amount the taxpayer is at risk with respect to such property as of the close of such taxable year.

“(B) AMOUNT AT RISK.—

“(i) IN GENERAL.—Except as provided in clause (ii), the term ‘at risk’ has the same meaning given such term by section 465(b) (without regard to paragraph (5) thereof).

“(ii) CERTAIN FINANCING.—In the case of a taxpayer who at all times is at risk (determined without regard to this clause) in an amount equal to at least 20 percent of the basis (determined under section 168(d)(1)(A)(i)) of property described in subparagraph (A) and who acquired such property from a person who is not a related person, such taxpayer shall for purposes of this paragraph be considered at risk with respect to any amount borrowed in connection with such property (other than convertible debt) to the extent that such amount—

“(I) is borrowed from a qualified person, or

“(II) represents a loan from any Federal, State, or local government or instrumentality thereof, or is guaranteed by, any Federal, State, or local government.

“(C) SPECIAL RULE FOR PARTNERSHIPS AND SUBCHAPTER S CORPORATIONS.—In the case of any partnership or electing small business corporation (within the meaning of section 1371(b)), any amount treated as at risk under subparagraph (B)(ii) shall be allocated among the partners or shareholders (and treated as an amount at risk with respect to such persons) in the same manner as the credit allowable by section 38.

“(D) QUALIFIED PERSON.—For purposes of this paragraph, the term ‘qualified person’ means any person—

“(i) which—

“(I) is an institution described in clause (i), (ii), or (iii) of subparagraph (A) or subparagraph (B) of section 128(c)(2) or an insurance company to which subchapter L applies, or

“(II) is a pension trust qualified under section 401(a) or a person not described in subclause (I) and which is actively and regularly engaged in the business of lending money,

“(ii) which is not a related person with respect to the taxpayer,

“(iii) which is not a person who receives a fee with respect to the taxpayer’s investment in property described in subparagraph (A) or a related person to such person, and

“(iv) which is not a person from which the taxpayer acquired the property described in subparagraph (A) or a related person to such person.

**“(E) RELATED PERSON.**—For purposes of this paragraph, the term ‘related person’ has the same meaning as such term is used in section 168(e)(4), except that in applying section 168(e)(4)(D)(i) in the case of a person described in subparagraph (D)(i)(II) of this paragraph, sections 267(b) and 707(b)(1) shall be applied by substituting ‘0 percent’ for ‘50 percent’.

**“(F) SPECIAL RULE FOR CERTAIN ENERGY PROPERTY.**—

**“(i) IN GENERAL.**—The provisions of subparagraph (A) shall not apply to amounts borrowed with respect to qualified energy property (other than amounts described in subparagraph (B)).

**“(ii) QUALIFIED ENERGY PROPERTY.**—The term ‘qualified energy property’ means energy property to which (but for this subparagraph) subparagraph (A) applies and—

**“(I) which is described in clause (iii),**

**“(II) with respect to which the energy percentage determined under section 46(a)(2)(C) at the time such property is placed in service is greater than zero,**

**“(III) with respect to which the taxpayer, as of the close of the taxable year in which the property is placed in service, is at risk (within the meaning of section 465(b) without regard to paragraph (5) thereof) in an amount equal to at least 25 percent of the basis of the property, and**

**“(IV) with respect to which any nonrecourse financing (other than financing described in section 46(c)(8)(B)(ii)) in connection with such property consists of a level payment loan.**

For purposes of subclause (II), the energy percentage for property described in clause (iii)(V) shall be treated as being greater than zero during any period the energy percentage for property described in section 48(l)(14) is greater than zero.

**“(iii) PROPERTY TO WHICH THIS SUBPARAGRAPH APPLIES.**—Energy property is described in this clause if such property is—

**“(I) described in clause (ii), (iv), or (vii) or section 48(l)(2),**

**“(II) described in section 48(l)(15),**

**“(III) described in section 48(l)(3)(A)(iii) (but only to the extent such property is used for converting an alternate substance into alcohol for fuel purposes),**

**“(IV) described in clause (i) of section 48(l)(2)(A) (but only to the extent such property is also described in section 48(l)(3)(A) (viii) or (ix)), or**

**“(V) property comprising a system for using the same energy source for the sequential generation of electrical power, mechanical shaft power, or both, in combination with steam, heat, or other forms of useful energy.**

*“(iv) LEVEL PAYMENT LOAN DEFINED.—The term ‘level payment loan’ means a loan in which each installment is substantially equal, a portion of each installment is attributable to the repayment of principal, and that portion is increased commensurate with decreases in the portion of the payment attributable to interest.”*

*“(9) SUBSEQUENT INCREASES IN THE TAXPAYER’S AMOUNT AT RISK WITH RESPECT TO THE PROPERTY.—*

*“(A) IN GENERAL.—If, at the close of a taxable year subsequent to the year in which property was placed in service, the amount which the taxpayer has at risk with respect to such property has increased (as determined under subparagraph (B)), such increase shall be taken into account as additional qualified investment in such property in accordance with subparagraph (C).”*

*“(B) INCREASES TO BE TAKEN INTO ACCOUNT.—For purposes of subparagraphs (A) and (C), the amount which a taxpayer has at risk with respect to the property shall be treated as increased by the sum of the cash and the fair market value of property (other than property with respect to which the taxpayer is not at risk) used during the taxable year to reduce the principal sum of any amount with respect to which the taxpayer is not at risk.”*

*“(C) MANNER IN WHICH TAKEN INTO ACCOUNT.—For purposes of determining the amount of credit allowed under section 38 and the amount of credit subject to the early disposition rules under section 47, an increase in a taxpayer’s qualified investment in property (determined under subparagraph (B)) shall be deemed to be additional qualified investment made by the taxpayer in the year in which the property referred to in subparagraph (A) was first placed in service. However, the credit determined by taking into account the increase in qualified investment under this paragraph shall be considered a credit earned in the taxable year of such increase.”*

*(2) RECAPTURE.—Section 47 (relating to certain dispositions of section 38 property), is amended by adding at the end thereof the following new subsection:*

*“(d) PROPERTY CEASING TO BE AT RISK.—*

*“(1) IN GENERAL.—If the taxpayer ceases to any extent to be at risk (within the meaning of section 46(c)(8)(B)) with respect to any amount in connection with section 38 property, then the tax under this chapter for such taxable year shall be increased by an amount equal to the aggregate decrease in credits allowed under section 38 for all prior taxable years which would have resulted from substituting, in determining qualified investment, the amount determined under section 46(c)(8) with respect to such property if, on the date the property was placed in service, the taxpayer had not been at risk with respect to the amount he ceased to be at risk to.”*

*“(2) CERTAIN TRANSFERS NOT TREATED AS CEASING TO BE AT RISK.—If, after the 12-month period after the date on which a taxpayer borrows an amount from a qualified person (within the meaning of section 48(c)(8)(D)) with respect to which such*

taxpayer is considered at risk under section 48(c)(8)(B), the qualified person transfers or agrees to transfer any evidence of such indebtedness to a person who is not a qualified person, then, for purposes of paragraph (1), the taxpayer shall not be treated as ceasing to be at risk with respect to such amount.

**“(3) SPECIAL RULES FOR CERTAIN ENERGY PROPERTY.—**

**“(A) IN GENERAL.—**In the case of the second taxable year following the taxable year in which any qualified energy property (within the meaning of section 46(c)(8)(E)) is placed in service by the taxpayer and any succeeding taxable year, the taxpayer, for purposes of paragraph (1), shall be treated as ceasing to be at risk with respect to such property for such taxable year in an amount equal to the credit recapture amount (if any).

**“(B) CREDIT RECAPTURE AMOUNT.—**For purposes of this paragraph, the term ‘credit recapture amount’ means an amount equal to the excess (if any) of—

“(i) the total amount of principal to be paid as of the close of any taxable year under a nonrecourse level payment loan (as defined in section 46(c)(8)(F)(iv) other than a loan described in section 46(c)(8)(B)(ii)) with respect to such property, over

“(ii) the sum of—

“(I) the amount of principal actually paid as of the close of such taxable year, plus

“(II) the sum of the credit recapture amounts with respect to such property for all preceding taxable years.

**“(C) SPECIAL RULES FOR DETERMINING PRINCIPAL TO BE PAID.—**For purposes of subparagraph (B)(i), in determining the amount of the principal to be paid under a level payment loan, such determination shall be made as if such loan was to be fully repaid by the end of a period equal to the earlier of—

“(i) the present class life (as defined in section 168(g)(2)) of the property or, if the property has no present class life, a similar period determined by the Secretary, or

“(ii) the period at the end of which full repayment is to occur under the terms of the loan.

**“(D) SPECIAL RULE FOR CERTAIN CUMULATIVE DEFICIENCIES.—**If the excess of—

“(i) the amount of the total scheduled principal payments under a loan described in subparagraph (B)(i) as of the close of the taxable year, over

“(ii) the total principal actually paid under such loan as of the close of such taxable year,

is equal to or greater than the amount of such total scheduled payments for the 5-taxable year period ending with such taxable year, then, notwithstanding subparagraph (B), the credit recapture amount for such taxable year shall be equal to the principal remaining to be paid as of the close of such taxable year over the sum of the credit recapture amounts with respect to such property for all preceding taxable years.



**“(E) SPECIAL RULE FOR CERTAIN DISPOSITIONS.—**

**“(i) IN GENERAL.—**If any property which is held by the taxpayer and to which this paragraph applies is disposed of by the taxpayer, then for purposes of paragraph (1) and notwithstanding subparagraph (B), the credit recapture amount for the taxpayer shall be an amount equal to the unpaid principal on the loan described in subparagraph (B)(i) as of the date of disposition;

**“(ii) ASSUMPTIONS, ETC.—**Any amount of the loan described in subparagraph (B)(i) which is assumed or taken subject to by any person shall be treated for purposes of clause (i) as not reducing unpaid principal with respect to such loan.

**“(F) APPLICATION WITH SUBSECTION (a).—**The amount of any increase in tax under subsection (a) with respect to any property to which this paragraph applies shall be determined by reducing the qualified investment with respect to such property by the aggregate credit recapture amounts for all taxable years under this paragraph.

**“(G) ADDITIONAL INTEREST.—**In the case of any increase in tax under paragraph (1) by reason of the application of this paragraph, there shall be added to such tax interest on such tax (determined under section 6621) as if the increase in tax under paragraph (1) was for the taxable year in which the property was placed in service.”

**(g) AMENDMENT OF RECAPTURE RULES.—**

**(1) IN GENERAL.—**Subsection (a) of section 47 (relating to certain dispositions, etc, of section 38 property) is amended by redesignating paragraphs (5), (6), and (7) as paragraphs (6), (7), and (8), respectively, and by inserting after paragraph (4) the following new paragraph:

**“(5) SPECIAL RULES FOR RECOVERY PROPERTY.—**

**“(A) GENERAL RULE.—**If, during any taxable year, section 38 recovery property is disposed of, or otherwise ceases to be section 38 property with respect to the taxpayer before the close of the recapture period, then, except as provided in subparagraph (D), the tax under this chapter for such taxable year shall be increased by the recapture percentage of the aggregate decrease in the credits allowed under section 38 for all prior taxable years which would have resulted solely from reducing to zero the qualified investment taken into account with respect to such property.

**“(B) RECAPTURE PERCENTAGE.—**For purposes of subparagraph (A), the recapture percentage shall be determined in accordance with the following table:

<i>"If the recovery property ceases to be section 38 property within</i>	<i>The recapture percentage is:</i>	
	<i>For 15-year, 10-year, and 5-year property</i>	<i>For 3-year property</i>
<i>One full year after placed in service.</i>	<i>100</i>	<i>100</i>
<i>One full year after the close of the period described in clause (i).</i>	<i>80</i>	<i>66</i>
<i>One full year after the close of the period described in clause (ii).</i>	<i>60</i>	<i>33</i>
<i>One full year after the close of the period described in clause (iii).</i>	<i>40</i>	<i>0</i>
<i>One full year after the close of the period described in clause (iv).</i>	<i>20</i>	<i>0</i>

**"(C) PROPERTY CEASES TO BE PROGRESS EXPENDITURE PROPERTY.**—If, during any taxable year, any recovery property taken into account in determining qualified investment under section 46(d)(1) ceases to be progress expenditure property (as determined under paragraph (3)) or becomes, with respect to the taxpayer, recovery property of a character other than that expected in determining the applicable percentage under section 46(d)(1)(B)(i), then the tax under this chapter for such taxable year shall be adjusted in accordance with regulations prescribed by the Secretary.

**"(D) LIMITATION.**—The tax for the taxable year shall be increased under subparagraph (A) only with respect to the credits allowed under section 38 which were used to reduce tax liability. In the case of credits not so used to reduce tax liability, the carrybacks and carryovers under section 46(b) shall be appropriately adjusted.

**"(E) DEFINITIONS AND SPECIAL RULES.**—

**"(i) SECTION 38 RECOVERY PROPERTY.**—For purposes of this paragraph, the term 'section 38 recovery proper-

ty' means any section 38 property which is recovery property (within the meaning of section 168).

"(ii) **RECAPTURE PERIOD.**—For purposes of this paragraph, the term 'recapture period' means, with respect to any recovery property, the period consisting of the first full year after the property is placed in service and the 4 succeeding full years (the 2 succeeding full years in the case of 3-year property).

"(iii) **CLASSIFICATION OF PROPERTY.**—For purposes of this paragraph, property shall be classified as provided in section 168(c).

"(iv) **PARAGRAPH (1) NOT TO APPLY.**—Paragraph (1) shall not apply with respect to any recovery property."

**(2) TECHNICAL AMENDMENTS.**—

(A) Subparagraph (D) of section 47(a)(3) is amended to read as follows:

"(D) **COORDINATION WITH PARAGRAPHS (1) AND (5).**—If, after property is placed in service, there is a disposition or other cessation described in paragraph (1), or a disposition, cessation, or change in expected use described in paragraph (5), then paragraph (1) or (5), as the case may be, shall be applied as if any credit, which was allowable by reason of section 46(d) and which has not been required to be recaptured before such disposition, cessation, or change in use were allowable for the taxable year the property was placed in service."

(B) Paragraph (6) of section 47(a) (as redesignated by paragraph (1) of this subsection) is amended by striking out "paragraph (1) or (3)" and inserting in lieu thereof "paragraph (1), (3), or (5)".

(C) Subparagraph (B) of section 47(a)(7) (as redesignated by paragraph (1)) is amended by striking out "paragraph (5)" and inserting in lieu thereof "paragraph (6)".

(h) **TREATMENT OF CERTAIN LEASED ROLLING STOCK.**—Clause (ii) of section 48(a)(2)(B) is amended to read as follows:

"(ii) rolling stock which is used within and without the United States and which is—

"(I) of a domestic railroad corporation providing transportation subject to subchapter I of chapter 105 of title 49, or

"(II) of a United States person (other than a corporation described in subclause (I)) but only if the rolling stock is not leased to one or more foreign persons for periods aggregating more than 12 months in any 24-month period;"

**(i) EFFECTIVE DATE.**—

(1) **IN GENERAL.**—Except as provided in this subsection, the amendments made by this section shall apply to property placed in service after December 31, 1980.

(2) **PROGRESS EXPENDITURES.**—The amendments made by subsection (b) shall apply to progress expenditures made after December 31, 1980.

(3) **PETROLEUM STORAGE FACILITIES.**—The amendments made by subsection (c) shall apply to periods after December 31, 1980, under rules similar to the rules under section 48(m).

(4) **NONCORPORATE LESSORS.**—The amendments made by subsection (d) shall apply to leases entered into after June 25, 1981.

(5) **AT RISK RULES.**—

(A) **IN GENERAL.**—The amendment made by subsection (f) shall not apply to—

(i) property placed in service by the taxpayer on or before February 18, 1981, and

(ii) property placed in service by the taxpayer after February 18, 1981, where such property is acquired by the taxpayer pursuant to a binding contract entered into on or before that date.

(B) **BINDING CONTRACT.**—For purposes of subparagraph (A)(ii), property acquired pursuant to a binding contract shall, under regulations prescribed by the Secretary, include property acquired in a manner so that it would have qualified as pretermination property under section 49(b) (as in effect before its repeal by the Revenue Act of 1978).

(6) **LEASED ROLLING STOCK.**—The amendment made by subsection (h) shall apply to taxable years beginning after December 31, 1980.

**SEC. 212. INCREASE IN INVESTMENT TAX CREDIT FOR QUALIFIED REHABILITATION EXPENDITURES.**

(a) **INCREASE IN AMOUNT OF CREDIT.**—

(1) **IN GENERAL.**—Subparagraph (A) of section 46(a)(2) (relating to amount of investment tax credit) is amended by striking out “and” at the end of clause (ii), by striking out the period at the end of clause (iii), by inserting in lieu thereof “, and”, and by adding at the end thereof the following new clause:

“(iv) in the case of that portion of the basis of any property which is attributable to qualified rehabilitation expenditures, the rehabilitation percentage.”

(2) **REHABILITATION PERCENTAGE DEFINED.**—Paragraph (2) of section 46(a) is amended by adding at the end thereof the following new subparagraph:

“(F) **REHABILITATION PERCENTAGE.**—For purposes of this paragraph—

“(i) **IN GENERAL.**—

“In the case of qualified rehabilitation expenditures with respect to a:

	The rehabilitation percentage is:
30-year building.....	15
40-year building.....	20
Certified historic structure.....	25.

“(ii) **REGULAR AND ENERGY PERCENTAGES NOT TO APPLY.**—The regular percentage and the energy percentage shall not apply to that portion of the basis of any property which is attributable to qualified rehabilitation expenditures.

“(iii) **DEFINITIONS.**—

“(I) **30-YEAR BUILDING.**—The term ‘30-year building’ means a qualified rehabilitated building other than a 40-year building and other than a certified historic structure.

“(II) **40-YEAR BUILDING.**—The term ‘40-year building’ means any building (other than a certi-

fied historic structure) which would meet the requirements of section 48(g)(1)(B) if '40' were substituted for '30' each place it appears in subparagraph (B) thereof.

**"(III) CERTIFIED HISTORIC STRUCTURE.**—The term 'certified historic structure' has the meaning given to such term by section 48(g)(3)."

**(3) CONFORMING AMENDMENT.**—Section 48(o) (defining certain credits) is amended by adding at the end thereof the following new paragraph:

**"(8) REHABILITATION INVESTMENT CREDIT.**—The term 'rehabilitation investment credit' means that portion of the credit allowable by section 38 which is attributable to the rehabilitation percentage."

**(b) QUALIFIED REHABILITATED BUILDINGS AND EXPENDITURES.**—Subsection (g) of section 48 (relating to special rules for qualified rehabilitated buildings) is amended to read as follows:

**"(g) SPECIAL RULES FOR QUALIFIED REHABILITATED BUILDINGS.**—For purposes of this subpart—

**"(1) QUALIFIED REHABILITATED BUILDING DEFINED.**—

**"(A) IN GENERAL.**—The term 'qualified rehabilitated building' means any building (and its structural components)—

**"(i) which has been substantially rehabilitated,**

**"(ii) which was placed in service before the beginning of the rehabilitation, and**

**"(iii) 75 percent or more of the existing external walls of which are retained in place as external walls in the rehabilitation process.**

**"(B) 30 YEARS MUST HAVE ELAPSED SINCE CONSTRUCTION.**—In the case of a building other than a certified historic structure, a building shall not be a qualified rehabilitated building unless there is a period of at least 30 years between the date the physical work on the rehabilitation began and the date the building was first placed in service.

**"(C) SUBSTANTIALLY REHABILITATED DEFINED.**—

**"(i) IN GENERAL.**—For purposes of subparagraph (A)(i), a building shall be treated as having been substantially rehabilitated only if the qualified rehabilitation expenditures during the 24-month period ending on the last day of the taxable year exceed the greater of—

**"(I) the adjusted basis of such property, or**

**"(II) \$5,000.**

The adjusted basis of the property shall be determined as of the beginning of the first day of such 24-month period, or of the holding period of the property (within the meaning of section 1250(e)), whichever is later.

**"(ii) SPECIAL RULE FOR PHASED REHABILITATION.**—In the case of any rehabilitation which may reasonably be expected to be completed in phases set forth in architectural plans and specifications completed before the rehabilitation begins, clause (i) shall be applied by substituting '60-month period' for '24-month period'.

“(iii) *LESSEES*.—The Secretary shall prescribe by regulation rules for applying this provision to lessees.

“(D) *RECONSTRUCTION*.—Rehabilitation includes reconstruction.

“(2) *QUALIFIED REHABILITATION EXPENDITURE DEFINED*.—

“(A) *IN GENERAL*.—The term ‘qualified rehabilitation expenditure’ means any amount properly chargeable to capital account which is incurred after December 31, 1981—

“(i) for property (or additions or improvements to property) which have a recovery period (within the meaning of section 168) of 15 years, and

“(ii) in connection with the rehabilitation of a qualified rehabilitated building.

“(B) *CERTAIN EXPENDITURES NOT INCLUDED*.—The term ‘qualified rehabilitation expenditure’ does not include—

“(i) *ACCELERATED METHODS OF DEPRECIATION MAY NOT BE USED*.—Any expenditures with respect to which an election has not been made under section 168(b)(3) (to use the straight-line method of depreciation).

“(ii) *COST OF ACQUISITION*.—The cost of acquiring any building or interest therein.

“(iii) *ENLARGEMENTS*.—Any expenditure attributable to the enlargement of an existing building.

“(iv) *CERTIFIED HISTORIC STRUCTURE, ETC*.—Any expenditure attributable to the rehabilitation of a certified historic structure or a building in a registered historic district, unless the rehabilitation is a certified rehabilitation (within the meaning of subparagraph (C)). The preceding sentence shall not apply to a building in a registered historic district if—

“(I) such building was not a certified historic structure,

“(II) the Secretary of the Interior certified to the Secretary that such building is not of historic significance to the district, and

“(III) if the certification referred to in subclause (II) occurs after the beginning of the rehabilitation of such building, the taxpayer certifies to the Secretary that, at the beginning of such rehabilitation, he in good faith was not aware of the requirements of subclause (II).

“(v) *EXPENDITURES OF LESSEE*.—Any expenditure of a lessee of a building if, on the date the rehabilitation is completed, the remaining term of the lease (determined without regard to any renewal periods) is less than 15 years.

“(C) *CERTIFIED REHABILITATION*.—For purposes of subparagraph (B), the term ‘certified rehabilitation’ means any rehabilitation of a certified historic structure which the Secretary of the Interior has certified to the Secretary as being consistent with the historic character of such property or the district in which such property is located.

“(3) *CERTIFIED HISTORIC STRUCTURE DEFINED*.—

**“(A) IN GENERAL.**—The term ‘certified historic structure’ means any building (and its structural components) which—

“(i) is listed in the National Register, or

“(ii) is located in a registered historic district and is certified by the Secretary of the Interior to the Secretary as being of historic significance to the district.

**“(B) REGISTERED HISTORIC DISTRICT.**—The term ‘registered historic district’ means—

“(i) any district listed in the National Register, and

“(ii) any district—

“(I) which is designated under a statute of the appropriate State or local government, if such statute is certified by the Secretary of the Interior to the Secretary as containing criteria which will substantially achieve the purpose of preserving and rehabilitating buildings of historic significance to the district, and

“(II) which is certified by the Secretary of the Interior to the Secretary as meeting substantially all of the requirements for the listing of districts in the National Register.

**“(4) PROPERTY TREATED AS NEW SECTION 38 PROPERTY.**—Property which is treated as section 38 property by reason of subsection (a)(1)(E) shall be treated as new section 38 property.

**“(5) ADJUSTMENT TO BASIS.**—

**“(A) IN GENERAL.**—For purposes of this subtitle, if a credit is allowed under this section for any qualified rehabilitation expenditure in connection with a qualified rehabilitated building other than a certified historic structure, the increase in basis of such property which would (but for this paragraph) result from such expenditure shall be reduced by the amount of the credit so allowed.

**“(B) CERTAIN DISPOSITIONS.**—If during any taxable year there is a recapture amount determined with respect to any qualified rehabilitated building the basis of which was reduced under subparagraph (A), the basis of such building (immediately before the event resulting in such recapture) shall be increased by an amount equal to such recapture amount. For purposes of the preceding sentence, the term ‘recapture amount’ means any increase in tax (or adjustment in carrybacks or carryovers) determined under section 47(a)(5).”

**(c) LODGING TO QUALIFY.**—Paragraph (3) of section 48(a) (relating to property used for lodging) is amended—

(1) by striking out “and” at the end of subparagraph (B),

(2) by striking out the period at the end of subparagraph (C) and inserting in lieu thereof “, and”, and

(3) by adding at the end thereof the following new subparagraph:

“(D) a certified historic structure to the extent of that portion of the basis which is attributable to qualified rehabilitation expenditures.”

**(d) REPEAL OF CERTAIN PROVISIONS RELATING TO HISTORIC STRUCTURES.**—

(1) *IN GENERAL.*—Section 191 (relating to amortization of certain rehabilitation expenditures for certified historic structures) and subsections (n) and (o) of section 167 (relating to depreciation) are hereby repealed.

(2) *CONFORMING AMENDMENTS.*—

(A) Paragraph (8) of section 48(a) (relating to amortized property) is amended by striking out “188, or 191” and inserting in lieu thereof “or 188”.

(B) Paragraph (2) of section 57(a) (relating to items of tax preference) is amended by striking out “or 191”.

(C) Section 280B (relating to demolition of certain historic structures) is amended—

(i) by striking out “section 191(d)(1)” in subsection (a), and inserting in lieu thereof “48(g)(3)(A)”, and

(ii) by striking out “section 191(d)(2)” in subsection (b) and inserting in lieu thereof “section 48(g)(3)(B)”.

(D) Subsection (f) of section 642 (relating to special rules for credits and deductions) is amended by striking out “188, and 191” and inserting in lieu thereof “and 188”.

(E) Subparagraph (B) of section 1082(a)(2) (relating to basis for determining gains or loss) is amended by striking out “188, or 191” and inserting in lieu thereof “or 188”.

(F) Paragraph (2) of section 1245(a) (relating to gain from dispositions of certain depreciable property) and paragraph (4) of section 1250(b) (relating to gain from dispositions of certain depreciable realty) are each amended by inserting “(as in effect before its repeal by the Economic Recovery Tax Act of 1981)” after “191” each place it appears.

(G) Subsection (a) of section 1016 (relating to adjustments to basis) is amended—

(i) by striking out “and” at the end of paragraph (22),

(ii) by striking out the period at the end of paragraph (23) and inserting in lieu thereof “, and”, and

(iii) by adding at the end thereof the following new paragraph:

“(24) to the extent provided in section 48(g)(5), in the case of expenditures with respect to which a credit has been allowed under section 38.”

(e) *EFFECTIVE DATES.*—

(1) *IN GENERAL.*—Except as provided in paragraph (2), the amendments made by this section shall apply to expenditures incurred after December 31, 1981, in taxable years ending after such date.

(2) *TRANSITIONAL RULE.*—The amendments made by this section shall not apply with respect to any rehabilitation of a building if—

(A) the physical work on such rehabilitation began before January 1, 1982, and

(B) such building meets the requirements of paragraph (1) of section 48(g) of the Internal Revenue Code of 1954 (as in effect on the day before the date of enactment of this Act) but does not meet the requirements of such paragraph (1) (as amended by this Act).



**SEC. 213. INVESTMENT CREDIT FOR USED PROPERTY; INCREASE IN DOLLAR LIMIT.**

(a) **IN GENERAL.**—Paragraph (2) of section 48(c) (relating to used section 38 property) is amended by amending subparagraphs (A), (B), and (C) to read as follows:

“(2) **DOLLAR LIMITATION.**—

“(A) **IN GENERAL.**—The cost of used section 38 property taken into account under section 46(c)(1)(B) for any taxable year shall not exceed \$150,000 (\$125,000 for taxable years beginning in 1981, 1982, 1983, or 1984). If such cost exceeds \$150,000 (or \$125,000 as the case may be), the taxpayer shall select (at such time and in such manner as the Secretary shall by regulations prescribe) the items to be taken into account, but only to the extent of an aggregate cost of \$150,000 (or \$125,000). Such a selection, once made, may be changed only in the manner, and to the extent, provided by such regulations.

“(B) **MARRIED INDIVIDUALS.**—In the case of a husband or wife who files a separate return, the limitation under subparagraph (A) shall be \$75,000 (\$62,500 for taxable years beginning in 1981, 1982, 1983, or 1984). This subparagraph shall not apply if the spouse of the taxpayer has no used section 38 property which may be taken into account as qualified investment for the taxable year of such spouse which ends within or with the taxpayer’s taxable year.

“(C) **CONTROLLED GROUPS.**—In the case of a controlled group, the amount specified under subparagraph (A) shall be reduced for each component member of the group by apportioning such amount among the component members of such group in accordance with their respective amounts of used section 38 property which may be taken into account.”

(b) **EFFECTIVE DATE.**—The amendment made by this section shall apply to property placed in service after December 31, 1980.

**SEC. 214. INVESTMENT TAX CREDIT ALLOWED FOR CERTAIN REHABILITATED BUILDINGS LEASED TO TAX-EXEMPT ORGANIZATIONS OR TO GOVERNMENTAL UNITS.**

(a) **USE BY TAX-EXEMPT ORGANIZATIONS.**—Paragraph (4) of section 48(a) (relating to property used by certain tax-exempt organizations) is amended by adding at the end thereof the following new sentence: “If any qualified rehabilitated building is used by the tax-exempt organization pursuant to a lease, this paragraph shall not apply to that portion of the basis of such building which is attributable to qualified rehabilitation expenditures.”

(b) **USE BY GOVERNMENTAL UNITS.**—Paragraph (5) of section 48(a) (relating to governmental units) is amended by adding at the end thereof the following new sentence: “If any qualified rehabilitated building is used by the governmental unit pursuant to a lease, this paragraph shall not apply to that portion of the basis of such building which is attributable to qualified rehabilitation expenditures.”

(c) **EFFECTIVE DATE.**—The amendments made by this section shall apply to uses after July 29, 1980, in taxable years ending after such date.

## **Subtitle C—Incentives for Research and Experimentation**

### **SEC. 221. CREDIT FOR INCREASING RESEARCH ACTIVITIES.**

(a) **GENERAL RULE.**—Subpart A of part IV of subchapter A of chapter 1 (relating to credits allowable) is amended by inserting after section 44E the following new section:

#### **“SEC. 44F. CREDIT FOR INCREASING RESEARCH ACTIVITIES.**

“(a) **GENERAL RULE.**—There shall be allowed as a credit against the tax imposed by this chapter for the taxable year an amount equal to 25 percent of the excess (if any) of—

“(1) the qualified research expenses for the taxable year, over

“(2) the base period research expenses.

“(b) **QUALIFIED RESEARCH EXPENSES.**—For purposes of this section—

“(1) **QUALIFIED RESEARCH EXPENSES.**—The term ‘qualified research expenses’ means the sum of the following amounts which are paid or incurred by the taxpayer during the taxable year in carrying on any trade or business of the taxpayer—

“(A) in-house research expenses, and

“(B) contract research expenses.

“(2) **IN-HOUSE RESEARCH EXPENSES.**—

“(A) **IN GENERAL.**—The term ‘in-house research expenses’ means—

“(i) any wages paid or incurred to an employee for qualified services performed by such employee,

“(ii) any amount paid or incurred for supplies used in the conduct of qualified research, and

“(iii) any amount paid or incurred to another person for the right to use personal property in the conduct of qualified research.

“(B) **QUALIFIED SERVICES.**—The term ‘qualified services’ means services consisting of—

“(i) engaging in qualified research, or

“(ii) engaging in the direct supervision or direct support of research activities which constitute qualified research.

If substantially all of the services performed by an individual for the taxpayer during the taxable year consists of services meeting the requirements of clause (i) or (ii), the term ‘qualified services’ means all of the services performed by such individual for the taxpayer during the taxable year.

“(C) **SUPPLIES.**—The term ‘supplies’ means any tangible property other than—

“(i) land or improvements to land, and

“(ii) property of a character subject to the allowance for depreciation.

“(D) **WAGES.**—

“(i) **IN GENERAL.**—The term ‘wages’ has the meaning given such term by section 3401(a).

“(ii) **SELF-EMPLOYED INDIVIDUALS AND OWNER-EMPLOYEES.**—In the case of an employee (within the meaning of section 401(c)(1)), the term ‘wages’ includes

the earned income (as defined in section 401(c)(2)) of such employee.

“(iii) **EXCLUSION FOR WAGES TO WHICH NEW JOBS OR WIN CREDIT APPLIES.**—The term ‘wages’ shall not include any amount taken into account in computing the credit under section 40 or 44B.

“(3) **CONTRACT RESEARCH EXPENSES.**—

“(A) **IN GENERAL.**—The term ‘contract research expenses’ means 65 percent of any amount paid or incurred by the taxpayer to any person (other than an employee of the taxpayer) for qualified research.

“(B) **PREPAID AMOUNTS.**—If any contract research expenses paid or incurred during any taxable year are attributable to qualified research to be conducted after the close of such taxable year, such amount shall be treated as paid or incurred during the period during which the qualified research is conducted.

“(c) **BASE PERIOD RESEARCH EXPENSES.**—For purposes of this section—

“(1) **IN GENERAL.**—The term ‘base period research expenses’ means the average of the qualified research expenses for each year in the base period.

“(2) **BASE PERIOD.**—

“(A) **IN GENERAL.**—For purposes of this subsection, the term ‘base period’ means the 3 taxable years immediately preceding the taxable year for which the determination is being made (hereinafter in this subsection referred to as the ‘determination year’).

“(B) **TRANSITIONAL RULES.**—Subparagraph (A) shall be applied—

“(i) by substituting ‘first taxable year’ for ‘3 taxable years’ in the case of the first determination year ending after June 30, 1981, and

“(ii) by substituting ‘2’ for ‘3’ in the case of the second determination year ending after June 30, 1981.

“(3) **MINIMUM BASE PERIOD RESEARCH EXPENSES.**—In no event shall the base period research expenses be less than 50 percent of the qualified research expenses for the determination year.

“(d) **QUALIFIED RESEARCH.**—For purposes of this section the term ‘qualified research’ has the same meaning as the term research or experimental has under section 174, except that such term shall not include—

“(1) qualified research conducted outside the United States,

“(2) qualified research in the social sciences or humanities, and

“(3) qualified research to the extent funded by any grant, contract, or otherwise by another person (or any governmental entity).

“(e) **CREDIT AVAILABLE WITH RESPECT TO CERTAIN BASIC RESEARCH BY COLLEGES, UNIVERSITIES, AND CERTAIN RESEARCH ORGANIZATIONS.**—

“(1) **IN GENERAL.**—65 percent of any amount paid or incurred by a corporation (as such term is defined in section 170(e)(4)(D)) to any qualified organization for basic research to be performed by such organization shall be treated as contract research ex-

penses. The preceding sentence shall apply only if the amount is paid or incurred pursuant to a written research agreement between the corporation and the qualified organization.

“(2) **QUALIFIED ORGANIZATION.**—For purposes of this subsection, the term ‘qualified organization’ means—

“(A) any educational organization which is described in section 170(b)(1)(A)(ii) and which is an institution of higher education (as defined in section 3304(f)), and

“(B) any other organization which—

“(i) is described in section 501(c)(3) and exempt from tax under section 501(a),

“(ii) is organized and operated primarily to conduct scientific research, and

“(iii) is not a private foundation.

“(3) **BASIC RESEARCH.**—The term ‘basic research’ means any original investigation for the advancement of scientific knowledge not having a specific commercial objective, except that such term shall not include—

“(A) basic research conducted outside the United States, and

“(B) basic research in the social sciences or humanities.

“(4) **SPECIAL RULES FOR GRANTS TO CERTAIN FUNDS.**—

“(A) **IN GENERAL.**—For purposes of this subsection, a qualified fund shall be treated as a qualified organization and the requirements of paragraph (1) that the basic research be performed by the qualified organization shall not apply.

“(B) **QUALIFIED FUND.**—For purposes of subparagraph (A), the term ‘qualified fund’ means any organization which—

“(i) is described in section 501(c)(3) and exempt from tax under section 501(a) and is not a private foundation,

“(ii) is established and maintained by an organization established before July 10, 1981, which meets the requirements of clause (i),

“(iii) is organized and operated exclusively for purposes of making grants pursuant to written research agreements to organizations described in paragraph (2)(A) for purposes of basic research, and

“(iv) makes an election under this paragraph.

“(C) **EFFECT OF ELECTION.**—

“(i) **IN GENERAL.**—Any organization which makes an election under this paragraph shall be treated as a private foundation for purposes of this title (other than section 4940, relating to excise tax based on investment income).

“(ii) **ELECTION REVOCABLE ONLY WITH CONSENT.**—An election under this paragraph, once made, may be revoked only with the consent of the Secretary.

“(f) **SPECIAL RULES.**—For purposes of this section—

“(1) **AGGREGATION OF EXPENDITURES.**—

“(A) **CONTROLLED GROUP OF CORPORATIONS.**—In determining the amount of the credit under this section—

“(i) all members of the same controlled group of corporations shall be treated as a single taxpayer, and

“(ii) the credit (if any) allowable by this section to each such member shall be its proportionate share of the increase in qualified research expenses giving rise to the credit.

“(B) COMMON CONTROL.—Under regulations prescribed by the Secretary, in determining the amount of the credit under this section—

“(i) all trades or businesses (whether or not incorporated) which are under common control shall be treated as a single taxpayer, and

“(ii) the credit (if any) allowable by this section to each such person shall be its proportionate share of the increase in qualified research expenses giving rise to the credit.

The regulations prescribed under this subparagraph shall be based on principles similar to the principles which apply in the case of subparagraph (A).

“(2) ALLOCATIONS.—

“(A) PASSTHROUGH IN THE CASE OF SUBCHAPTER S CORPORATIONS, ETC.—Under regulations prescribed by the Secretary, rules similar to the rules of subsections (d) and (e) of section 52 shall apply.

“(B) ALLOCATION IN THE CASE OF PARTNERSHIPS.—In the case of partnerships, the credit shall be allocated among partners under regulations prescribed by the Secretary.

“(3) ADJUSTMENTS FOR CERTAIN ACQUISITIONS, ETC.—Under regulations prescribed by the Secretary—

“(A) ACQUISITIONS.—If, after June 30, 1980, a taxpayer acquires the major portion of a trade or business of another person (hereinafter in this paragraph referred to as the ‘predecessor’) or the major portion of a separate unit of a trade or business of a predecessor, then, for purposes of applying this section for any taxable year ending after such acquisition, the amount of qualified research expenses paid or incurred by the taxpayer during periods before such acquisition shall be increased by so much of such expenses paid or incurred by the predecessor with respect to the acquired trade or business as is attributable to the portion of such trade or business or separate unit acquired by the taxpayer.

“(B) DISPOSITIONS.—If, after June 30, 1980—

“(i) a taxpayer disposes of the major portion of any trade or business or the major portion of a separate unit of a trade or business in a transaction to which subparagraph (A) applies, and

“(ii) the taxpayer furnished the acquiring person such information as is necessary for the application of subparagraph (A),

then, for purposes of applying this section for any taxable year ending after such disposition, the amount of qualified research expenses paid or incurred by the taxpayer during periods before such disposition shall be decreased by so much of such expenses as is attributable to the portion of such trade or business or separate unit disposed of by the taxpayer.

**“(C) INCREASE IN BASE PERIOD.**—If during any of the 3 taxable years following the taxable year in which a disposition to which subparagraph (B) applies occurs, the disposing taxpayer (or a person with whom the taxpayer is required to aggregate expenditures under paragraph (1)) reimburses the acquiring person (or a person required to so aggregate expenditures with such person) for research on behalf of the taxpayer, then the amount of qualified research expenses of the taxpayer for the base period for such taxable year shall be increased by the lesser of—

“(i) the amount of the decrease under subparagraph (B) which is allocable to such base period, or

“(ii) the product of the number of years in the base period, multiplied by the amount of the reimbursement described in this subparagraph.

**“(4) SHORT TAXABLE YEARS.**—In the case of any short taxable year, qualified research expenses shall be annualized in such circumstances and under such methods as the Secretary may prescribe by regulation.

**“(5) CONTROLLED GROUP OF CORPORATIONS.**—The term ‘controlled group of corporations’ has the same meaning given to such term by section 1563(a), except that—

“(A) ‘more than 50 percent’ shall be substituted for ‘at least 80 percent’ each place it appears in section 1563(a)(1), and

“(B) the determination shall be made without regard to subsections (a)(4) and (e)(3)(C) of section 1563.

**“(g) LIMITATION BASED ON AMOUNT OF TAX.**—

**“(1) LIABILITY FOR TAX.**—

“(A) **IN GENERAL.**—Except as provided in subparagraph (B), the credit allowed by subsection (a) for any taxable year shall not exceed the amount of the tax imposed by this chapter reduced by the sum of the credits allowable under a section of this part having a lower number or letter designation than this section, other than the credits allowable by sections 31, 39, and 43. For purposes of the preceding sentence, the term ‘tax imposed by this chapter’ shall not include any tax treated as not imposed by this chapter under the last sentence of section 53(a).

“(B) **SPECIAL RULE FOR PASSTHROUGH OF CREDIT.**—In the case of an individual who—

“(i) owns an interest in an unincorporated trade or business,

“(ii) is a partner in a partnership,

“(iii) is a beneficiary of an estate or trust, or

“(iv) is a shareholder in an electing small business corporation (within the meaning of section 1371(b)),

the credit allowed by subsection (a) for any taxable year shall not exceed the lesser of the amount determined under subparagraph (A) for the taxable year or an amount (separately computed with respect to such person’s interest in such trade or business or entity) equal to the amount of tax attributable to that portion of a person’s taxable income which is allocable or apportionable to the person’s interest in such trade or business or entity.

**“(2) CARRYBACK AND CARRYOVER OF UNUSED CREDIT.—**

**“(A) ALLOWANCE OF CREDIT.—***If the amount of the credit determined under this section for any taxable year exceeds the limitation provided by paragraph (1) for such taxable year (hereinafter in this paragraph referred to as the ‘unused credit year’), such excess shall be—*

*“(i) a research credit carryback to each of the 3 taxable years preceding the unused credit year, and*

*“(ii) a research credit carryover to each of the 15 taxable years following the unused credit year, and shall be added to the amount allowable as a credit by this section for such years. If any portion of such excess is a carryback to a taxable year beginning before July 1, 1981, this section shall be deemed to have been in effect for such taxable year for purposes of allowing such carryback as a credit under this section. The entire amount of the unused credit for an unused credit year shall be carried to the earliest of the 18 taxable years to which (by reason of clauses (i) and (ii)) such credit may be carried, and then to each of the other 17 taxable years to the extent that, because of the limitation contained in subparagraph (B), such unused credit may not be added for a prior taxable year to which such unused credit may be carried.*

**“(B) LIMITATION.—***The amount of the unused credit which may be added under subparagraph (A) for any preceding or succeeding taxable year shall not exceed the amount by which the limitation provided by paragraph (1) for such taxable year exceeds the sum of—*

*“(i) the credit allowable under this section for such taxable year, and*

*“(ii) the amounts which, by reason of this paragraph, are added to the amount allowable for such taxable year and which are attributable to taxable years preceding the unused credit year.”*

**(b) TECHNICAL AMENDMENTS RELATED TO CARRYOVER AND CARRYBACK OF CREDITS.—**

**(1) CARRYOVER OF CREDIT.—**

**(A)** *Subparagraph (A) of section 55(c)(4) (relating to carryover and carryback of certain credits) is amended by striking out “section 44E(e)(1)” and inserting in lieu thereof “section 44F(g)(1), 44E(e)(1)”.*

**(B)** *Subsection (c) of section 381 (relating to items of the distributor or transferor corporation) is amended by adding at the end thereof the following new paragraph:*

**“(28) CREDIT UNDER SECTION 44F.—***The acquiring corporation shall take into account (to the extent proper to carry out the purposes of this section and section 44F, and under such regulations as may be prescribed by the Secretary) the items required to be taken into account for purposes of section 44F in respect of the distributor or transferor corporation.”*

**(C)** *Section 383 (relating to special limitations on unused investment credits, work incentive program credits, new employee credits, alcohol fuel credits, foreign taxes, and capital losses), as in effect for taxable years beginning after June 30, 1982, is amended—*

(i) by inserting "to any unused credit of the corporation under section 44F(g)(2)," after "44E(e)(2)," and

(ii) by inserting "RESEARCH CREDITS," after "ALCOHOL FUEL CREDITS," in the section heading.

(D) Section 383 (as in effect on the day before the date of the enactment of the Tax Reform Act of 1976) is amended—

(i) by inserting "to any unused credit of the corporation which could otherwise be carried forward under section 44F(g)(2)," after "44E(e)(2)," and

(ii) by inserting "RESEARCH CREDITS," after "ALCOHOL FUEL CREDITS," in the section heading.

(E) The table of sections for part V of subchapter C of chapter 1 is amended by inserting "alcohol fuel credits, research credits," after "new employee credits," in the item relating to section 383.

**(2) CARRYBACK OF CREDIT.—**

(A) Subparagraph (C) of section 6511(d)(4) (defining credit carryback) is amended by striking out "and new employee credit carryback" and inserting in lieu thereof "new employee credit carryback, and research credit carryback".

(B) Section 6411 (relating to quick refunds in respect of tentative carryback adjustments) is amended—

(i) by striking out "or unused new employee credit" each place it appears and inserting in lieu thereof "unused new employee credit, or unused research credit";

(ii) by inserting "by a research credit carryback provided in section 44F(g)(2)," after "53(b)," in the first sentence of subsection (a);

(iii) by striking out "or a new employee credit carryback from" each place it appears and inserting in lieu thereof "a new employee credit carryback, or a research credit carryback from"; and

(iv) by striking out "work incentive program carryback)" and inserting in lieu thereof "work incentive program carryback, or, in the case of a research credit carryback, to an investment credit carryback, a work incentive program carryback, or a new employee credit carryback)".

**(c) OTHER TECHNICAL AND CLERICAL AMENDMENTS.—**

(1) Subsection (b) of section 6096 (relating to designation of income tax payments to Presidential Election Campaign Fund) is amended by striking out "and 44E" and inserting in lieu thereof "44E, and 44F".

(2) The table of sections for subpart A of part IV of subchapter A of chapter 1 is amended by inserting after the item relating to section 44E the following new item:

"Sec. 44F. Credit for increasing research activities."

**(d) EFFECTIVE DATE.—**

(1) **IN GENERAL.—**The amendments made by this section shall apply to amounts paid or incurred after June 30, 1981, and before January 1, 1986.

**(2) TRANSITIONAL RULE.—**

(A) **IN GENERAL.—**If, with respect to the first taxable year to which the amendments made by this section apply and



which ends in 1981 or 1982, the taxpayer may only take into account qualified research expenses paid or incurred during a portion of such taxable year, the amount of the qualified research expenses taken into account for the base period of such taxable year shall be the amount which bears the same ratio to the total qualified research expenses for such base period as the number of months in such portion of such taxable year bears to the total number of months in such taxable year. A similar rule shall apply in the case of a taxpayer's first taxable year ending after December 31, 1985.

**(B) DEFINITIONS.**—For purposes of the preceding sentence, the terms “qualified research expenses” and “base period” have the meanings given to such terms by section 44F of the Internal Revenue Code of 1954 (as added by this section).

**SEC. 222. CHARITABLE CONTRIBUTIONS OF SCIENTIFIC PROPERTY USED FOR RESEARCH.**

**(a) IN GENERAL.**—Subsection (e) of section 170 (relating to deductions for charitable, etc., contributions and gifts) is amended by adding at the end thereof the following new paragraph:

“(4) **SPECIAL RULE FOR CONTRIBUTIONS OF SCIENTIFIC PROPERTY USED FOR RESEARCH.**—

“(A) **LIMIT ON REDUCTION.**—In the case of a qualified research contribution, the reduction under paragraph (1)(A) shall be no greater than the amount determined under paragraph (3)(B).

“(B) **QUALIFIED RESEARCH CONTRIBUTIONS.**—For purposes of this paragraph, the term ‘qualified research contribution’ means a charitable contribution by a corporation of tangible personal property described in paragraph (1) of section 1221, but only if—

“(i) the contribution is to an educational organization which is described in subsection (b)(1)(A)(ii) of this section and which is an institution of higher education (as defined in section 3304(f)),

“(ii) the property is constructed by the taxpayer,

“(iii) the contribution is made not later than 2 years after the date the construction of the property is substantially completed,

“(iv) the original use of the property is by the donee,

“(v) the property is scientific equipment or apparatus substantially all of the use of which by the donee is for research or experimentation (within the meaning of section 174), or for research training, in the United States in physical or biological sciences,

“(vi) the property is not transferred by the donee in exchange for money, other property, or services, and

“(vii) the taxpayer receives from the donee a written statement representing that its use and disposition of the property will be in accordance with the provisions of clauses (v) and (vi).

“(C) **CONSTRUCTION OF PROPERTY BY TAXPAYER.**—For purposes of this paragraph, property shall be treated as constructed by the taxpayer only if the cost of the parts used in the construction of such property (other than parts manu-

factured by the taxpayer or a related person) do not exceed 50 percent of the taxpayer's basis in such property.

**"(D) CORPORATION.**—For purposes of this paragraph, the term 'corporation' shall not include—

"(i) an electing small business corporation (as defined in section 1371(b)),

"(ii) a personal holding company (as defined in section 542), and

"(iii) a service organization (as defined in section 414(m)(3))."

**(b) EFFECTIVE DATE.**—The amendment made by subsection (a) shall apply to charitable contributions made after the date of the enactment of this Act, in taxable years ending after such date.

**SEC. 223. SUSPENSION OF REGULATIONS RELATING TO ALLOCATION UNDER SECTION 861 OF RESEARCH AND EXPERIMENTAL EXPENDITURES.**

**(a) 2-YEAR SUSPENSION.**—In the case of the taxpayer's first 2 taxable years beginning within 2 years after the date of the enactment of this Act, all research and experimental expenditures (within the meaning of section 174 of the Internal Revenue Code of 1954) which are paid or incurred in such year for research activities conducted in the United States shall be allocated or apportioned to sources within the United States.

**(b) STUDY.**—

**(1) IN GENERAL.**—The Secretary of the Treasury shall conduct a study with respect to the impact which section 1.861-8 of the Internal Revenue Service Regulations would have (A) on research and experimental activities conducted in the United States and (B) on the availability of the foreign tax credit.

**(2) REPORT.**—Not later than the date 6 months after the date of the enactment of this Act, the Secretary of the Treasury shall submit to the Committee on Ways and Means of the House of Representatives and the Committee on Finance of the Senate a report on the study conducted under paragraph (1) (together with such recommendations as he may deem advisable).

## **Subtitle D—Small Business Provisions**

**SEC. 231. REDUCTION IN CORPORATE TAX RATES.**

**(a) IN GENERAL.**—Subsection (b) of section 11 (relating to amount of corporate tax) is amended—

(1) by striking out "17 percent" in paragraph (1) and inserting in lieu thereof "15 percent" (16 percent for taxable years beginning in 1982)", and

(2) by striking out "20 percent" in paragraph (2) and inserting in lieu thereof "18 percent (19 percent for taxable years beginning in 1982)".

**(b) CONFORMING AMENDMENTS.**—

(1) Paragraph (2) of section 821(a) (relating to imposition of tax on mutual insurance companies to which part II applies) is amended to read as follows:

"(2) **CAP ON TAX WHERE INCOME IS LESS THAN \$12,000.**—The tax imposed by paragraph (1) on so much of the mutual insurance company taxable income as does not exceed \$12,000 shall not exceed 32 percent (30 percent for taxable years beginning

after December 31, 1982) of the amount by which such income exceeds \$6,000.”

(2) Subparagraph (B) of section 821(c)(1) (relating to imposition of alternative tax for certain small companies) is amended to read as follows:

“(B) **CAP WHERE INCOME IS LESS THAN \$6,000.**—The tax imposed by subparagraph (A) on so much of the taxable investment income as does not exceed \$6,000 shall not exceed 32 percent (30 percent for taxable years beginning after December 31, 1982) of the amount by which such income exceeds \$3,000.”

(3) The amendments made by paragraphs (1) and (2) shall apply to taxable years beginning after December 31, 1978; except that for purposes of applying sections 821(a)(2) and 821(c)(1)(B) of the Internal Revenue Code of 1954 (as amended by this subsection) to taxable years beginning before January 1, 1982, the percentage referred to in such section shall be deemed to be 34 percent.

(c) **EFFECTIVE DATE.**—The amendments made by subsection (a) shall apply to taxable years beginning after December 31, 1981.

**SEC. 232. INCREASE IN ACCUMULATED EARNINGS CREDIT.**

(a) **INCREASE IN CREDIT FOR CERTAIN CORPORATIONS.**—Paragraph (2) of section 535(c) (relating to accumulated earnings credit) is amended to read as follows:

“(2) **MINIMUM CREDIT.**—

“(A) **IN GENERAL.**—The credit allowable under paragraph (1) shall in no case be less than the amount by which \$250,000 exceeds the accumulated earnings and profits of the corporation at the close of the preceding taxable year.

“(B) **CERTAIN SERVICE CORPORATIONS.**—In the case of a corporation the principal function of which is the performance of services in the field of health, law, engineering, architecture, accounting, actuarial science, performing arts, or consulting, subparagraph (A) shall be applied by substituting ‘\$150,000’ for ‘\$250,000’.”

(b) **CONFORMING AMENDMENTS.**—

(1) Paragraph (3) of section 535(c) is amended by striking out “\$150,000” and inserting in lieu thereof “\$250,000”.

(2) Sections 243(b)(3)(C)(i) (relating to qualifying dividends for purposes of the dividends received deduction) and 1551(a) (relating to disallowance of surtax exemption and accumulated earnings credit) are each amended by striking out “\$150,000”.

(3) Section 1561(a)(2) (relating to limitations on certain multiple tax benefits in the case of certain controlled corporations) is amended by striking out “\$150,000” and inserting in lieu thereof “\$250,000 (\$150,000 if any component member is a corporation described in section 535(c)(2)(B))”.

(c) **EFFECTIVE DATE.**—The amendments made by this section shall apply to taxable years beginning after December 31, 1981.

**SEC. 233. SUBCHAPTER S SHAREHOLDERS.**

(a) **INCREASE IN NUMBER OF SHAREHOLDERS.**—Section 1371(a) (defining small business corporation) is amended by striking out “15 shareholders” in paragraph (1) and inserting in lieu thereof “25 shareholders”.

(b) **EFFECTIVE DATE.**—The amendment made by this section shall apply with respect to taxable years beginning after December 31, 1981.

**SEC. 234. TREATMENT OF TRUSTS AS SUBCHAPTER S SHAREHOLDERS.**

(a) **IN GENERAL.**—Subsection (e) of section 1371 (relating to certain trusts permitted as shareholders) is amended to read as follows:

“(e) **CERTAIN TRUSTS PERMITTED AS SHAREHOLDERS.**—

“(1) **IN GENERAL.**—For purposes of subsection (a), the following trusts may be shareholders:

“(A) A trust all of which is treated (under subpart E of part I of subchapter J of this chapter) as owned by an individual who is a citizen or resident of the United States.

“(B) A trust which was described in subparagraph (A) immediately before the death of the deemed owner and which continues in existence after such death, but only for the 60-day period beginning on the day of the deemed owner's death. If a trust is described in the preceding sentence and if the entire corpus of the trust is includible in the gross estate of the deemed owner, the preceding sentence shall be applied by substituting ‘2-year period’ for ‘60-day period’.

“(C) A trust with respect to stock transferred to it pursuant to the terms of a will, but only for the 60-day period beginning on the day on which such stock is transferred to it.

“(D) A trust created primarily to exercise the voting power of stock transferred to it.

“(2) **TREATMENT AS SHAREHOLDERS.**—For purposes of subsection (a)—

“(A) In the case of a trust described in subparagraph (A) of paragraph (1), the deemed owner shall be treated as the shareholder.

“(B) In the case of a trust described in subparagraph (B) of paragraph (1), the estate of the deemed owner shall be treated as the shareholder.

“(C) In the case of a trust described in subparagraph (C) of paragraph (1), the estate of the testator shall be treated as the shareholder.

“(D) In the case of a trust described in subparagraph (D) of paragraph (1), each beneficiary of the trust shall be treated as a shareholder.”

(b) **QUALIFIED SUBCHAPTER S TRUSTS.**—Section 1371 is amended by adding at the end thereof the following new subsection:

“(g) **SPECIAL RULE FOR QUALIFIED SUBCHAPTER S TRUST.**—

“(1) **IN GENERAL.**—In the case of a qualified subchapter S trust with respect to which a beneficiary makes an election under paragraph (2)—

“(A) such trust shall be treated as a trust described in subsection (e)(1)(A), and

“(B) for purposes of section 678(a), the beneficiary of such trust shall be treated as the owner of that portion of the trust which consists of stock in an electing small business corporation with respect to which the election under paragraph (2) is made.

“(2) **ELECTION.**—

**“(A) IN GENERAL.**—A beneficiary of a qualified subchapter S trust (or his legal representative) may elect to have this subsection apply.

**“(B) MANNER AND TIME OF ELECTION.**—An election under this paragraph shall be made—

“(i) separately with respect to each electing small business corporation the stock of which is held by the trust,

“(ii) separately with respect to each successive income beneficiary of the trust, and

“(iii) in such manner and form, and at such time, as the Secretary may prescribe.

**“(C) ELECTION IRREVOCABLE.**—An election under this paragraph, once made, may be revoked only with the consent of the Secretary.

**“(D) GRACE PERIOD.**—An election under this paragraph shall be effective up to 60 days before the date of the election.

**“(3) QUALIFIED SUBCHAPTER S TRUST.**—For purposes of this subsection, the term ‘qualified subchapter S trust’ means a trust—

“(A) which owns stock in 1 or more electing small business corporations,

“(B) all of the income of which is distributed currently to one individual who is a citizen or resident of the United States, and

“(C) the terms of which require that—

“(i) at any time, there shall be only one income beneficiary of the trust,

“(ii) any corpus distributed during the term of the trust may be distributed only to the current income beneficiary thereof,

“(iii) each income interest in the trust shall terminate on the earlier of the death of the income beneficiary or the termination of the trust, and

“(iv) upon the termination of the trust during the life of an income beneficiary, the trust shall distribute all of its assets to such income beneficiary.

**“(4) TRUST CEASING TO BE QUALIFIED.**—If a qualified subchapter S trust ceases to meet any requirement under paragraph (3), the provisions of this subsection shall not apply to such trust as of the date it ceases to meet such requirements.”

**(c) EFFECTIVE DATE.**—The amendments made by this section shall apply to taxable years beginning after December 31, 1981.

**SEC. 235. SIMPLIFICATION OF LIFO BY USE OF GOVERNMENT INDEXES TO BE PROVIDED BY REGULATIONS.**

Section 472 is amended by adding at the end thereof the following new subsection:

**“(f) USE OF GOVERNMENT PRICE INDEXES IN PRICING INVENTORY.**—The Secretary shall prescribe regulations permitting the use of suitable published governmental indexes in such manner and circumstances as determined by the Secretary for purposes of the method described in subsection (b).”

**SEC. 236. 3-YEAR AVERAGING PERMITTED FOR INCREASES IN INVENTORY VALUE.**

(a) **GENERAL RULE.**—Subsection (d) of section 472 is amended to read as follows:

“(d) **3-YEAR AVERAGING FOR INCREASES IN INVENTORY VALUE.**—The beginning inventory for the first taxable year for which the method described in subsection (b) is used shall be valued at cost. Any change in the inventory amount resulting from the application of the preceding sentence shall be taken into account ratably in each of the 3 taxable years beginning with the first taxable year for which the method described in subsection (b) is first used.”

(b) **EFFECTIVE DATE.**—The amendment made by subsection (a) shall apply to taxable years beginning after December 31, 1981.

**SEC. 237. ELECTION BY SMALL BUSINESS TO USE ONE INVENTORY POOL WHEN LIFO IS ELECTED.**

(a) **IN GENERAL.**—Subpart D of part II of subchapter E of chapter 1 (relating to inventories) is amended by adding at the end thereof the following new section:

**“SEC. 474. ELECTION BY CERTAIN SMALL BUSINESSES TO USE ONE INVENTORY POOL.**

“(a) **IN GENERAL.**—A taxpayer which is an eligible small business and which uses the dollar-value method of pricing inventories under the method provided by section 472(b) may elect to use one inventory pool for any trade or business of such taxpayer.

“(b) **ELIGIBLE SMALL BUSINESS DEFINED.**—For purposes of this section, a taxpayer is an eligible small business for any taxable year if the average annual gross receipts of the taxpayer do not exceed \$2,000,000 for the 3-taxable-year period ending with the taxable year.

“(c) **SPECIAL RULES.**—For purposes of this section—

“(1) **CONTROLLED GROUPS.**—

“(A) **IN GENERAL.**—In the case of a taxpayer which is a member of a controlled group, all persons which are component members of such group at any time during the calendar year shall be treated as one taxpayer for such year for purposes of determining the gross receipts of the taxpayer.

“(B) **CONTROLLED GROUP DEFINED.**—For purposes of subparagraph (A), persons shall be treated as being members of a controlled group if such persons would be treated as a single employer under the regulations prescribed under section 52(b).

“(2) **ELECTION.**—

“(A) **IN GENERAL.**—The election under this section may be made without the consent of the Secretary and shall be made at such time and in such manner as the Secretary may by regulations prescribe.

“(B) **PERIOD TO WHICH ELECTION APPLIES.**—The election under this section shall apply—

“(i) to the taxable year for which it is made, and

“(ii) to all subsequent taxable years for which the taxpayer is an eligible small business,

unless the taxpayer secures the consent of the Secretary to the revocation of such election.

“(3) **TRANSITIONAL RULES.**—In the case of a taxpayer who changes the number of inventory pools maintained by him in a

taxable year by reason of an election (or cessation thereof) under this section—

“(A) the inventory pools combined or separated shall be combined or separated in the manner provided by regulations under section 472;

“(B) the aggregate dollar value of the taxpayer’s inventory as of the beginning of the first taxable year—

“(i) for which an election under this section is in effect, or

“(ii) after such election ceases to apply, shall be the same as the aggregate dollar value as of the close of the taxable year preceding the taxable year described in clause (i) or (ii) (as the case may be), and

“(C) the first taxable year for which an election under this section is in effect or after such election ceases to apply (as the case may be) shall be treated as a new base year in accordance with procedures provided by regulations under section 472.”

(b) **CLERICAL AMENDMENT.**—The table of sections for such subpart D is amended by adding at the end thereof the following new item:

“Sec. 474. Election by certain small businesses to use one inventory pool.”

(c) **EFFECTIVE DATE.**—The amendments made by this section shall apply to taxable years beginning after December 31, 1981.

**SEC. 238. STUDY OF ACCOUNTING METHODS FOR INVENTORY.**

(a) **STUDY.**—The Secretary of the Treasury shall conduct a full and complete study of methods of tax accounting for inventory with a view toward the development of simplified methods. Such study shall include (but shall not be limited to) an examination of the last-in first-out method and the cash receipts and disbursements method.

(b) **REPORT.**—Not later than December 31, 1982, the Secretary of the Treasury shall submit to the Committee on Ways and Means of the House of Representatives and to the Committee on Finance of the Senate a report on the study conducted under subsection (a), together with such recommendations as he deems appropriate.

## **Subtitle E—Savings and Loan Associations**

**SEC. 241. REORGANIZATIONS INVOLVING FINANCIALLY TROUBLED THRIFT INSTITUTIONS.**

**AMENDMENT OF SECTION 368(a)(3)(D).**—Section 368(a)(3)(D) (relating to agency receivership proceedings which involve financial institutions) is amended to read as follows:

“(D) **AGENCY PROCEEDINGS WHICH INVOLVE FINANCIAL INSTITUTIONS.**—

“(i) For purpose of subparagraphs (A) and (B)—

“(I) In the case of a receivership, foreclosure, or similar proceeding before a Federal or State agency involving a financial institution to which section 585 applies, the agency shall be treated as a court, and

“(II) In the case of a financial institution to which section 593 applies, the term ‘title 11 or sim-

ilar case' means only a case in which the Board (which will be treated as the court in such case) makes the certification described in clause (ii).

"(ii) A transaction otherwise meeting the requirements of subparagraph (G) of paragraph (1), in which the transferor corporation is a financial institution to which section 593 applies, will not be disqualified as a reorganization if no stock or securities of the corporation to which the assets are transferred (transferee) are received or distributed, but only if all of the following conditions are met:

"(I) the requirements of subparagraphs (A) and (B) of section 354(b)(1) are met with respect to the acquisition of the assets,

"(II) substantially all of the liabilities of the transferor immediately before the transfer become, as a result of the transfer, liabilities of the transferee, and

"(III) the Board certifies that the grounds set forth in section 1464(d)(6)(A) (i), (ii), or (iii) of title 12, United States Code, exist with respect to the transferor or will exist in the near future in the absence of action by the Board.

"(iii) For purposes of this subparagraph, the 'Board' means the Federal Home Loan Bank Board or the Federal Savings and Loan Insurance Corporation or, if neither has supervisory authority with respect to the transferor, the equivalent State authority."

#### **SEC. 242. LIMITATIONS ON CARRYOVERS OF FINANCIAL INSTITUTIONS.**

Section 382(b)(7) (relating to reduction of net operating loss carryovers in title 11 or similar cases), as added by section 2(d) of Public Law 96-589, is amended to read as follows:

"(7) **SPECIAL RULE FOR REORGANIZATIONS IN TITLE 11 OR SIMILAR CASES.**—For purposes of this subsection—

"(A) a creditor who receives stock in a reorganization in a title 11 or similar case (within the meaning of section 368(a)(3)(A)) shall be treated as a stockholder immediately before the reorganization and

"(B) in a transaction qualifying under section 368(a)(3)(D)(ii)—

"(i) a depositor in the transferor shall be treated as a stockholder immediately before the reorganization of the loss corporation,

"(ii) deposits in the transferor which become, as a result of the transfer, deposits in the transferee shall be treated as stock of the acquiring corporation owned as a result of owning stock of the loss corporation, and

"(iii) the fair market value of the outstanding stock of the acquiring corporation shall include the amount of deposits in the acquiring corporation immediately after the reorganization.

#### **SEC. 243. RESERVES FOR LOSSES ON LOANS.**

Paragraph (1) of section 593(e) (relating to distributions to shareholders of a domestic building and loan association) is amended by striking out "applies." in the last sentence thereof and substituting



therefor the following: "applies, or to any distribution to the Federal Savings and Loan Insurance Corporation in redemption of an interest in an association, if such interest was originally received by the Federal Savings and Loan Insurance Corporation in exchange for financial assistance pursuant to section 406(f) of the National Housing Act (12 U.S.C. sec. 1729(f))."

**SEC. 244. FSLIC FINANCIAL ASSISTANCE.**

(a) *IN GENERAL.*—Part II of subchapter H of subtitle A of chapter 1 is amended by adding at the end thereof the following new section:

**"SEC. 597. FSLIC FINANCIAL ASSISTANCE.**

"(a) *EXCLUSION FROM GROSS INCOME.*—Gross income of a domestic building and loan association does not include any amount of money or other property received from the Federal Savings and Loan Insurance Corporation pursuant to section 406(f) of the National Housing Act (12 U.S.C. sec. 1729(f)), regardless of whether any note or other instrument is issued in exchange therefor.

"(b) *NO REDUCTION IN BASIS OF ASSETS.*—No reduction in the basis of assets of a domestic building and loan association shall be made on account of money or other property received under the circumstances referred to in subsection (a)."

(b) *CLERICAL AMENDMENT.*—The table of sections for part II of subchapter H of chapter 1 is amended by inserting after the item relating to section 596 the following:

"Sec. 597. FSLIC financial assistance."

**SEC. 245. MUTUAL SAVINGS BANKS WITH CAPITAL STOCK.**

(a) *IN GENERAL.*—Section 591 (relating to dividends paid on deposits) is amended—

(1) by inserting "(a) *IN GENERAL.*—" before "In", and

(2) by adding at the end thereof the following new subsection:

"(b) *MUTUAL SAVINGS BANK TO INCLUDE CERTAIN BANKS WITH CAPITAL STOCK.*—For purposes of this part, the term 'mutual savings bank' includes any bank—

"(1) which has capital stock represented by shares, and

"(2) which is subject to, and operates under, Federal or State laws relating to mutual savings bank."

(b) *PERCENTAGE OF TAXABLE INCOME METHOD.*—

(1) Subparagraph (B) of section 593(b)(2) (relating to reduction of applicable percentage in certain cases) is amended by inserting "which is not described in section 591(b)" after "mutual savings bank" each place it appears.

(2) Subparagraph (C) of section 593(b)(2) is amended by inserting "which are not described in section 591(b)" after "mutual savings banks".

(c) *CONFORMING AMENDMENTS.*—

(1) Sections 593(a) (relating to reserves for losses on loans) is amended by striking out "not having capital stock represented by shares".

(2) Paragraph (1) of section 593(e) (relating to distributions to shareholders) is amended by inserting "or an institution that is treated as a mutual savings bank under section 591(b)" after "association" each place it appears.

**SEC. 246. EFFECTIVE DATES.**

(a) The amendment made by sections 241 and 242 shall apply to any transfer made on or after January 1, 1981.

(b) The amendment made by section 243 shall apply to any distribution made on or after January 1, 1981.

(c) The amendment made by section 244 shall apply to any payment made on or after January 1, 1981.

(d) The amendments made by section 245 shall apply with respect to taxable years ending after the date of the enactment of this Act.

### **Subtitle F—Stock Options, etc.**

**SEC. 251. STOCK OPTIONS.**

(a) **IN GENERAL.**—Part II of subchapter D of chapter 1 (relating to certain stock options) is amended by adding after section 422 the following new section:

**“SEC. 422A. INCENTIVE STOCK OPTIONS.**

“(a) **IN GENERAL.**—Section 421(a) shall apply with respect to the transfer of a share of stock to an individual pursuant to his exercise of an incentive stock option if—

“(1) no disposition of such share is made by him within 2 years from the date of the granting of the option nor within 1 year after the transfer of such share to him, and

“(2) at all times during the period beginning on the date of the granting of the option and ending on the day 3 months before the date of such exercise, such individual was an employee of either the corporation granting such option, a parent or subsidiary corporation of such corporation, or a corporation or a parent or subsidiary corporation of such corporation issuing or assuming a stock option in a transaction to which section 425(a) applies.

“(b) **INCENTIVE STOCK OPTION.**—For purposes of this part, the term ‘incentive stock option’ means an option granted to an individual for any reason connected with his employment by a corporation, if granted by the employer corporation or its parent or subsidiary corporation, to purchase stock of any of such corporations, but only if—

“(1) the option is granted pursuant to a plan which includes the aggregate number of shares which may be issued under options and the employees (or class of employees) eligible to receive options, and which is approved by the stockholders of the granting corporation within 12 months before or after the date such plan is adopted;

“(2) such option is granted within 10 years from the date such plan is adopted, or the date such plan is approved by the stockholders, whichever is earlier;

“(3) such option by its terms is not exercisable after the expiration of ten years from the date such option is granted;

“(4) the option price is not less than the fair market value of the stock at the time such option is granted;

“(5) such option by its terms is not transferable by such individual otherwise than by will or the laws of descent and distribution, and is exercisable, during his lifetime, only by him;

*“(6) such individual, at the time the option is granted, does not own stock possessing more than 10 percent of the total combined voting power of all classes of stock of the employer corporation or of its parent or subsidiary corporation;*

*“(7) such option by its terms is not exercisable while there is outstanding (within the meaning of subsection (c)(7)) any incentive stock option which was granted, before the granting of such option, to such individual to purchase stock in his employer corporation or in a corporation which (at the time of the granting of such option) is a parent or subsidiary corporation of the employer corporation, or in a predecessor corporation of any of such corporations; and*

*“(8) in the case of an option granted after December 31, 1980, under the terms of the plan the aggregate fair market value (determined as of the time the option is granted) of the stock for which any employee may be granted options in any calendar year (under all such plans of his employer corporation and its parent and subsidiary corporation) shall not exceed \$100,000 plus any unused limit carryover to such year.*

**“(c) SPECIAL RULES.—**

*“(1) EXERCISE OF OPTION WHEN PRICE IS LESS THAN VALUE OF STOCK.—If a share of stock is transferred pursuant to the exercise by an individual of an option which would fail to qualify as an incentive stock option under subsection (b) because there was a failure in an attempt, made in good faith, to meet the requirement of subsection (b)(4), the requirement of subsection (b)(4) shall be considered to have been met.*

*“(2) CERTAIN DISQUALIFYING DISPOSITIONS WHERE AMOUNT REALIZED IS LESS THAN VALUE AT EXERCISE.—If—*

*“(A) an individual who has acquired a share of stock by the exercise of an incentive stock option makes a disposition of such share within the 2-year period described in subsection (a)(1), and*

*“(B) such disposition is a sale or exchange with respect to which a loss (if sustained) would be recognized to such individual,*

*then the amount which is includible in the gross income of such individual, and the amount which is deductible from the income of his employer corporation, as compensation attributable to the exercise of such option shall not exceed the excess (if any) of the amount realized on such sale or exchange over the adjusted basis of such share.*

*“(3) CERTAIN TRANSFERS BY INSOLVENT INDIVIDUALS.—If an insolvent individual holds a share of stock acquired pursuant to his exercise of an incentive stock option, and if such share is transferred to a trustee, receiver, or other similar fiduciary in any proceeding under title 11 or any other similar insolvency proceeding, neither such transfer, nor any other transfer of such share for the benefit of his creditors in such proceeding, shall constitute a disposition of such share for purposes of subsection (a)(1).*

*“(4) CARRYOVER OF UNUSED LIMIT.—*

*“(A) IN GENERAL.—If—*

*“(i) \$100,000 exceeds,*

“(ii) the aggregate fair market value (determined as of the time the option is granted) of the stock for which an employee was granted options in any calendar year after 1980 (under all plans described in subsection (b) of his employer corporation and its parent and subsidiary corporations),

one-half of such excess shall be unused limit carry-over to each of the 3 succeeding calendar years.

“(B) AMOUNT CARRIED TO EACH YEAR.—The amount of the unused limit carryover from any calendar year which may be taken into account in any succeeding calendar year shall be the amount of such carryover reduced by the amount of such carryover which was used in prior calendar years.

“(C) SPECIAL RULES.—For purposes of subparagraph (B)—

“(i) the amount of options granted during any calendar year shall be treated as first using up the \$100,000 limitation of subsection (b)(8), and

“(ii) then shall be treated as using up unused limit carryovers to such year in the order of the calendar years in which the carryovers arose.

(5) PERMISSIBLE PROVISIONS.—An option which meets the requirements of subsection (b) shall be treated as an incentive stock option even if—

“(A) the employee may pay for the stock with stock of the corporation granting the option,

“(B) the employee has a right to receive property at the time of exercise of the option, or

“(C) the option is subject to any condition not inconsistent with the provisions of subsection (b).

Subparagraph (B) shall apply to a transfer of property (other than cash) only if section 83 applies to the property so transferred.

“(6) COORDINATION WITH SECTIONS 422 AND 424.—Sections 422 and 424 shall not apply to an incentive stock option.

“(7) OPTIONS OUTSTANDING.—For purposes of subsection (b)(7), any incentive stock option shall be treated as outstanding until such option is exercised in full or expires by reason of lapse of time.

“(8) 10-PERCENT SHAREHOLDER RULE.—Subsection (b)(6) shall not apply if at the time such option is granted the option price is at least 110 percent of the fair market value of the stock subject to the option and such option by its terms is not exercisable after the expiration of 5 years from the date such option is granted.

“(9) SPECIAL RULE WHEN DISABLED.—For purposes of subsection (a)(2), in the case of an employee who is disabled (within the meaning of section 105(d)(4)), the 3-month period of subsection (a)(2) shall be 1 year.”

(b) TECHNICAL AND CONFORMING AMENDMENTS.—

(1) Section 421 (relating to general rules in the case of stock options) is amended—

(A) by inserting “422A(a),” after “422(a),” in subsections (a), (b), and (c)(1)(A), and

(B) by inserting "422A(a)(1)," after "section 422(a)(1)," in subsection (b).

(2) Section 425(d) (relating to attribution of stock ownership) is amended by inserting "422A(b)(6)," after "422(b)(7),".

(3) Section 425(g) (relating to special rules) is amended by inserting "422A(a)(2)," after "422(a)(2),".

(4) Section 425(h)(3)(B) (relating to definition of modification) is amended by inserting "422A(b)(5)," after "422(b)(6),".

(5) Section 6039 (relating to information required in connection with certain options) is amended—

(A) by inserting ", an incentive stock option," after "qualified stock option" in subsection (a)(1),

(B) by inserting "incentive stock option," after "qualified stock option," in subsection (b)(1), and

(C) by adding at the end of subsection (c) the following new paragraph:

"(4) The term 'incentive stock option', see section 422A(b)."

(6) The table of sections for part II of subchapter D of chapter 1 is amended by inserting after the item relating to section 422 the following new item:

"Sec. 422A. Incentive stock options."

**(c) EFFECTIVE DATES AND TRANSITIONAL RULES.—**

**(1) OPTIONS TO WHICH SECTION APPLIES.—**

(A) **IN GENERAL.**—Except as provided in subparagraph (B), the amendments made by this section shall apply with respect to options granted on or after January 1, 1976, and exercised on or after January 1, 1981, or outstanding on such date.

(B) **ELECTION AND DESIGNATION OF OPTIONS.**—In the case of an option granted before January 1, 1980, the amendments made by this section shall apply only if the corporation granting such option elects (in the manner and at the time prescribed by the Secretary of the Treasury or his delegate) to have the amendments made by this section apply to such option. The aggregate fair market value (determined at the time the option is granted) of the stock for which any employee was granted options (under all plans of his employer corporation and its parent and subsidiary corporations) to which the amendments made by this section apply by reason of this subparagraph shall not exceed \$50,000 per calendar year and shall not exceed \$200,000 in the aggregate.

(2) **CHANGES IN TERMS OF OPTIONS.**—In the case of an option granted on or after January 1, 1976, and outstanding on the date of the enactment of this Act, paragraph (1) of section 425(h) of the Internal Revenue Code of 1954 shall not apply to any change in the terms of such option (or the terms of the plan under which granted, including shareholder approval) made within 1 year after such date of enactment to permit such option to qualify as a incentive stock option.

**SEC. 252. PROPERTY TRANSFERRED TO EMPLOYEES SUBJECT TO CERTAIN RESTRICTIONS.**

(a) **GENERAL RULE.**—Subsection (c) of section 83 (relating to special rules) is amended by adding at the end thereof the following new paragraph:

**“(3) SALES WHICH MAY GIVE RISE TO SUIT UNDER SECTION 16(b) OF THE SECURITIES AND EXCHANGE ACT OF 1934.**—So long as the sale of property at a profit could subject a person to suit under section 16(b) of the Securities and Exchange Act of 1934, such person’s rights in such property are—

- “(A) subject to a substantial risk of forfeiture, and  
“(B) not transferable.”

**(b) SPECIAL RULE FOR CERTAIN ACCOUNTING RULES.**—For purposes of section 83 of the Internal Revenue Code of 1954, property is subject to substantial risk of forfeiture and is not transferable so long as such property is subject to a restriction on transfer to comply with the “Pooling-of-Interests Accounting” rules set forth in Accounting Series Release Numbered 130 ((10/5/72) 37 FR 20937; 17 CFR 211.130) and Accounting Series Release Numbered 135 ((1/18/73) 38 FR 1734; 17 CFR 211.135).

**(c) EFFECTIVE DATE.**—The amendment made by subsection (a) and the provisions of subsection (b) shall apply to taxable years ending after December 31, 1981.

## **Subtitle G—Miscellaneous Provisions**

### **SEC. 261. ADJUSTMENTS TO NEW JOBS CREDIT.**

**(a) EXTENSION.**—Paragraph (4) of section 51(c) (defining wages) is amended to read as follows:

“(4) **TERMINATION.**—The term ‘wages’ shall not include any amount paid or incurred to an individual who begins work for the employer after December 31, 1982.”

**(b) INDIVIDUALS QUALIFYING AS MEMBERS OF A TARGETED GROUP.**—

**(1) IN GENERAL.**—Paragraph (1) of section 51(d) (defining members of targeted groups) is amended by striking out “or” at the end of subparagraph (F), by striking out the period at the end of subparagraph (G) and inserting in lieu thereof a comma, and by adding at the end thereof the following new subparagraphs:

“(H) an eligible work incentive employee, or

“(I) an involuntarily terminated CETA employee.”

**(2) DEFINITIONS.**—

**(A) IN GENERAL.**—Subsection (d) of section 51 is amended by redesignating paragraphs (9), (10), (11), and (12) as paragraphs (11), (12), (13), and (14,) respectively, and by inserting after paragraph (8) the following new paragraph:

“(9) **ELIGIBLE WORK INCENTIVE EMPLOYEES.**—The term ‘eligible work incentive employee’ means an individual who has been certified by the designated local agency as—

“(A) being eligible for financial assistance under part A of title IV of the Social Security Act and as having continually received such financial assistance during the 90-day period which immediately precedes the date on which such individual is hired by the employer, or

“(B) having been placed in employment under a work incentive program established under section 432(b)(1) of the Social Security Act.

“(10) **INVOLUNTARILY TERMINATED CETA EMPLOYEE.**—The term ‘involuntarily terminated CETA employee’ means an individual

who is certified by the designated local agency as having been involuntarily terminated after December 31, 1980, from employment financed in whole or in part under a program under part D of title II or title VI of the Comprehensive Employment and Training Act."

**(B) CONFORMING AMENDMENTS.—**

(i) Subsection (a) of section 50B (relating to definitions and special rules) is amended by adding at the end thereof the following new paragraph:

"(5) **TERMINATION.**—The term 'work incentive program expenses; shall not include any amount paid or incurred in any taxable year beginning after December 31, 1981.'"

(ii) subsection (c) of section 51 (defining wages) is amended by striking out paragraph (3) and redesignating paragraph (4) as paragraph (3).

(iii) Paragraphs (3)(A)(ii), (4)(C), and (7)(B) of section 51(d) are each amended by striking out "paragraph (9)" and inserting in lieu thereof "paragraph (11)".

**(3) REMOVAL OF AGE LIMITATION ON VIETNAM VETERANS.—** Paragraph (4) of section 51(d) (relating to Vietnam veterans) is amended—

(A) by inserting "and" at the end of subparagraph (B),

(B) by striking out ", and" at the end of subparagraph (C) and inserting in lieu thereof a period, and

(C) by striking out subparagraph (D).

**(4) YOUTHS PARTICIPATING IN QUALIFIED COOPERATIVE EDUCATION PROGRAMS MUST BE ECONOMICALLY DISADVANTAGED.—** Subparagraph (A) of section 51(d)(8) is amended by striking out "and" at the end of clause (ii), by striking out the period at the end of clause (iii) and inserting in lieu thereof ", and", and by adding at the end thereof the following new clause:

"(iv) being a member of an economically disadvantaged family (as determined under paragraph (11))."

**(c) CERTIFICATIONS.—**

**(1) CERTIFICATIONS MUST BE MADE BEFORE EMPLOYEE BEGINS WORK, ETC.—** Subsection (d) of section 51 is amended by adding at the end thereof the following new paragraph:

"(15) **SPECIAL RULES FOR CERTIFICATIONS.—**

"(A) **IN GENERAL.**—An individual shall not be treated as a member of a targeted group unless, before the day on which such individual begins work for the employer, the employer—

"(i) has received a certification from a designated local agency that such individual is a member of a targeted group, or

"(ii) has requested in writing such certification from the designated local agency.

"(B) **INCORRECT CERTIFICATIONS.—**If—

"(i) an individual has been certified as a member of a targeted group, and

"(ii) such certification is incorrect because it was based on false information provided by such individual,

the certification shall be revoked and wages paid by the employer after the date on which notice of revocation is re-

ceived by the employer shall not be treated as qualified wages."

(2) **CERTIFICATION OF ECONOMICALLY DISADVANTAGED FAMILIES.**—Paragraph (11) of section 51(d) (as redesignated by subsection (b)(2)(A)) is amended to read as follows:

"(11) **MEMBERS OF ECONOMICALLY DISADVANTAGED FAMILIES.**—An individual is a member of an economically disadvantaged family if the designated local agency determines that such individual was a member of a family which had an income during the 6 months immediately preceding the month in which such determination occurs, which, on an annual basis, would be 70 percent or less of the Bureau of Labor Statistics lower living standard. Any such determination shall be valid for the 45-day period beginning on the date such determination is made."

(d) **ELIGIBILITY.**—Section 51 is amended by adding at the end thereof the following new subsection:

"(i) **CERTAIN INDIVIDUALS INELIGIBLE.**—

"(1) **RELATED INDIVIDUALS.**—No wages shall be taken into account under subsection (a) with respect to an individual who—

"(A) bears any of the relationships described in paragraphs (1) through (8) of section 152(a) to the taxpayer, or, if the taxpayer is a corporation, to an individual who owns, directly or indirectly, more than 50 percent in value of the outstanding stock of the corporation (determined with the application of section 267(c)),

"(B) if the taxpayer is an estate or trust, is a grantor, beneficiary, or fiduciary of the estate or trust, or is an individual who bears any of the relationships described in paragraphs (1) through (8) of section 152(a) to a grantor, beneficiary, or fiduciary of the estate or trust, or

"(C) is a dependent (described in section 152(a)(9)) of the taxpayer, or, if the taxpayer is a corporation, of an individual described in subparagraph (A), or, if the taxpayer is an estate or trust, of a grantor, beneficiary, or fiduciary of the estate or trust.

"(2) **NONQUALIFYING REHIRES.**—No wages shall be taken into account under subsection (a) with respect to any individual if, prior to the hiring date of such individual, such individual had been employed by the employer at any time during which he was not a member of a targeted group."

(e) **REPEAL OF PROVISION LIMITING FIRST-YEAR WAGES TO 30 PERCENT OF FUTA WAGES.**—

(1) Subsection (e) of section 51 is hereby repealed.

(2) Subsection (f) of section 51 is amended—

(A) by striking out paragraph (3), and

(B) by striking out "any year" in paragraphs (1) and (2) and inserting in lieu thereof "any taxable year".

(f) **ADMINISTRATION, AUTHORIZATION OF APPROPRIATIONS.**—

(1) **ADMINISTRATION.**—

(a) **DESIGNATED LOCAL AGENCY.**—Paragraph (14) of section 51(d) (as redesignated by subsection (b)(2)(A)) is amended to read as follows:

"(14) **DESIGNATED LOCAL AGENCY.**—The term 'designated local agency' means a State employment security agency established



in accordance with the Act of June 6, 1933, as amended (29 U.S.C. 49-49n).”

(B) **NOTIFICATION.**—Subsection (g) of section 51 (relating to notification of employers) is amended by striking out “Secretary of Labor” each place it appears in the heading and text and inserting in lieu thereof “United States Employment Service”.

(2) **AUTHORIZATION OF APPROPRIATIONS.**—There is authorized to be appropriated for fiscal year 1982 the sum of \$30,000,000 to carry out the functions described by the amendments made by paragraph (1), except that, of the amounts appropriated pursuant to this paragraph—

(A) \$5,000,000 shall be used to test whether individuals certified as members of targeted groups under section 51 of such Code are eligible for such certification (including the use of statistical sampling techniques), and

(B) the remainder shall be distributed under performance standards prescribed by the Secretary of Labor.

(g) **EFFECTIVE DATES.**—

(1) **AMENDMENTS RELATING TO MEMBERS OF TARGETED GROUPS.**—

(A) **IN GENERAL.**—Except as provided in subparagraphs (B), (C), and (D), the amendments made by subsections (b), (c)(2), and (d) shall apply to wages paid or incurred with respect to individuals first beginning work for an employer after the date of the enactment of this Act in taxable years ending after such date.

(B) **ELIGIBLE WORK INCENTIVE EMPLOYEES.**—The amendments made by subsection (b)(2)(A) to the extent relating to the designation of eligible work incentive employees (within the meaning of section 51(d)(9) of the Internal Revenue Code of 1954) as members of a targeted group and subsection (b)(2)(B)(ii) shall apply to taxable years beginning after December 31, 1981. In the case of an eligible work incentive employee, subsections (a) and (b) of section 51 of such Code shall be applied for taxable years beginning after December 31, 1981, as if such employees had been members of a targeted group for taxable years beginning before January 1, 1982.

(C) **COOPERATIVE EDUCATION PROGRAM PARTICIPANTS.**—The amendments made by subsection (b)(4) shall apply to wages paid or incurred after December 31, 1981, in taxable years ending after such date.

(D) **DESIGNATED LOCAL AGENCY.**—The amendments made by subsection (f)(1) shall take effect on the date 60 days after the date of the enactment of this Act.

(2) **CERTIFICATIONS.**—

(A) **IN GENERAL.**—The amendment made by subsection (c)(1) shall apply to all individuals whether such individuals began work for their employer before, on, or after the date of the enactment of this Act.

(B) **SPECIAL RULE FOR INDIVIDUALS WHO BEGAN WORK FOR THE EMPLOYER BEFORE 45TH DAY BEFORE DATE OF ENACTMENT.**—In the case of any individual (other than an individual described in section 51(d)(8) of the Internal Revenue

Code of 1954) who began work for the employer before the date 45 days before the date of the enactment of this Act, paragraph (15) of section 51(d) of the Internal Revenue Code of 1954 (as added by subsection (c)(1)) shall be applied by substituting "July 23, 1981," for the day on which such individual begins work for the employer.

(C) **INDIVIDUALS WHO BEGIN WORK FOR EMPLOYER WITHIN 45 DAYS BEFORE OR AFTER DATE OF ENACTMENT.**—In the case of any individual (other than an individual described in section 51(d)(8) of the Internal Revenue Code of 1954) who begins work for the employer during the 90-day period beginning with the date 45 days before the date of the enactment of this Act, and in the case of an individual described in section 51(d)(8) of such Code who begins work before the end of such 90-day period, paragraph (15) of section 51(d) of such Code (as added by subsection (c)(1)) shall be applied by substituting "the last day of the 90-day period beginning with the date 45 days before the date of the enactment of this Act" for the day on which such individual begins work for the employer.

(3) **LIMITATION ON QUALIFIED FIRST-YEAR WAGES.**—The amendment made by subsection (e) shall apply to taxable years beginning after December 31, 1981.

**SEC. 262. SECTION 189 MADE INAPPLICABLE TO LOW-INCOME HOUSING.**

(a) **IN GENERAL.**—The table contained in subsection (b) of section 189 (relating to amortization of real property construction period, interest, and taxes) is amended by striking out the column relating to "Low-income housing".

(b) **CONFORMING AMENDMENT.**—Subsection (d) of section 189 (relating to certain residential property excluded) is amended to read as follows:

"(d) **CERTAIN PROPERTY EXCLUDED.**—This section shall not apply to any—

"(1) low-income housing, or

"(2) real property acquired, constructed, or carried if such property is not, and cannot reasonably be expected to be, held in a trade or business, or in an activity conducted for profit."

(c) **EFFECTIVE DATE.**—The amendments made by this section shall apply to taxable years beginning after December 31, 1981.

**SEC. 263. INCREASE IN DEDUCTION ALLOWABLE TO A CORPORATION IN ANY TAXABLE YEAR FOR CHARITABLE CONTRIBUTIONS.**

(a) **IN GENERAL.**—Paragraph (2) of section 170(b) (relating to percentage limitations) is amended by striking out "5 percent" and inserting in lieu thereof "10 percent".

(b) **EFFECTIVE DATE.**—The amendment made by this section shall apply to taxable years beginning after December 31, 1981.

**SEC. 264. AMORTIZATION OF LOW-INCOME HOUSING.**

(a) **IN GENERAL.**—Paragraph (2) of section 167(k) (relating to rehabilitation of low-income rental housing) is amended by striking out "The" in subparagraph (A) and inserting in lieu thereof "Except as provided in subparagraph (B), the", by redesignating subparagraph (B) as subparagraph (C), and by inserting after subparagraph (A) the following:

"(B) The aggregate amount of rehabilitation expenditures paid or incurred by the taxpayer with respect to any dwell-

ing unit in any low-income rental housing which may be taken into account under paragraph (1) may exceed \$20,000, but shall not exceed \$40,000, if the rehabilitation is conducted pursuant to a program certified by the Secretary of Housing and Urban Development, or his delegate, or by the government of a State or political subdivision of the United States and if:

“(i) the certification of development costs is required;

“(ii) the tenants occupy units in the property as their principal residence and the program provides for sale of the units to tenants demonstrating home ownership responsibility; and

“(iii) the leasing and sale of such units are pursuant to a program in which the sum of the taxable income, if any, from leasing of each such unit, for the entire period of such leasing, and the amount realized from sale or other disposition of a unit, if sold, normally does not exceed the excess of the taxpayer's cost basis for such unit of property, before adjustment under section 1016 for deductions under section 167, over the net tax benefits realized by the taxpayer, consisting of the tax benefits from such deductions under section 167 minus the tax incurred on such taxable income from leasing, if any.”

(b) **EFFECTIVE DATE.**—The amendments made by this section shall apply with respect to rehabilitation expenditures incurred after December 31, 1980.

**SEC. 265. DEDUCTIBILITY OF GIFTS BY EMPLOYERS TO EMPLOYEES.**

(a) **IN GENERAL.**—Subparagraph (C) of section 274(b)(1) (relating to limitation on deductibility of gifts) is amended to read as follows:

“(C) an item of tangible personal property which is awarded to an employee by reason of length of service, productivity, or safety achievement, but only to the extent that—

“(i) the cost of such item to the taxpayer does not exceed \$400, or

“(ii) such item is a qualified plan award.”

(b) **QUALIFIED PLAN AWARD DEFINED.**—Subsection (b) of section 274 is amended by adding at the end thereof the following new paragraph:

“(3) **QUALIFIED PLAN AWARD.**—For purposes of this subsection—

“(A) **IN GENERAL.**—The term ‘qualified plan award’ means an item which is awarded as part of a permanent, written plan or program of the taxpayer which does not discriminate in favor of officers, shareholders, or highly compensated employees as to eligibility or benefits.

“(B) **AVERAGE AMOUNT OF AWARDS.**—An item shall not be treated as a qualified plan award for any taxable year if the average cost of all items awarded under all plans described in subparagraph (A) of the taxpayer during the taxable year exceeds \$400.

“(C) **MAXIMUM AMOUNT PER ITEM.**—An item shall not be treated as a qualified plan award under this paragraph to the extent that the cost of such item exceeds \$1,600.”

(c) **EFFECTIVE DATE.**—The amendments made by this section shall apply to taxable years ending on or after the date of the enactment of this Act.

**SEC. 266. DEDUCTION FOR MOTOR CARRIER OPERATING AUTHORITY.**

(a) **GENERAL RULE.**—For purposes of chapter 1 of the Internal Revenue Code of 1954, in computing the taxable income of a taxpayer who, on July 1, 1980, held one or more motor carrier operating authorities, an amount equal to the aggregate adjusted basis of all motor carrier operating authorities held by the taxpayer on July 1, 1980, or acquired subsequent thereto pursuant to a binding contract in effect on July 1, 1980, shall be allowed as a deduction ratably over a period of 60 months. Such 60-month period shall begin with the month of July 1980 (or if later, the month in which acquired), or at the election of the taxpayer, the first month of the taxpayer's first taxable year beginning after July 1, 1980.

(b) **DEFINITION OF MOTOR CARRIER OPERATING AUTHORITY.**—For purposes of this section, the term "motor carrier operating authority" means a certificate or permit held by a motor common or contract carrier of property and issued pursuant to subchapter II of chapter 109 of title 49 of the United States Code.

(c) **SPECIAL RULES.**—

(1) **ADJUSTED BASIS.**—For purposes of the Internal Revenue Code of 1954, proper adjustments shall be made in the adjusted basis of any motor carrier operating authority held by the taxpayer on July 1, 1980, for the amounts allowable as a deduction under this section.

(2) **CERTAIN STOCK ACQUISITIONS.**—

(A) **IN GENERAL.**—Under regulations prescribed by the Secretary of the Treasury or his delegate, and at the election of the holder of the authority, in any case in which a corporation—

(i) on or before July 1, 1980 (or after such date pursuant to a binding contract in effect on such date), acquired stock in a corporation which held, directly or indirectly, any motor carrier operating authority at the time of such acquisition, and

(ii) would have been able to allocate to the basis of such authority that portion of the acquiring corporation's cost basis in such stock attributable to such authority if the acquiring corporation had received such authority in the liquidation of the acquired corporation immediately following such acquisition and such allocation would have been proper under section 334(b)(2) of such Code.

the holder of the authority may, for purposes of this section, allocate a portion of the basis of the acquiring corporation in the stock of the acquired corporation to the basis of such authority in such manner as the Secretary may prescribe in such regulations.

(b) **ADJUSTMENT TO BASIS.**—Under regulations prescribed by the Secretary of the Treasury or his delegate, proper adjustment shall be made to the basis of the stock or other assets in the manner provided by such regulations to take into account any allocation under subparagraph (A).

(d) **EFFECTIVE DATE.**—The provisions of this section shall apply to taxable years ending after June 30, 1980.

**SEC. 267. LIMITATION ON ADDITIONS TO BANK LOSS RESERVES.**

(a) **GENERAL RULE.**—

(1) The first sentence after subparagraph (B) of paragraph (2) of section 585(b) is amended by striking out “but before 1982; and 0.6 percent for taxable years beginning after 1981” and inserting in lieu thereof “but before 1982; 1.0 percent for taxable years beginning in 1982; and 0.6 percent for taxable years beginning after 1982.”

(2) The last sentence of paragraph (2) of section 585(b) is amended by striking out “but before 1982, the last taxable year beginning before 1976, and for taxable years beginning after 1981, the last taxable year beginning before 1982” and inserting in lieu thereof “but before 1983, the last taxable year beginning before 1976, and for taxable years beginning after 1982, the last taxable year beginning before 1983”.

(b) **EFFECTIVE DATE.**—The amendment made by subsection (a) shall apply to taxable years beginning after 1981.

## **TITLE III—SAVINGS PROVISIONS**

### **Subtitle A—Interest Exclusion**

**SEC. 301. EXCLUSION OF INTEREST ON CERTAIN SAVINGS CERTIFICATES.**

(a) **GENERAL RULE.**—Part III of subchapter B of chapter 1 (relating to items specifically excluded from gross income) is amended by redesignating section 128 as section 129 and by inserting after section 127 the following new section:

**“SEC. 128. INTEREST ON CERTAIN SAVINGS CERTIFICATES.**

**“(a) IN GENERAL.**—Gross income does not include any amount received by any individual during the taxable year as interest on a depository institution tax-exempt savings certificate.

**“(b) MAXIMUM DOLLAR AMOUNT.**—

**“(1) IN GENERAL.**—The aggregate amount excludable under subsection (a) for any taxable year shall not exceed the excess of—

**“(A) \$1,000 (\$2,000 in the case of a joint return under section 6013), over**

**“(B) the aggregate amount received by the taxpayer which was excludable under subsection (a) for any prior taxable year.**

**“(2) SPECIAL RULE.**—For purposes of paragraph (1)(B), one-half of the amount excluded under subsection (a) on any joint return shall be treated as received by each spouse.

**“(c) DEPOSITORY INSTITUTION TAX-EXEMPT SAVINGS CERTIFICATE.**—For purposes of this section—

**“(1) IN GENERAL.**—The term ‘depository institution tax-exempt savings certificate’ means any certificate—

**“(A) which is issued by a qualified savings institution after September 30, 1981, and before January 1, 1983,**

**“(B) which has a maturity of 1 year,**

**“(C) which has an investment yield equal to 70 percent of the average investment yield for the most recent auction**

(before the week in which the certificate is issued) of United States Treasury bills with maturities of 52 weeks, and

“(D) which is made available in denominations of \$500.

“(2) QUALIFIED INSTITUTION.—The term ‘qualified institution’ means—

“(A)(i) a bank (as defined in section 581),

“(ii) a mutual savings bank, cooperative bank, domestic building and loan association, or other savings institution chartered and supervised as a savings and loan or similar institution under Federal or State law, or

“(iii) a credit union,

the deposits or accounts of which are insured under Federal or State law or are protected or guaranteed under State law, or

“(B) an industrial loan association or bank chartered and supervised under Federal or State law in a manner similar to a savings and loan institution.

The term “qualified institution” does not include any foreign branch or international banking facility of an institution described in the preceding sentence and such a branch or facility shall not be taken into account under subsection (d).

“(d) INSTITUTIONS REQUIRED TO PROVIDE RESIDENTIAL PROPERTY FINANCING.—

“(1) IN GENERAL.—If a qualified savings institution (other than an institution described in subsection (c)(2)(A)(iii)) issues any depository institution tax-exempt savings certificate during any calendar quarter, the amount of the qualified residential financing provided by such institution shall during the succeeding calendar quarter not be less than the lesser of—

“(A) 75 percent of the face amount of depository institution tax-exempt savings certificates issued during the calendar quarter, or

“(B) 75 percent of the qualified net savings for the calendar quarter.

The aggregate amount of qualified tax-exempt savings certificates issued by any institution described in subsection (c)(2)(A)(iii) which are outstanding at the close of any calendar quarter may not exceed the limitation determined under paragraph (4) with respect to such institution for such quarter.

“(2) PENALTY FOR FAILURE TO MEET REQUIREMENTS.—If, as of the close of any calendar quarter, a qualified institution has not met the requirements of paragraph (1) with respect to the preceding calendar quarter, such institution may not issue any certificates until it meets such requirements.

“(3) QUALIFIED RESIDENTIAL FINANCING.—The term ‘qualified residential financing’ includes, and is limited to—

“(A) any loan secured by a lien on a single-family or multifamily residence,

“(B) any secured or unsecured qualified home improvement loan (within the meaning of section 103A(l)(6) without regard to the \$15,000 limit),

“(C) any mortgage (within the meaning of section 103A(l)(1)) on a single family or multifamily residence

which is insured or guaranteed by the Federal, State, or local government or any instrumentality thereof,

“(D) any loan to acquire a mobile home,

“(E) any construction loan for the construction or rehabilitation of a single-family or multifamily residence,

“(F) the purchase of mortgages secured by single-family or multifamily residences on the secondary market but only to the extent the amount of such purchases exceed the amount of sales of such mortgages by an institution,

“(G) the purchase of securities issued or guaranteed by the Federal National Mortgage Association, the Government National Mortgage Association, or the Federal Home Loan Mortgage Corporation, or securities issued by any other person if such securities are secured by mortgages originated by a qualified institution, but only to the extent the amount of such purchases exceed the amount of sales of such securities by an institution, and

“(H) any loan for agricultural purposes.

For purposes of this paragraph, the term ‘single-family residence’ includes 2-, 3-, and 4-family residences, and the term ‘residence’ includes stock in a cooperative housing corporation (as defined in section 216(b)).

“(4) **LIMITATION FOR CREDIT UNIONS.**—For purposes of paragraph (1), the limitation determined under this paragraph with respect to any institution described in subsection (c)(2)(A)(iii) for any calendar quarter is the sum of—

“(A) the aggregate of the amounts described in subparagraph (A) of paragraph (5) with respect to such institution as of September 30, 1981, plus

“(B) 10 percent of the excess of—

“(i) the aggregate of such amounts as of the close of such calendar quarter, over

“(ii) the amount referred to in subparagraph (A).

“(5) **QUALIFIED NET SAVINGS.**—The term ‘qualified net savings’ means, with respect to any qualified institution, the excess of—

“(A) the amounts paid into passbook savings account, 6-month money market certificates, 30-month small-saver certificates, time deposits with a face amount of less than \$100,000, and depository institution tax-exempt savings certificates issued by such institution, over

“(B) the amounts withdrawn or redeemed in connection with the accounts and certificates described in subparagraph (A).

“(6) **CONSOLIDATED GROUPS.**—For purposes of this subsection, all members of the same affiliated group (as defined in section 1504) which file a consolidated return for the taxable year shall be treated as 1 corporation.

“(e) **PENALTY FOR EARLY WITHDRAWALS.**—

“(1) **IN GENERAL.**—If any portion of a depository institution tax-exempt savings certificate is redeemed before the date on which it matures—

“(A) subsection (a) shall not apply to any interest on such certificate for the taxable year of redemption and any subsequent taxable year, and

“(B) there shall be included in gross income for the taxable year of redemption the amount of any interest on such certificate excluded under subsection (a) for any preceding taxable year.

“(2) CERTIFICATE PLEDGED AS COLLATERAL.—For purposes of paragraph (1), if the taxpayer uses any depository institution tax-exempt savings certificate (or portion thereof) as collateral or security for a loan, the taxpayer shall be treated as having redeemed such certificate.

“(f) OTHER SPECIAL RULES.—

“(1) COORDINATION WITH SECTION 116.—Section 116 shall not apply to the interest on any depository institution tax-exempt savings certificate.

“(2) ESTATES AND TRUSTS.—

“(A) IN GENERAL.—Except as provided in subparagraph (B), the exclusion provided by this section shall not apply to estates and trusts.

“(B) CERTIFICATES ACQUIRED BY ESTATE FROM DECEDENT.—In the case of a depository institution tax-exempt savings certificate acquired by an estate by reason of the death of the decedent—

“(i) subparagraph (A) shall not apply, and

“(ii) subsection (b) shall be applied as if the estate were the decedent.”

(b) CONFORMING AMENDMENTS.—

(1) The table of sections for part III of subchapter B of chapter 1 is amended by striking out the item relating to section 128 and inserting in lieu thereof the following new items

“Sec. 128. Interest on certain savings certificates.

“Sec. 129. Cross references to other Acts.”

(2) Section 265 (relating to expenses and interest relating to tax-exempt income) is amended by inserting “, or to purchase or carry any certificate to the extent the interest on such certificate is excludable under section 128” after “116”.

(3) Paragraph (2) of section 584(c) (relating to income of participants in common trust funds), as in effect for taxable years beginning in 1981, is amended by inserting “or 128” after “116”.

(4) Paragraph (7) of section 643(a) (defining distributable net income), as in effect for taxable years beginning in 1981, is amended by inserting “or section 128 (relating to interest on certain savings certificates)” after “received”.

(5) Section 702(a)(5) (relating to income and credits of partners), as in effect for taxable years beginning in 1981, is amended by inserting “or 128” after “116”.

(6) Each of the following provisions, as in effect for taxable years beginning after December 31, 1981, are amended by inserting “or interest” after “dividends” each place it appears in the caption or text:

(A) section 584(c)(2),

(B) section 643(a)(7),

(C) section 702(a)(5).

(c) STUDY.—The Secretary of the Treasury or his delegate shall conduct a study of the exemption from income of interest earned on



depository institution tax-exempt savings certificates established by this section to determine the exemption's effectiveness in generating additional savings. Such report shall be submitted to the Congress before June 1, 1983.

**(d) EFFECTIVE DATES.—**

**(1) IN GENERAL.—**Except as provided in paragraph (2), the amendments made by this section shall apply to taxable years ending after September 30, 1981.

**(2) CONFORMING AMENDMENTS.—**The amendments made by subsection (b)(6) shall apply to taxable years beginning after December 31, 1981.

**SEC. 302. PARTIAL EXCLUSION OF INTEREST**

**(a) AMOUNT OF EXCLUSION.—**Section 128 (relating to the interest on certain savings certificates) is amended to read as follows:

**“SEC. 128. PARTIAL EXCLUSION OF INTEREST.**

**“(a) IN GENERAL.—**Gross income does not include the amounts received during the taxable year by an individual as interest.

**“(b) MAXIMUM DOLLAR AMOUNT.—**The aggregate amount excludable under subsection (a) for any taxable year shall not exceed 15 percent of the lesser of—

**“(1) \$3,000 (\$6,000 in the case of a joint return under section 6013), or**

**“(2) the excess of the amount of interest received by the taxpayer during such taxable year (less the amount of any deduction under section 62(12)) over the amount of qualified interest expenses of such taxpayer for the taxable year.**

**“(c) DEFINITIONS.—**For purposes of this section—

**“(1) INTEREST DEFINED.—**The term ‘interest’ means—

**“(A) interest on deposits with a bank (as defined in section 581),**

**“(B) amounts (whether or not designated as interest) paid, in respect of deposits, investment certificates, or withdrawable or repurchasable shares, by—**

**“(i) an institution which is—**

**“(I) a mutual savings bank, cooperative bank, domestic building and loan association, or credit union, or**

**“(II) any other savings or thrift institution which is chartered and supervised under Federal or State law,**

**the deposits or accounts in which are insured under Federal or State law or which are protected and guaranteed under State law, or**

**“(ii) an industrial loan association or bank chartered and supervised under Federal or State law in a manner similar to a savings and loan institution.**

**“(C) interest on—**

**“(i) evidences of indebtedness (including bonds, debentures, notes, and certificates) issued by a domestic corporation in registered form, and**

**“(ii) to the extent provided in regulations prescribed by the Secretary, other evidences of indebtedness issued by a domestic corporation of a type offered by corporations to the public,**

“(D) interest on obligations of the United States, a State, or a political subdivision of a State (not excluded from gross income of the taxpayer under any other provision of law),

“(E) interest attributable to participation shares in a trust established and maintained by a corporation established pursuant to Federal law, and

“(F) interest paid by an insurance company under an agreement to pay interest on—

“(i) prepaid premiums,

“(ii) life insurance policy proceeds which are left on deposit with such company by a beneficiary, and

“(iii) under regulations prescribed by the Secretary, policyholder dividends left on deposit with such company.

“(2) **QUALIFIED INTEREST EXPENSE DEFINED.**—The term ‘qualified interest expense’ means an amount equal to the excess of—

“(A) the amount of the deduction allowed the taxpayer under section 163(a) (relating to interest) for the taxable year, over

“(B) the amount of such deduction allowed with respect to interest paid or accrued on indebtedness incurred in—

“(i) acquiring, constructing, reconstructing, or rehabilitating property which is primarily used by the taxpayer as a dwelling unit (as defined in section 280A(f)(1)), or

“(ii) the taxpayer’s conduct of a trade or business.”

(b) **REPEAL OF PARTIAL EXCLUSION OF INTEREST.**—

(1) **IN GENERAL.**—Subsection (c) of section 404 of the Crude Oil Windfall Profit Tax Act of 1980 is amended by striking out “1983” and inserting in lieu thereof “1982”.

(2) **CONFORMING AMENDMENT.**—Section 116(a) (relating to partial exclusion of dividends) is amended to read as follows:

“(a) **EXCLUSION FROM GROSS INCOME.**—

“(1) **IN GENERAL.**—Gross income does not include amounts received by an individual as dividends from domestic corporations.

“(2) **MAXIMUM DOLLAR AMOUNT.**—The aggregate amount excluded under subsection (a) for any taxable year shall not exceed \$100 (\$200 in the case of a joint return under section 6013).

(c) **CONFORMING AMENDMENTS.**—

(1) The table of sections for part III of subchapter B of chapter 1, as amended by section 301(b)(1), is amended by striking out the item relating to section 128 and inserting in lieu thereof the following new item:

“Sec. 128. Partial exclusion of interest.”

(2) Section 265 (relating to expenses and interest relating to tax-exempt income), as amended by section 301(b)(2), is amended by striking out “or to purchase or carry any certificate to the extent the interest on such certificate is excludable under section 128” and inserting in lieu thereof “or to purchase or carry obligations or shares, or to make other deposits or investments, the interest on which is described in section 128(c)(1) to the

extent such interest is excludable from gross income under section 128”.

(3) Section 46(c)(8) (relating to limitation to amount at risk) is amended by striking out “clause (i), (ii), or (iii) of subparagraph (A) or subparagraph (B) of section 128(c)(2)” and inserting in lieu thereof “subparagraph (A) or (B) of section 128(c)(1)”.

(4) Subsection (b) of section 854 is amended to read as follows:

“(b) **OTHER DIVIDENDS AND TAXABLE INTEREST.**—

“(1) **DEDUCTION UNDER SECTION 243.**—In the case of a dividend received from a regulated investment company (other than a dividend to which subsection (a) applies)—

“(A) if such investment company meets the requirements of section 852(a) for the taxable year during which it paid such dividend; and

“(B) the aggregate dividends received by such company during such taxable year are less than 75 percent of its gross income.

then, in computing the deduction under section 243, there shall be taken into account only that portion of the dividend which bears the same ratio to the amount of such dividend as the aggregate dividends received by such company during such taxable year bear to its gross income for such taxable year.

“(2) **EXCLUSION UNDER SECTIONS 116 AND 128.**—For purposes of sections 116 and 128, in the case of any dividend (other than a dividend described in subsection (a)) received from a regulated investment company which meets the requirements of section 852 for the taxable year in which it paid the dividend—

“(A) the entire amount of such dividend shall be treated as a dividend if the aggregate dividends received by such company during the taxable year equal or exceed 75 percent of its gross income,

“(B) the entire amount of such dividend shall be treated as interest if the aggregate interest received by such company during the taxable year equals or exceeds 75 percent of its gross income, or

“(C) if subparagraphs (A) and (B) do not apply, a portion of such dividend shall be treated as a dividend (and a portion of such dividend shall be treated as interest) based on the portion of the company’s gross income which consists of aggregate dividends or aggregate interest, as the case may be. For purposes of the preceding sentence, gross income and aggregate interest received shall each be reduced by so much of the deduction allowable by section 163 for the taxable year as does not exceed aggregate interest received for the taxable year.

“(3) **NOTICE TO SHAREHOLDERS.**—The amount of any distribution by a regulated investment company which may be taken into account as a dividend for purposes of the exclusion under section 116 and the deduction under section 243 or as interest for purposes of section 128 shall not exceed the amount so designated by the company in a written notice to its shareholders mailed not later than 45 days after the close of its taxable year.

“(4) **DEFINITIONS.**—For purposes of this subsection—

*“(A) The term ‘gross income’ does not include gain from the sale or other disposition of stock or securities.*

*“(B) The term ‘aggregate dividends received’ includes only dividends received from domestic corporations other than dividends described in section 116(b)(2) (relating to dividends excluded from gross income). In determining the amount of any dividend for purposes of this subparagraph, the rules provided in section 116(c)(2) (relating to certain distributions) shall apply.*

*“(C) The term ‘aggregate interest received’ includes only interest described in section 128(c)(1).”*

*(5) Subsection (c) of section 857 is amended to read as follows:*

***“(c) LIMITATIONS APPLICABLE TO DIVIDENDS RECEIVED FROM REAL ESTATE INVESTMENT TRUSTS.—***

*“(1) IN GENERAL.—For purposes of section 116 (relating to an exclusion for dividends received by individuals) and section 243 (relating to deductions for dividends received by corporations), a dividend received from a real estate investment trust which meets the requirements of this part shall not be considered as a dividend.*

*“(2) TREATMENT FOR SECTION 128.—In the case of a dividend (other than a capital gain dividend, as defined in subsection (b)(3)(C)) received from a real estate investment trust which meets the requirements of this part for the taxable year in which it paid the dividend—*

*“(A) such dividend shall be treated as interest if the aggregate interest received by the real estate investment trust for the taxable year equals or exceeds 75 percent of its gross income, or*

*“(B) if subparagraph (A) does not apply, the portion of such dividend which bears the same ratio to the amount of such dividend as the aggregate interest received bears to gross income shall be treated as interest.*

***“(3) ADJUSTMENTS TO GROSS INCOME AND AGGREGATE INTEREST RECEIVED.—For purposes of paragraph (2)—***

*“(A) gross income does not include the net capital gain,*

*“(B) gross income and aggregate interest received shall each be reduced by so much of the deduction allowable by section 163 for the taxable year (other than for interest on mortgages on real property owned by the real estate investment trust) as does not exceed aggregate interest received by the taxable year, and*

*“(C) gross income shall be reduced by the sum of the taxes imposed by paragraphs (4), (5), and (6) of section 857(b).*

***“(4) AGGREGATE INTEREST RECEIVED.—For purposes of this subsection, the term ‘aggregate interest received’ means only interest described in section 128(c)(1).***

***“(5) NOTICE TO SHAREHOLDERS.—The amount of any distribution by a real estate investment trust which may be taken into account as interest for purposes of the exclusion under section 128 shall not exceed the amount so designated by the trust in a written notice to its shareholders mailed not later than 45 days after the close of its taxable year.”***

***(d) EFFECTIVE DATES.—***

(1) *IN GENERAL.*—The amendments made by subsections (a) and (c) shall apply to taxable years beginning after December 31, 1984.

(2) *DIVIDEND EXCLUSION.*—The amendment made by subsection (b)(2) shall apply to taxable years beginning after December 31, 1981.

## **Subtitle B—Retirement Savings Provisions**

### **SEC. 311. RETIREMENT SAVINGS.**

(a) *GENERAL RULE.*—Section 219 (relating to deduction for retirement savings) is amended to read as follows:

#### **“SEC. 219. RETIREMENT SAVINGS.**

“(a) *ALLOWANCE OF DEDUCTION.*—In the case of an individual, there shall be allowed as a deduction an amount equal to the qualified retirement contributions of the individual for the taxable year.

“(b) *MAXIMUM AMOUNT OF DEDUCTION.*—

“(1) *IN GENERAL.*—The amount allowable as a deduction under subsection (a) to any individual for any taxable year shall not exceed the lesser of—

“(A) \$2,000, or

“(B) an amount equal to the compensation includible in the individual’s gross income for such taxable year.

“(2) *SPECIAL RULES FOR EMPLOYER CONTRIBUTIONS UNDER SIMPLIFIED EMPLOYEE PENSIONS.*—

“(A) *LIMITATION.*—If there is an employer contribution on behalf of the employee to a simplified employee pension, an employee shall be allowed as a deduction under subsection (a) (in addition to the amount allowable under paragraph (1)) an amount equal to the lesser of—

“(i) 15 percent of the compensation from such employer includible in the employee’s gross income for the taxable year (determined without regard to the employer contribution to the simplified employee pension), or

“(ii) the amount contributed by such employer to the simplified employee pension and included in gross income (but not in excess of \$7,500).

“(B) *CERTAIN LIMITATIONS DO NOT APPLY TO EMPLOYER CONTRIBUTION.*—Paragraph (1) of this subsection and paragraph (1) of subsection (d) shall not apply with respect to the employer contribution to a simplified employee pension.

“(C) *SPECIAL RULE FOR APPLYING SUBPARAGRAPH (A)(ii).*—In the case of an employee who is an officer, shareholder, or owner-employee described in section 408(k)(3), the \$7,500 amount specified in subparagraph (A)(ii) shall be reduced by the amount of tax taken into account with respect to such individual under subparagraph (D) of section 408(k)(3).

“(3) *SPECIAL RULE FOR INDIVIDUAL RETIREMENT PLANS.*—If the individual has paid any qualified voluntary employee contributions for the taxable year, the amount of the qualified retirement contributions (other than employer contributions to a simplified employee pension) which are paid for the taxable year to an individual retirement plan and which are allowable

as a deduction under subsection (a) for such taxable year shall not exceed—

“(A) the amount determined under paragraph (1) for such taxable year, reduced by

“(B) the amount of the qualified voluntary employee contributions for the taxable year.

“(4) CERTAIN DIVORCED INDIVIDUALS.—

“(A) IN GENERAL.—In the case of an individual to whom this paragraph applies, the limitation of paragraph (1) shall not be less than the lesser of—

“(i) \$1,125, or

“(ii) the sum of the amount referred to in paragraph (1)(B) and any qualifying alimony received by the individual during the taxable year.

“(B) QUALIFYING ALIMONY.—For purposes of this paragraph, the term ‘qualifying alimony’ means amounts includible in the individual’s gross income under paragraph (1) of section 71(a) (relating to decree of divorce or separate maintenance).

“(C) INDIVIDUALS TO WHOM SECTION APPLIES.—This section shall apply to an individual if—

“(i) an individual retirement plan was established for the benefit of the individual at least 5 years before the beginning of the calendar year in which the decree of divorce or separate maintenance was issued, and

“(ii) for at least 3 of the former spouse’s most recent 5 taxable years ending before the taxable year in which the decree was issued, such former spouse was allowed a deduction under subsection (c) (or the corresponding provisions of prior law) for contributions to such individual retirement plan.

“(c) SPECIAL RULES FOR CERTAIN MARRIED INDIVIDUALS.—

“(1) IN GENERAL.—In the case of any individual with respect to whom a deduction is otherwise allowable under subsection (a)—

“(A) who files a joint return under section 6013 for a taxable year, and

“(B) whose spouse has no compensation (determined without regard to section 911) for such taxable year, there shall be allowed as a deduction any amount paid in cash for the taxable year by or on behalf of the individual to an individual retirement plan established for the benefit of his spouse.

“(2) LIMITATION.—The amount allowable as a deduction under paragraph (1) shall not exceed the excess of—

“(A) the lesser of—

“(i) \$2,250, or

“(ii) an amount equal to the compensation includible in the individual’s gross income for the taxable year, over

“(B) the amount allowed as a deduction under subsection (a) for the taxable year.

In no event shall the amount allowable as a deduction under paragraph (1) exceed \$2,000.

“(d) OTHER LIMITATIONS AND RESTRICTIONS.—

**“(1) INDIVIDUALS WHO HAVE ATTAINED AGE 70½.—**No deduction shall be allowed under this section with respect to any qualified retirement contribution which is made for a taxable year of an individual if such individual has attained age 70½ before the close of such taxable year.

**“(2) RECONTRIBUTED AMOUNTS.—**No deduction shall be allowed under this section with respect to a rollover contribution described in section 402(a)(5), 402(a)(7), 403(a)(4), 403(b)(8), 408(d)(3), or 409(b)(3)(C).

**“(3) AMOUNTS CONTRIBUTED UNDER ENDOWMENT CONTRACT.—**In the case of an endowment contract described in section 408(b), no deduction shall be allowed under this section for that portion of the amounts paid under the contract for the taxable year which is properly allocable, under regulations prescribed by the Secretary, to the cost of life insurance.

**“(e) DEFINITION OF RETIREMENT SAVINGS CONTRIBUTIONS, ETC.—**For purposes of this section—

**“(1) QUALIFIED RETIREMENT CONTRIBUTION.—**The term ‘qualified retirement contribution’ means—

**“(A) any qualified voluntary employee contribution paid in cash by the individual for the taxable year, and**

**“(B) any amount paid in cash for the taxable year by or on behalf of such individual for his benefit to an individual retirement plan.**

For purposes of the preceding sentence, the term ‘individual retirement plan’ includes a retirement bond described in section 409 only if the bond is not redeemed within 12 months of its issuance.

**“(2) QUALIFIED VOLUNTARY EMPLOYEE CONTRIBUTION.—**

**“(A) IN GENERAL.—**The term ‘qualified voluntary employee contribution’ means any voluntary contribution—

**“(i) which is made by an individual as an employee under a qualified employer plan or government plan, which plan allows an employee to make contributions which may be treated as qualified voluntary employee contributions under this section, and**

**“(ii) with respect to which the individual has not designated such contribution as a contribution which should not be taken into account under this section.**

**“(B) VOLUNTARY CONTRIBUTION.—**For purposes of subparagraph (A), the term ‘voluntary contribution’ means any contribution which is not a mandatory contribution (within the meaning of section 411(c)(2)(C)).

**“(C) DESIGNATION.—**For purposes of determining whether or not an individual has made a designation described in subparagraph (A)(ii) with respect to any contribution during any calendar year under a qualified employer plan or government plan, such individual shall be treated as having made such designation if he notifies the plan administrator of such plan, not later than the earlier of—

**“(i) April 15 of the succeeding calendar year, or**

**“(ii) the time prescribed by the plan administrator, that the individual does not want such contribution taken into account under this section. Any designation or notification referred to in the preceding sentence shall be made**

in such manner as the Secretary shall by regulations prescribe and, after the last date on which such designation or notification may be made, shall be irrevocable for such taxable year.

**“(3) QUALIFIED EMPLOYER PLAN.**—The term ‘qualified employer plan’ means—

“(A) a plan described in section 401(a) which includes a trust exempt from tax under section 501(a),

“(B) an annuity plan described in section 403(a),

“(C) a qualified bond purchase plan described in section 405(a),

“(D) a simplified employee pension (within the meaning of section 408(k)), and

“(E) a plan under which amounts are contributed by an individual’s employer for an annuity contract described in section 403(b).

**“(4) GOVERNMENT PLAN.**—The term ‘government plan’ means any plan, whether or not qualified, established and maintained for its employees by the United States, by a State or political subdivision thereof, or by an agency or instrumentality of any of the foregoing.

**“(5) PAYMENTS FOR CERTAIN PLANS.**—The term ‘amounts paid to an individual retirement plan’ includes amounts paid for an individual retirement annuity or a retirement bond.

**“(f) OTHER DEFINITIONS AND SPECIAL RULES.**—

**“(1) COMPENSATION.**—For purposes of this section, the term ‘compensation’ includes earned income as defined in section 401(c)(2).

**“(2) MARRIED INDIVIDUALS.**—The maximum deduction under subsections (b) and (c) shall be computed separately for each individual, and this section shall be applied without regard to any community property laws.

**“(3) TIME WHEN CONTRIBUTIONS DEEMED MADE.**—

**“(A) INDIVIDUAL RETIREMENT PLANS.**—For purposes of this section, a taxpayer shall be deemed to have made a contribution to an individual retirement plan on the last day of the preceding taxable year if the contribution is made on account of such taxable year and is made not later than the time prescribed by law for filing the return for such taxable year (including extensions thereof).

**“(B) QUALIFIED EMPLOYER OR GOVERNMENT PLANS.**—For purposes of this section, if a qualified employer or government plan elects to have the provisions of this subparagraph apply, a taxpayer shall be deemed to have made a voluntary contribution to such plan on the last day of the preceding calendar year (if, without regard to this paragraph, such contribution may be made on such date) if the contribution is made by April 15 of the calendar year or such earlier time as is provided by the plan administrator.

**“(4) REPORTS.**—The Secretary shall prescribe regulations which prescribe the time and the manner in which reports to the Secretary and plan participants shall be made by the plan administrator of a qualified employer or government plan receiving qualified voluntary employee contributions.



**“(5) EMPLOYER PAYMENTS.—**For purposes of this title, any amount paid by an employer to an individual retirement plan shall be treated as payment of compensation to the employee (other than a self-employed individual who is an employee within the meaning of section 401(c)(1)) includible in his gross income in the taxable year for which the amount was contributed, whether or not a deduction for such payment is allowable under this section to the employee.

**(6) “EXCESS CONTRIBUTIONS TREATED AS CONTRIBUTION MADE DURING SUBSEQUENT YEAR FOR WHICH THERE IS AN UNUSED LIMITATION.—**

**“(A) IN GENERAL.—**If for the taxable year the maximum amount allowable as a deduction under this section for contributions to an individual retirement plan exceeds the amount contributed, then the taxpayer shall be treated as having made an additional contribution for the taxable year in an amount equal to the lesser of—

“(i) the amount of such excess, or

“(ii) the amount of the excess contributions for such taxable year (determined under section 4973(b)(2) without regard to subparagraph (C) thereof).

**“(B) AMOUNT CONTRIBUTED.—**For purposes of this paragraph, the amount contributed—

“(i) shall be determined without regard to this paragraph, and

“(ii) shall not include any rollover contribution.

**“(C) SPECIAL RULE WHERE EXCESS DEDUCTION WAS ALLOWED FOR CLOSED YEAR.—**Proper reduction shall be made in the amount allowable as a deduction by reason of this paragraph for any amount allowed as a deduction under this section for a prior taxable year for which the period for assessing deficiency has expired if the amount so allowed exceeds the amount which should have been allowed for such prior taxable year.

**“(g) CROSS REFERENCE.—**

**“For failure to provide required reports, see section 6652(h).”**

**(b) TREATMENT OF DISTRIBUTIONS FROM EMPLOYER PLAN TO WHICH EMPLOYEE MADE DEDUCTIBLE CONTRIBUTIONS.—**

**(1) IN GENERAL.—**Section 72 (relating to annuities; certain proceeds of endowment and life insurance contracts) is amended by redesignating subsection (o) as subsection (p) and by inserting after subsection (n) the following new subsection:

**“(o) SPECIAL RULES FOR DISTRIBUTIONS FROM QUALIFIED PLANS TO WHICH EMPLOYEE MADE DEDUCTIBLE CONTRIBUTIONS.—**

**“(1) TREATMENT OF CONTRIBUTIONS.—**For purposes of this section and sections 402, 403, and 405, notwithstanding section 414(h), any deductible employee contribution made to a qualified employer plan or government plan shall be treated as an amount contributed by the employer which is not includible in the gross income of the employee.

**“(2) ADDITIONAL TAX IF AMOUNT RECEIVED BEFORE AGE 59½.—**If—

**“(A) any accumulated deductible employee contributions are received from a qualified employer plan or government**

plan to which the employee made one or more deductible employee contributions,

“(B) such amount is received by the employee before the employee attains the age of 59½, and

“(C) such amount is not attributable to such employee’s becoming disabled (within the meaning of subsection (m)(7)),

then the employee’s tax under this chapter for the taxable year in which such amount is received shall be increased by an amount equal to 10 percent of the amount so received to the extent that such amount is includible in gross income. For purposes of this title, any tax imposed by this paragraph shall be treated as a tax imposed by subsection (m)(5)(B).

“(3) AMOUNTS CONSTRUCTIVELY RECEIVED.—

“(A) IN GENERAL.—For purposes of this subsection, rules similar to the rules provided by subsection (m) (4) and (8) shall apply.

“(B) PURCHASE OF LIFE INSURANCE.—To the extent any amount of accumulated deductible employee contributions of an employee are applied to the purchase of life insurance contracts, such amount shall be treated as distributed to the employee in the year so applied.

“(4) SPECIAL RULE FOR TREATMENT OF ROLLOVER AMOUNTS.—For purposes of sections 402(a)(5), 402(a)(7), 403(a)(4), 408(d)(3), and 409(b)(3)(C), the Secretary shall prescribe regulations providing for such allocations of amounts attributable to accumulated deductible employee contributions, and for such other rules, as may be necessary to insure that such accumulated deductible employee contributions do not become eligible for additional tax benefits (or freed from limitations) through the use of rollovers.

“(5) DEFINITIONS AND SPECIAL RULES.—For purposes of this subsection—

“(A) DEDUCTIBLE EMPLOYEE CONTRIBUTIONS.—The term ‘deductible employee contribution’ means any qualified voluntary employee contribution (as defined in section 219(e)(2)) made after December 31, 1981, in a taxable year beginning after such date and allowable as a deduction under section 219(a) for such taxable year.

“(B) ACCUMULATED DEDUCTIBLE EMPLOYEE CONTRIBUTIONS.—The term ‘accumulated deductible employee contributions’ means the deductible employee contributions—

“(i) increased by the amount of income and gain allocable to such contributions, and

“(ii) reduced by the sum of the amount of loss and expense allocable to such contributions and the amounts distributed with respect to the employee which are attributable to such contributions (or income or gain allocable to such contributions).

“(C) QUALIFIED EMPLOYER PLAN.—The term ‘qualified employer plan’ has the meaning given to such term by section 219(e)(3).

“(D) GOVERNMENT PLAN.—The term ‘government plan’ has the meaning given such term by section 219(e)(4).

**“(6) ORDERING RULES.**—Unless the plan specifies otherwise, any distribution from such plan shall not be treated as being made from the accumulated deductible employee contributions until all other amounts to the credit of the employee have been distributed.”

**(2) 10-YEAR AVERAGING AND CAPITAL GAINS NOT TO APPLY.**—Subparagraph (A) of section 402(e)(4) (defining lump sum distribution) is amended by adding at the end thereof the following new sentence: “For purposes of this section and section 403, the balance to the credit of the employee does not include the accumulated deductible employee contributions under the plan (within the meaning of section 72(o)(5)).”

**(3) CONFORMING AMENDMENTS RELATING TO ROLLOVER DISTRIBUTIONS.**—

**(A) Paragraph (5) of section 402(a) (relating to rollover amounts) is amended—**

**(i) by inserting “(other than accumulated deductible employee contributions within the meaning of section 72(o)(5))” after “contributions” in subparagraph (B),**

**(ii) by striking out “or” at the end of subparagraph (D)(i)(I),**

**(iii) by striking out the period at the end of subparagraph (D)(i)(II) and inserting in lieu thereof “, or”, and**

**(iv) by inserting at the end of subparagraph (D) the following new subclause:**

**“(III) which constitute a distribution of accumulated deductible employee contributions (within the meaning of section 72(o)(5)).”**

**(B) Paragraph (8) of section 403(b) (relating to rollover amounts) is amended by inserting “, or 1 or more distributions of accumulated deductible employee contributions (within the meaning of section 72(o)(5))” after “subsection (a)” in subparagraph (B)(i).**

**(c) UNREALIZED APPRECIATION OF EMPLOYER SECURITIES.**—

**(1) Paragraph (1) of section 402(a) (relating to taxability of beneficiary of exempt trust) is amended by striking out in the second sentence thereof “by the employee” and inserting in lieu thereof “by the employee (other than deductible employee contributions within the meaning of section 72(o)(5)).”**

**(2) Subparagraph (J) of section 402(e) (relating to tax on lump sum distribution) is amended by adding at the end thereof the following new sentence: “This subparagraph shall not apply to distributions of accumulated deductible employee contributions (within the meaning of section 77(o)(5)).”**

**(d) ESTATE AND GIFT TAX EXCLUSION.**—

**(1) ESTATE TAX.**—Subsection (c) of section 2039 (relating to exemption of annuities under certain trusts and plans) is amended by adding at the end thereof the following new sentence: “For purposes of this subsection, any deductible employee contributions (within the meaning of paragraph (5) of section 72(o)) shall be considered as made by a person other than the decedent.”

**(2) GIFT TAX.**—Subsection (b) of section 2517 (relating to transfers attributable to employee contributions) is amended by adding at the end thereof the following new sentence: “For pur-

poses of this subsection, any deductible employee contributions (within the meaning of paragraph (5) of section 72(o)) shall be considered as made by a person other than the employee."

(e) **REPEAL OF SECTION 220.**—Section 220 (relating to deduction for retirement savings for certain married individuals) is hereby repealed.

(f) **PENALTIES FOR FAILURE TO PROVIDE NECESSARY REPORTS.**—Section 6652 is amended by redesignating subsection (h) as subsection (i) and inserting after subsection (g) the following new subsection:

"(h) **INFORMATION REQUIRED IN CONNECTION WITH DEDUCTIBLE EMPLOYEE CONTRIBUTIONS.**—In the case of failure to make a report required by section 219(f)(4) which contains the information required by such section on the date prescribed therefor (determined with regard to any extension of time for filing), there shall be paid (on notice and demand by the Secretary and in the same manner as tax) by the person failing so to file, an amount equal to \$25 for each participant with respect to whom there was a failure to file such information, multiplied by the number of years during which such failure continues, but the total amount imposed under this subsection on any person for failure to file shall not exceed \$10,000."

(g) **AMENDMENTS RELATING TO INCREASE IN IRA LIMITATIONS.**—

(1) The following provisions are each amended by striking out "\$1,500" each place it appears and inserting in lieu thereof "\$2,000":

(A) Section 408(a)(1) (defining individual retirement account).

(B) Section 408(b) (defining individual retirement annuity).

(C) Section 408(j) (relating to increase in maximum limitations for simplified employee pensions).

(D) Section 409(a)(4) (defining retirement bond).

(2) Subparagraph (A) of section 408(d)(5) is amended by striking out "\$1,750" and inserting in lieu thereof "\$2,250".

(3) Subparagraph (A) of section 409(b)(3) (relating to redemption within 12 months) is amended by adding the following sentence at the end thereof: "The preceding sentence shall not apply to the extent that the bond was purchased with a rollover contribution described in subparagraph (C) of this paragraph or in section 402(a)(5), 402(a)(7), 403(a)(4), 403(b)(8), 405(b)(3), or 408(d)(3)."

(4)(A) Paragraph (2) of section 415(a) is amended to read as follows:

"(2) **SECTION APPLIES TO CERTAIN ANNUITIES AND ACCOUNTS.**—  
In the case of—

"(A) an employee annuity plan described in section 403(a),

"(B) an annuity contract described in section 403(b),

"(C) a simplified employee pension described in section 408(k), or

"(D) a plan described in section 405(a),

such a contract, plan, or pension shall not be considered to be described in section 403(a), 403(b), 405(a), or 408(k), as the case may be, unless it satisfies the requirements of subparagraph (A) or subparagraph (B) of paragraph (1), whichever is appropriate,

and has not been disqualified under subsection (g). In the case of an annuity contract described in section 403(b), the preceding sentence shall apply only to the portion of the annuity contract which exceeds the limitation of subsection (b) or the limitation of subsection (c), whichever is appropriate, and the amount of the contribution for such portion shall reduce the exclusion allowance as provided in section 403(b)(2).”

(B) The last sentence of paragraph (2) of section 415(c) is amended to read as follows: “For the purposes of this paragraph, employee contributions under subparagraph (B) are determined without regard to any rollover contributions (as defined in sections 402(a)(5), 403(a)(4), 403(b)(8), 405(d)(3), 408(d)(3), and 409(b)(3)(C)) without regard to employee contributions to a simplified employee pension allowable as a deduction under section 219(a), and without regard to deductible employee contributions within the meaning of section 72(o)(5).”

(C) Paragraph (5) of section 415(e) is amended to read as follows:

“(5) SPECIAL RULES FOR SECTIONS 403(b) AND 408.—For purposes of this section, any annuity contract described in section 403(b) (except in the case of a participant who has elected under subsection (c)(4)(D) to have the provisions of subsection (c)(4)(C) apply) for the benefit of a participant shall be treated as a defined contribution plan maintained by each employer with respect to which the participant has the control required under subsection (b) or (c) of section 414 (as modified by subsection (h)). For purposes of this section, any contribution by an employer to a simplified employee pension for an individual for a taxable year shall be treated as an employer contribution to a defined contribution plan for such individual for such year. In the case of any annuity contract described in section 403(b), the amount of the contribution disqualified by reason of subsection (g) shall reduce the exclusion allowance as provided in section 403(b)(2).”

(h) AMENDMENTS CONFORMING TO THE REPEAL OF SECTION 220.—

(1) Paragraph (10) of section 62 (defining adjusted gross income) is amended by striking out “and the deduction allowed by section 220 (relating to retirement savings for certain married individuals)”.

(2) Paragraphs (4) and (5) of section 408(d) (relating to tax treatment of distributions) are each amended by striking out “section 219 or 220” each place it appears and inserting in lieu thereof “section 219”.

(3) Subsection (a) of section 415 is amended by striking out paragraph (3).

(4) Subsection (e) of section 2039 (relating to exclusion of individual retirement accounts, etc.) is amended by striking out “section 219 or 220” each place it appears and inserting in lieu thereof “section 219”.

(5) Subsection (d) of section 2503 is hereby repealed.

(6) Subparagraph (D) of section 3401(a)(12) is amended by striking out “section 219(a) or 220(a)” and inserting in lieu thereof “section 219(a)”.

(7) Subsection (b) of section 4973 is amended by striking out "section 219 or 220" each place it appears and inserting in lieu thereof "section 219".

(8) Subsection (d) of section 6047 is amended by striking out "section 219(a) or 220(a)" and inserting in lieu thereof "section 219(a)".

(9) Subsection (a) of section 4973 is amended by striking out the last sentence and inserting in lieu thereof the following: "The tax imposed by this subsection shall be paid by such individual."

(10) Subparagraph (C) of section 4973(b)(2) is amended by striking out "sections 219(c)(5) and 220(c)(6)" and inserting in lieu thereof "section 219(f)(6)".

(11) The table of sections for part VII of subchapter B of chapter 1 is amended by striking out the item relating to section 220.

(i) **EFFECTIVE DATES.**—

(1) **IN GENERAL.**—Except as provided in this subsection, the amendments made by this section shall apply to taxable years beginning after December 31, 1981.

(2) **TRANSITIONAL RULE.**—For purposes of the Internal Revenue Code of 1954, any amount allowed as a deduction under section 220 of such Code (as in effect before its repeal by this Act) shall be treated as if it were allowed by section 219 of such Code.

(3) **CERTAIN BOND ROLLOVER PROVISIONS.**—The amendment made by subsection (g)(3) shall apply to taxable years beginning after December 31, 1974.

(4) **SECTION 415 AMENDMENTS.**—The amendments made by subsections (g)(4) and (h)(3) shall apply to years after December 31, 1981.

**SEC. 312. INCREASE IN AMOUNT OF SELF-EMPLOYED RETIREMENT PLAN DEDUCTION.**

(a) **IN GENERAL.**—Subsection (e) of section 404 (relating to special limitations for self-employed individuals) is amended by striking out "\$7,500" in paragraphs (1) and (2) and inserting in lieu thereof "\$15,000".

(b) **MAXIMUM AMOUNT OF COMPENSATION TAKEN INTO ACCOUNT.**—

(1) **IN GENERAL.**—Paragraph (17) of section 401(a) (relating to maximum amount of compensation which may be taken into account) is amended by striking out all after "only" and inserting in lieu thereof "if—

"(A) the annual compensation of each employee taken into account under the plan does not exceed the first \$200,000 of compensation, and

"(B) in the case of—

"(i) a defined contribution plan with respect to which compensation in excess of \$100,000 is taken into account, contributions on behalf of each employee (other than an employee within the meaning of section 401(c)(1)) to the plan or plans are at a rate (expressed as a percentage of compensation) not less than 7.5 percent, or

"(ii) a defined benefit plan with respect to which compensation in excess of \$100,000 is taken into ac-

count, the annual benefit accrual for each employee (other than an employee within the meaning of section 401(c)(1)) is a percentage of compensation which is not less than one-half of the applicable percentage provided by subsection (j)(3)."

(2) **SIMPLIFIED EMPLOYEE PENSIONS.**—Subparagraph (C) of section 408(k)(3) (relating to uniform relationships of contributions) is amended to read as follows:

"(C) **CONTRIBUTIONS MUST BEAR A UNIFORM RELATIONSHIP TO TOTAL COMPENSATION.**—For purposes of subparagraph (A), employer contributions to simplified employee pensions shall be considered discriminatory unless—

"(i) contributions thereto bear a uniform relationship to the total compensation (not in excess of the first \$200,000) of each employee maintaining a simplified employee pension, and

"(ii) if compensation in excess of \$100,000 is taken into account under a simplified employee pension for an employee, contributions to a simplified employee pension on behalf of each employee for whom a contribution is required are at a rate (expressed as a percentage of compensation) not less than 7.5 percent."

(c) **CONFORMING AMENDMENTS.**—

(1) Subparagraphs (A) and (C) of section 219(b)(2), as amended by section 311(a), are each amended by striking out "\$7,500" and inserting in lieu thereof "\$15,000".

(2) Subsection (e) of section 401 is amended by striking out "for all such years exceeds \$7,500" and inserting in lieu thereof "for such taxable year exceeds \$15,000".

(3) Subparagraph (A) of section 401(j)(2) (relating to benefit plans for self-employed individuals and shareholder-employees) is amended by striking out "\$50,000" and inserting in lieu thereof "\$100,000".

(4) Paragraph (3) of section 401(j) is amended by adding at the end thereof the following new sentence: "For purposes of this paragraph, a change in the annual compensation taken into account under subparagraph (A) of subsection (j)(2) shall be treated as beginning a new period of plan participation."

(5) Subsections (d)(5) and (j) of section 408 are each amended by striking out "\$7,500" and inserting in lieu thereof "\$15,000".

(6) Subparagraph (B) of section 1379(b)(1) (relating to certain qualified pension, etc., plans) is amended by striking out "\$7,500" and inserting in lieu thereof "\$15,000".

(d) **LOANS TO PARTICIPANTS.**—Subsection (m) of section 72 (relating to special rules) is amended—

(1) by adding at the end of paragraph (6) the following new sentence: "For purposes of the preceding sentence, the term 'owner-employee' shall except in applying paragraph (5), include an employee within the meaning of section 401(c)(1).", and

(2) by adding at the end thereof the following new paragraph:

"(8) **LOANS TO OWNER-EMPLOYEES.**—If, during any taxable year, an owner-employee receives, directly or indirectly, any amount as a loan from a trust described in section 401(a) which is exempt from tax under section 501(a), such amount shall be

treated as having been received by such owner-employee as a distribution from such trust.”

**(e) CORRECTION OF EXCESS CONTRIBUTION PERMITTED WITHOUT PENALTY.—**

(1) Subsection (m) of section 72 (relating to special rules applicable to employee annuities and distributions under employee plans) (as amended by subsection (d)) is amended by adding at the end thereof the following new paragraph:

“(9) RETURN OF EXCESS CONTRIBUTIONS BEFORE DUE DATE OF RETURN.—

“(A) IN GENERAL.—If an excess contribution is distributed in a qualified distribution—

“(i) such distribution of such excess contribution shall not be included in gross income, and

“(ii) this section (other than this paragraph) shall be applied as if such excess contribution and such distribution had not been made.

“(B) EXCESS CONTRIBUTION.—For purposes of this paragraph, the term ‘excess contribution’ means any contribution to a qualified trust described in section 401(a) or under a plan described in section 403(a) or 405(a) made on behalf of an employee (within the meaning of section 401(c)) for any taxable year to the extent such contribution exceeds the amount allowable as a deduction under section 404(a).

“(C) QUALIFIED DISTRIBUTION.—The term ‘qualified distribution’ means any distribution of an excess contribution which meets requirements similar to the requirements of subparagraphs (A), (B), and (C) of section 408(d)(4). In the case of such a distribution, the rules of the last sentence of section 408(d)(4) shall apply.”

(2) Paragraph (4) of section 401(d) (relating to additional requirements for qualification of trusts and plans benefiting owner-employees) is amended by adding at the end thereof the following new sentence: “Subparagraph (B) shall not apply to any distribution to which section 72(m)(9) applies.”

(3) Subsection (b) of section 4972 (defining excess contributions) is amended by adding at the end thereof the following new paragraph:

“(6) EXCESS CONTRIBUTIONS RETURNED BEFORE DUE DATE.—For purposes of this subsection, any contribution which is distributed in a distribution to which section 72(m)(9) applies shall be treated as an amount not contributed.”

**(f) EFFECTIVE DATE.—**

(1) IN GENERAL.—Except as provided in paragraph (2), the amendments made by this section shall apply to plans which include employees within the meaning of section 401(c)(1) with respect to taxable years beginning after December 31, 1981.

(2) TRANSITIONAL RULE.—The amendments made by subsection (d) shall not apply to any loan from a plan to a self-employed individual who is an employee within the meaning of section 401(c)(1) which is outstanding on December 31, 1981. For purposes of the preceding sentence, any loan which is renegotiated, extended, renewed, or revised after such date shall be treated as a new loan.



**SEC. 313. ROLLOVERS UNDER BOND PURCHASE PLANS.**

(a) **GENERAL RULE.**—Subsection (d) of section 405 (relating to taxability of beneficiary of qualified bond purchase plan) is amended by adding at the end thereof the following new paragraph:

“(3) **ROLLOVER INTO AN INDIVIDUAL RETIREMENT ACCOUNT OR ANNUITY.**—

“(A) **IN GENERAL.**—If—

“(i) any qualified bond is redeemed,

“(ii) any portion of the excess of the proceeds from such redemption over the basis of such bond is transferred to an individual retirement plan which is maintained for the benefit of the individual redeeming such bond, and

“(iii) such transfer is made on or before the 60th day after the day on which the individual received the proceeds of such redemption,

then, gross income shall not include the proceeds to the extent so transferred and the transfer shall be treated as a rollover contribution described in section 408(d)(3).

“(B) **QUALIFIED BOND.**—For purposes of this paragraph, the term ‘qualified bond’ means any bond described in subsection (b) which is distributed under a qualified bond purchase plan or from a trust described in section 401(a) which is exempt from tax under section 501(a).”

(b) **TECHNICAL AMENDMENTS.**—

(1) The second sentence of paragraph (1) of section 405(d) is amended by striking out “the proceeds” and inserting “except as provided in paragraph (3), the proceeds”.

(2) Sections 219(c)(2), 408(a)(1), and 4973(b)(1)(A) are each amended by inserting “405(d)(3),” after “403(b)(8),”.

(3) Subsection (e) of section 2039 is amended by inserting “405(d)(3),” after “a contract described in subsection (c)(3),”.

(c) **EFFECTIVE DATE.**—The amendments made by this section shall apply to redemptions after the date of the enactment of this Act in taxable years ending after such date.

**SEC. 314. MISCELLANEOUS PROVISIONS.**

(a) **REMOVAL OF FIVE-YEAR BAN ON CONTRIBUTIONS TO OWNER-EMPLOYEE PLANS WHERE PLAN TERMINATES.**—

(1) **IN GENERAL.**—Paragraph (5) of section 401(d) (relating to additional requirements for qualifications of trusts and plans benefiting owner-employees) is amended by adding at the end thereof the following: “Subparagraph (C) shall not apply to a distribution on account of the termination of the plan.”

(2) **EFFECTIVE DATE.**—The amendment made by paragraph (1) shall apply to distributions after December 31, 1980, in taxable years beginning after such date.

(b) **INVESTMENT BY INDIVIDUAL RETIREMENT ACCOUNTS, ETC., IN COLLECTIBLES TREATED AS DISTRIBUTIONS.**—

(1) **IN GENERAL.**—Section 408 (relating to individual retirement accounts) is amended by redesignating subsection (n) as subsection (o) and by inserting after subsection (m) the following new subsection:

“(n) **INVESTMENT IN COLLECTIBLES TREATED AS DISTRIBUTIONS.**—

“(1) **IN GENERAL.**—The acquisition by an individual retirement account or by an individually-directed account under a

plan described in section 401(a) of any collectible shall be treated (for purposes of this section and section 402) as a distribution from such account in an amount equal to the cost to such account of such collectible.

“(2) **COLLECTIBLE DEFINED.**—For purposes of this subsection, the term ‘collectible’ means—

“(A) any work of art,

“(B) any rug or antique,

“(C) any metal or gem,

“(D) any stamp or coin,

“(E) any alcoholic beverage, or

“(F) any other tangible personal property specified by the Secretary for purposes of this subsection.”

(2) **EFFECTIVE DATE.**—The amendment made by paragraph (1) shall apply to property acquired after December 31, 1981, in taxable years ending after such date.

(c) **TAXABILITY OF DISTRIBUTIONS TO EMPLOYEES.**—

(1) **CONTRIBUTIONS MADE AVAILABLE.**—Paragraph (1) of section 402(a) (relating to taxability of beneficiary of exempt trust) is amended by striking out each place it appears “or made available”.

(2) **EFFECTIVE DATE.**—The amendment made by paragraph (1) shall apply to taxable years beginning after December 31, 1981.

### **Subtitle C—Reinvestment of Dividends in Public Utilities**

#### **SEC. 321. ENCOURAGEMENT OF REINVESTMENT OF DIVIDENDS IN THE STOCK OF PUBLIC UTILITIES.**

(a) **AMENDMENT OF SECTION 305.**—Section 305 (relating to distributions of stock and stock rights) is amended by redesignating subsection (e) as subsection (f) and by inserting after subsection (d) the following new subsection:

“(e) **DIVIDEND REINVESTMENT IN STOCK OF PUBLIC UTILITIES.**—

“(1) **IN GENERAL.**—Subsection (b) shall not apply to any qualified reinvested dividend.

“(2) **QUALIFIED REINVESTED DIVIDEND DEFINED.**—For purposes of this subsection, the term ‘qualified reinvested dividend’ means—

“(A) a distribution by a qualified public utility of shares of its qualified common stock to an individual with respect to the common or preferred stock of such corporation pursuant to a plan under which shareholders may elect to receive dividends in the form of stock instead of property, but

“(B) only if the shareholder elects to have this subsection apply to such shares.

“(3) **QUALIFIED PUBLIC UTILITY DEFINED.**—

“(A) **IN GENERAL.**—For purposes of this subsection, the term ‘qualified public utility’ means, for any taxable year of the corporation, a domestic corporation which, for the 10-year period ending on the day before the beginning of the taxable year, acquired public utility recovery property having a cost equal to at least 60 percent of the aggregate cost of all tangible personal depreciable property acquired by the corporation during such period.

**“(B) SPECIAL RULES.—For purposes of subparagraph (A)—**

**“(i) all members of an affiliated group shall be treated as one corporation,**

**“(ii) a successor corporation shall take into account the acquisitions of its predecessor, and**

**“(iii) a new corporation to which clause (ii) does not apply shall substitute its period of existence for the 10-year period set forth in subparagraph (A).**

**“(C) DEFINITIONS.—For purposes of this paragraph—**

**“(i) AFFILIATED GROUP.—The term ‘affiliated group’ has the meaning given to such term by subsection (a) of section 1504 (determined without regard to subsection (b) of section 1504).**

**“(ii) PUBLIC UTILITY RECOVERY PROPERTY.—The term ‘public utility recovery property’ means public utility property (within the meaning of section 167(1)(3)(A)) which is recovery property which is 10-year property or 15-year public utility property (within the meaning of section 168), except that any requirement that the property be placed in service after December 31, 1980, shall not apply.**

**“(4) QUALIFIED COMMON STOCK DEFINED.—**

**“(A) IN GENERAL.—For purposes of this subsection, the term ‘qualified common stock’ means authorized but unissued common stock of the corporation—**

**“(i) which has been designated by the board of directors of the corporation as issued for purposes of this subsection, but**

**“(ii) only if the number of shares to be issued to a shareholder was determined by reference to a value which is not less than 95 percent and not more than 105 percent of the stock’s fair market value during the period immediately before the distribution (determined under regulations prescribed by the Secretary).**

**“(B) CERTAIN PURCHASES BY CORPORATION OF ITS OWN STOCK.—Except as provided in subparagraph (D), if a corporation has purchased or purchases its common stock within a 2-year period beginning 1 year before the date of the distribution and ending 1 year after such date, such distribution shall be treated as not being a qualified reinvested dividend.**

**“(C) MEMBERS OF AFFILIATED GROUP.—For purposes of subparagraph (B), the purchase by any corporation which is a member of the same affiliated group (as defined in paragraph (3)(C)(i)) as the distributing corporation of common stock in any corporation which is a member of such group from any person (other than a member of such group) shall be treated as a purchase by the distributing corporation of its common stock.**

**“(D) WAIVER OF SUBPARAGRAPH (B) WHERE THERE IS BUSINESS PURPOSE.—Under regulations prescribed by the Secretary, subparagraph (B) shall not apply where the distributing corporation establishes that there was a business purpose for the purchase of the stock and such purchase is not inconsistent with the purposes of this subsection.**

**“(5) SHARE INCLUDES FRACTIONAL SHARE.—**For purposes of this subsection, the term ‘share’ includes a fractional share.

**“(6) LIMITATION.—**

**“(A) IN GENERAL.—**In the case of any individual, the aggregate amount of distributions to which this subsection applies for the taxable year shall not exceed \$750 (\$1,500 in the case of a joint return).

**“(B) APPLICATION OF CEILING.—**If, but for this subparagraph, a share of stock would, by reason of subparagraph (A), be treated as partly within this subsection and partly outside this subsection, such share shall be treated as outside this subsection.

**“(7) BASIS AND HOLDING PERIOD.—**In the case of stock received as a qualified reinvested dividend—

**“(A) notwithstanding section 307, the basis shall be zero, and**

**“(B) the holding period shall begin on the date the dividend would (but for this subsection) be includible in income.**

**“(8) ELECTION.—**An election under this subsection with respect to any share shall be made on the shareholder’s return for the taxable year in which the dividend would (but for this subsection) be includible in income. Any such election, once made, shall be revocable only with the consent of the Secretary.

**“(9) DISPOSITIONS WITHIN 1 YEAR OF DISTRIBUTION.—**Under regulations prescribed by the Secretary—

**“(A) DISPOSITION OF OTHER COMMON STOCK.—**If—

**“(i) a shareholder receives any qualified reinvested dividend from a corporation, and**

**“(ii) during the period which begins on the record date for the qualified reinvested dividend and ends 1 year after the date of the distribution of such dividend, the shareholder disposes of any common stock of such corporation,**

**the shareholder shall be treated as having disposed of the stock received as a qualified reinvested dividend (to the extent there remains such stock to which this paragraph has not applied).**

**“(B) ORDINARY INCOME TREATMENT.—**If any stock received as a qualified reinvested dividend is disposed of within 1 year after the date such stock is distributed, such disposition shall be treated as a disposition of property which is not a capital asset.

**“(10) NO REDUCTION IN EARNINGS AND PROFITS FOR DISTRIBUTION OF QUALIFIED COMMON STOCK.—**The earnings and profits of any corporation shall not be reduced by reason of the distribution of any qualified common stock of such corporation pursuant to a plan under which shareholders may elect to receive dividends in the form of stock instead of property.

**“(11) CERTAIN INDIVIDUALS INELIGIBLE.—**

**“(A) IN GENERAL.—**This subsection shall not apply to any individual who is—

**“(i) a trust or estate, or**

**“(ii) a nonresident alien individual.**

**“(B) 5 PERCENT SHAREHOLDERS INELIGIBLE.**—Any distribution by a corporation to a 5 percent shareholder in such corporation shall not be treated as a qualified reinvested dividend.

**“(C) 5 PERCENT SHAREHOLDER DEFINED.**—For purposes of subparagraph (B), the term ‘5 percent shareholder’ means any individual who, immediately before the distribution, owns (directly or through the application of section 318)—

“(i) stock possessing more than 5 percent of the total combined voting power of the distributing corporation, or

“(ii) more than 5 percent of the total value of all classes of stock of the distributing corporation.

**“(12) TERMINATION.**—This subsection shall not apply to distributions after December 31, 1985.”

**(b) AMENDMENT OF SECTION 305(d).**—Paragraph (1) of section 305(d) (defining stock) is amended by striking out “this section” and inserting in lieu thereof “this section (other than subsection (e))”.

**(c) EFFECTIVE DATE.**—The amendments made by this section shall apply to distributions after December 31, 1981, in taxable years ending after such date.

## **Subtitle D—Employee Stock Ownership Provisions**

### **SEC. 331. PAYROLL-BASED CREDIT FOR ESTABLISHING EMPLOYEE STOCK OWNERSHIP PLAN.**

**(a) IN GENERAL.**—Subpart A of part IV of subchapter A of chapter 1 (relating to credits allowed), as amended by section 221 of this Act, is further amended by inserting immediately after section 44F the following new section:

#### **“SEC. 44G. EMPLOYEE STOCK OWNERSHIP CREDIT.**

**“(a) GENERAL RULE.**—

**“(1) CREDIT ALLOWED.**—In the case of a corporation which elects to have this section apply for the taxable year and which meets the requirements of subsection (c)(1), there is allowed as a credit against the tax imposed by this chapter for the taxable year an amount equal to the amount of the credit determined under paragraph (2) for such taxable year.

**“(2) DETERMINATION OF AMOUNT.**—

**“(A) IN GENERAL.**—The amount of the credit determined under this paragraph for the taxable year shall be equal to the lesser of—

“(i) the aggregate value of employer securities transferred by the corporation for the taxable year to a tax credit employee stock ownership plan maintained by the corporation, or

“(ii) the applicable percentage of the amount of the aggregate compensation (within the meaning of section 415(c)(3)) paid or accrued during the taxable year to all employees under a tax credit employee stock ownership plan.

**“(B) APPLICABLE PERCENTAGE.**—For purposes of applying subparagraph (A)(ii), the applicable percentage shall be determined in accordance with the following table:

**“For aggregate compensation paid or accrued during a portion of the taxable year occurring in calendar year:**

	<i>The applicable percentage is:</i>
1983.....	0.5
1984.....	0.5
1985.....	0.75
1986.....	0.75
1987.....	0.75
1988 or thereafter.....	0

**“(b) LIMITATION BASED ON AMOUNT OF TAX.—**

**“(1) LIABILITY FOR TAX.—**

**“(A) IN GENERAL.—**The credit allowed by subsection (a) for any taxable year shall not exceed an amount equal to the sum of—

“(i) so much of the liability for tax for the taxable year as does not exceed \$25,000, plus

“(ii) 90 percent of so much of the liability for tax for the taxable year as exceeds \$25,000.

**“(B) LIABILITY FOR TAX DEFINED.—**For purposes of this paragraph, the term ‘liability for tax’ means the tax imposed by this chapter for the taxable year, reduced by the sum of the credits allowed under a section of this subpart having a lower number designation than this section, other than credits allowable by sections 31, 39, and 43. For purposes of the preceding sentence, the term ‘tax imposed by this chapter’ shall not include any tax treated as not imposed by this chapter under the last sentence of section 53(a).

**“(C) CONTROLLED GROUPS.—**In the case of a controlled group of corporations, the \$25,000 amount specified in subparagraph (A) shall be reduced for each component member of such group by apportioning \$25,000 among the component members of such group in such manner as the Secretary shall by regulations prescribe. For purposes of the preceding sentence, the term ‘controlled group of corporations’ has the meaning assigned to such term by section 1563(a) (determined without regard to subsections (a)(4) and (e)(3)(C) of such section).

**“(2) CARRYBACK AND CARRYOVER OF UNUSED CREDIT.—**

**“(A) ALLOWANCE OF CREDIT.—**If the amount of the credit determined under this section for any taxable year exceeds the limitation provided under paragraph (1)(A) for such taxable year (hereinafter in this paragraph referred to as the ‘unused credit year’), such excess shall be—

“(i) an employee stock ownership credit carryback to each of the 3 taxable years preceding the unused credit year, and

“(ii) an employee stock ownership credit carryover to each of the 15 taxable years following the unused credit year,

and shall be added to the amount allowable as a credit by this section for such years. If any portion of such excess is a carryback to a taxable year ending before January 1, 1983, this section shall be deemed to have been in effect for such taxable year for purposes of allowing such carryback as a

credit under this section. The entire amount of the unused credit for an unused credit year shall be carried to the earliest of the 18 taxable years to which (by reason of clauses (i) and (ii)) such credit may be carried, and then to each of the other 17 taxable years to the extent that, because of the limitation contained in subparagraph (B), such unused credit may not be added for a prior taxable year to which such unused credit may be carried.

“(B) **LIMITATION.**—The amount of the unused credit which may be added under subparagraph (A) for any preceding or succeeding taxable year shall not exceed the amount by which the limitation provided under paragraph (1)(A) for such taxable year exceeds the sum of—

“(i) the credit allowable under this section for such taxable year, and

“(ii) the amounts which, by reason of this paragraph, are added to the amount allowable for such taxable year and which are attributable to taxable years preceding the unused credit year.

“(3) **CERTAIN REGULATED COMPANIES.**—No credit shall be allowed under this section to a taxpayer if—

“(A) the taxpayer’s cost of service for ratemaking purposes or in its regulated books of account is reduced by reason of any portion of such credit which results from the transfer of employer securities or cash to a tax credit employee stock ownership plan which meets the requirements of section 409A;

“(B) the base to which the taxpayer’s rate of return for ratemaking purposes is applied is reduced by reason of any portion of such credit which results from a transfer described in subparagraph (A) to such employee stock ownership plan; or

“(C) any portion of the amount of such credit which results from a transfer described in subparagraph (A) to such employee stock ownership plan is treated for ratemaking purposes in any way other than as though it had been contributed by the taxpayer’s common shareholders.

“(c) **DEFINITIONS AND SPECIAL RULES.**—

“(1) **REQUIREMENTS FOR CORPORATION.**—A corporation meets the requirements of this paragraph if it—

“(A) establishes a plan—

“(i) which meets the requirements of section 409A, and

“(ii) under which no more than one-third of the employer contributions for the taxable year are allocated to the group of employees consisting of—

“(I) officers,

“(II) shareholders owning more than 10 percent of the employer’s stock (within the meaning of section 415(c)(6)(B)(iv)), or

“(III) employees described in section 415(c)(6)(B)(iii), and

“(B) agrees, as a condition for the allowance of the credit allowed by this subsection—

“(i) to make transfers of employer securities to a tax credit employee stock ownership plan maintained by the corporation having an aggregate value of not more than the applicable percentage for the taxable year (determined under subsection (a)(2)) of the amount of the aggregate compensation (within the meaning of section 415(c)(3)) paid or accrued by the corporation during the taxable year, and

“(ii) to make such transfers at the times prescribed in paragraph (2).

“(2) **TIMES FOR MAKING TRANSFERS.**—The transfers required under paragraph (1)(B) shall be made not later than 30 days after the due date (including extensions) for filing the return for the taxable year.

“(3) **ADJUSTMENTS TO CREDIT.**—If the credit allowed under this section is reduced by a final determination, the employer may reduce the amount required to be transferred to the tax credit employee stock ownership plan under paragraph (1)(B) for the taxable year in which the final determination occurs or any succeeding taxable year by an amount equal to such reduction to the extent such reduction is not taken into account in any deduction allowed under section 404(i)(2).

“(4) **CERTAIN CONTRIBUTIONS OF CASH TREATED AS CONTRIBUTIONS OF EMPLOYER SECURITIES.**—For purposes of this section, a transfer of cash shall be treated as a transfer of employer securities if the cash is, under the tax credit employee stock ownership plan, used within 30 days to purchase employer securities.

“(5) **DISALLOWANCE OF DEDUCTION.**—Except as provided in section 404(i), no deduction shall be allowed under section 162, 212, or 404 for amounts required to be transferred to a tax credit employee stock ownership plan under this section.

“(6) **EMPLOYER SECURITIES.**—For purposes of this section, the term ‘employer securities’ has the meaning given such term in section 409A(1).

“(7) **VALUE.**—For purposes of this section, the term ‘value’ means—

“(A) in the case of securities listed on a national exchange, the average of closing prices of such securities for the 20 consecutive trading days immediately preceding the date on which the securities are contributed to the plan, or

“(B) in the case of securities not listed on a national exchange, the fair market value as determined in good faith and in accordance with regulations prescribed by the Secretary.”

(b) **DEDUCTIBILITY OF UNUSED PORTIONS OF THE CREDIT.**—Section 404 is amended by adding at the end thereof the following new subsection:

“(i) **DEDUCTIBILITY OF UNUSED PORTIONS OF EMPLOYEE STOCK OWNERSHIP CREDIT.**—

“(1) **UNUSED CREDIT CARRYOVERS.**—There shall be allowed as a deduction (without regard to any limitations provided under this section) for the last taxable year to which an unused employee stock ownership credit carryover (within the meaning of section 44G(b)(2)(A)) may be carried, an amount equal to the



portion of such unused credit carryover which expires at the close of such taxable year.

*“(2) REDUCTIONS IN CREDIT.—There shall be allowed as a deduction (subject to the limitations provided under this section) an amount equal to any reduction of the credit allowed under section 44G resulting from a final determination of such credit to the extent such reduction is not taken into account in section 44G(c)(3).”*

*(c) CONFORMING AMENDMENTS.—*

*(1) Section 409A (relating to qualifications for tax credit employee stock ownership plans) is amended—*

*(A) by inserting “or 44G(c)(1)(B)” after “section 48(n)(1)(A)” in subsection (b)(1)(A),*

*(B) by inserting “or the credit allowed under section 44G (relating to the employee stock ownership credit)” after “basic employee plan credit” in subsection (b)(4),*

*(C) by inserting “or 44G(c)(1)(B)” after “section 48(n)(1)” in subsection (g),*

*(D) by inserting “or the credit allowed under section 44G (relating to employee stock ownership credit)” after “employee plan credit” in subsection (g),*

*(E) by inserting “or 44G(c)(1)(B)” after “section 48(n)(1)” in subsection (i)(1)(A),*

*(F) by inserting “section 44G(c)(1)(B), or” after “required under” in subsection (m),*

*(G) by inserting “or employee stock ownership credit” after “employee plan credit” in subsection (n)(2), and*

*(H) by adding at the end of subsection (n) the following new paragraph:*

*“(3) For requirements for allowance of an employee stock ownership credit, see section 44G.”*

*(2) Subsection (c) of section 56 (relating to regular tax deductions defined) is amended by striking out “and 43” and inserting in lieu thereof “43, and 44G”.*

*(3) Subsection (a) of section 6699 (relating to assessable penalties relating to tax credit employee stock ownership plan) is amended—*

*(A) by inserting “or a credit allowable under section 44G (relating to the employee stock ownership credit)” after “employee plan credit”,*

*(B) by striking out “section 409A, or” in paragraph (1) and inserting in lieu thereof “section 409A with respect to a qualified investment made before January 1, 1983,”*

*(C) by inserting after paragraph (2) the following new paragraphs:*

*“(3) fails to satisfy any requirement provided under section 409A with respect to a credit claimed under section 44G in taxable years ending after December 31, 1982, or*

*“(4) fails to make any contribution which is required under section 44G(c)(1)(B) within the period required for making such contribution.”*

*(4) Paragraph (2) of section 6699 is amended to read as follows:*

*“(2) MAXIMUM AND MINIMUM AMOUNT.—*

*“(A) The amount determined under paragraph (1) with respect to a failure described in paragraph (1) or (2) of subsection (a)—*

*“(i) shall not exceed the amount of the employee plan credit claimed by the employer to which such failure relates, and*

*“(ii) shall not be less than the product of one-half of 1 percent of the amount referred to in subparagraph (A), multiplied by the number of months (or parts thereof) during which such failure continues.*

*“(B) The amount determined under paragraph (1) with respect to a failure described in paragraph (3) or (4) of subsection (a)—*

*“(i) shall not exceed the amount of the credit claimed by the employer under section 44G to which such failure relates, and*

*“(ii) shall not be less than the product of one-half of 1 percent of the amount referred to in subparagraph (A), multiplied by the number of months (or parts thereof) during which such failure continues.”*

**(d) TECHNICAL AMENDMENTS RELATED TO CARRYOVER AND CARRY-BACK OF CREDITS.—**

**(1) CARRYOVER OF CREDIT.—**

*(A) Subparagraph (A) of section 55(c)(4) (relating to credits), as amended by this Act, is amended by inserting “44G(b)(1),” before “53(b)”*

*(B) Subsection (c) of section 381 (relating to items of the distributor or transferor corporation), as amended by this Act, is amended by adding at the end thereof the following new paragraph:*

*“(29) CREDIT UNDER SECTION 44G.—The acquiring corporation shall take into account (to the extent proper to carry out the purposes of this section and section 44G, and under such regulations as may be prescribed by the Secretary) the items required to be taken into account for purposes of section 44G in respect of the distributor or transferor corporation.”*

*(C) Section 383 (relating to special limitations on unused investment credits, work incentive program credits, new employee credits, alcohol fuel credits, foreign taxes, and capital losses), as in effect for taxable years beginning with and after the first taxable year to which the amendments made by the Tax Reform Act of 1976 apply, is amended—*

*(i) by inserting “to any unused credit of the corporation under section 44G(b)(2),” after “44F(g)(2),” and*

*(ii) by inserting “EMPLOYEE STOCK OWNERSHIP CREDITS,” after “RESEARCH CREDITS,” in the section heading.*

*(D) Section 383 (as in effect on the day before the date of the enactment of the Tax Reform Act of 1976) is amended—*

*(i) by inserting “to any unused credit of the corporation which could otherwise be carried forward under section 44G(b)(2),” after “44F(g)(2),” and*

*(ii) by inserting “EMPLOYEE STOCK OWNERSHIP CREDITS,” after “RESEARCH CREDITS,” in the section heading.*

*(E) The Table of sections for part V of subchapter C of chapter 1 is amended by inserting “employee stock owner-*

ship credits," after "research credits," in the item relating to section 383.

**(2) CARRYBACK OF CREDIT.—**

(A) Subparagraph (C) of section 6511(d)(4) (defining credit carryback), as amended by this Act, is amended by striking out "and research credit carryback" and inserting in lieu thereof "research credit carryback, and employee stock ownership credit carryback".

(B) Section 6411 (relating to quick refunds in respect of tentative carryback adjustments), as amended by this Act, is amended—

(i) by striking out "or unused research credit" each place it appears and inserting in lieu thereof "unused research credit, or unused employee stock ownership credit";

(ii) by inserting "by an employee stock ownership credit carryback provided by section 44G(b)(2)" after "by a research and experimental credit carryback provided in section 44F(g)(2), in the first sentence of subsection (a);

(iii) by striking out "or a research credit carryback from" each place it appears and inserting in lieu thereof "a research credit carryback, or employee stock ownership credit carryback from"; and

(iv) by striking out "new employee credit carryback)" in the second sentence of subsection (a) and inserting in lieu thereof "new employee credit carryback, or, in the case of an employee stock ownership credit carryback, to an investment credit carryback, a new employee credit carryback or a research and experimental credit carryback)".

**(e) OTHER TECHNICAL AND CLERICAL AMENDMENTS.—**

(1) Subsection (b) of section 6096 (relating to designation of income tax payments to Presidential Election Campaign Fund), as amended by this Act, is amended by striking out "and 44F" and inserting in lieu thereof "44F, and 44G".

(2) The table of sections for subpart A of part IV of subchapter A of chapter 1 is amended by inserting after the item relating to section 44F the following new item:

"Sec. 44G. Employee stock ownership credit."

**(f) EFFECTIVE DATE.—**

(1) The amendments made by subsection (a) shall apply to aggregate compensation (within the meaning of section 415(c)(3) of the Internal Revenue Code of 1954), paid or accrued after December 31, 1982, in taxable years ending after such date.

(2) The amendments made by subsections (b) and (c) shall apply to taxable years ending after December 31, 1982.

**SEC. 332. TERMINATION OF THE PORTION OF THE INVESTMENT CREDIT ATTRIBUTABLE TO EMPLOYEE PLAN PERCENTAGE.**

(a) **IN GENERAL.—**Subparagraph (E) of section 46(a)(2) (relating to employee plan percentage) is amended—

(1) by striking out "December 31, 1983" in clauses (i) and (ii) and inserting in lieu thereof "December 31, 1982";

(2) by striking out "and" at the end of clause (i),

(3) by striking out the period at the end of clause (ii) and inserting in lieu thereof “, and”, and

(4) by inserting after clause (ii) the following new clause:

“(iii) with respect to any period beginning after December 31, 1982, zero.”

(b) **TECHNICAL AMENDMENT.**—Clause (i) of section 48(n)(1)(A) (relating to requirements for allowance of employee plan percentage) is amended by striking out “equal to” and inserting in lieu thereof “which does not exceed”.

(c) **EFFECTIVE DATES.**—

(1) The amendments made by subsection (a) shall be effective on the date of enactment of this Act.

(2) The amendment made by subsection (b) shall apply to qualified investments made after December 31, 1981.

**SEC. 333. TAX TREATMENT OF CONTRIBUTIONS ATTRIBUTABLE TO PRINCIPAL AND INTEREST PAYMENTS IN CONNECTION WITH AN EMPLOYEE STOCK OWNERSHIP PLAN.**

(a) **DEDUCTIBILITY.**—Section 404(a) (relating to deductions for employer contributions to an employees’ trust) is amended by adding at the end thereof the following new paragraph:

“(10) **CERTAIN CONTRIBUTIONS TO EMPLOYEE STOCK OWNERSHIP PLANS.**—

“(A) **PRINCIPAL PAYMENTS.**—Notwithstanding the provisions of paragraphs (3) and (7), if contributions are paid into a trust which forms a part of an employee stock ownership plan (as described in section 4975(e)(7)), and such contributions are, on or before the time prescribed in paragraph (6), applied by the plan to the repayment of the principal of a loan incurred for the purpose of acquiring qualifying employer securities (as described in section 4975(e)(8)), such contributions shall be deductible under this paragraph for the taxable year determined under paragraph (6). The amount deductible under this paragraph shall not, however, exceed 25 percent of the compensation otherwise paid or accrued during the taxable year to the employees under such employee stock ownership plan. Any amount paid into such trust in any taxable year in excess of the amount deductible under this paragraph shall be deductible in the succeeding taxable years in order of time to the extent of the difference between the amount paid and deductible in each such succeeding year and the maximum amount deductible for such year under the preceding sentence.

“(B) **INTEREST PAYMENT.**—Notwithstanding the provisions of paragraphs (3) and (7), if contributions are made to an employee stock ownership plan (described in subparagraph (A)) and such contributions are applied by the plan to the repayment of interest on a loan incurred for the purpose of acquiring qualifying employer securities (as described in subparagraph (A)), such contributions shall be deductible for the taxable year with respect to which such contributions are made as determined under paragraph (6).”

(b) **EXCLUSION FROM LIMITATION ON ANNUAL ADDITIONS.**—

(1) **IN GENERAL.**—Section 415(c)(6) (relating to limitations on benefits and contributions made under qualified plans) is amended by adding at the end thereof the following new subparagraph:

“(C) In the case of an employee stock ownership plan (as described in section 4975(e)(7)), under which no more than one-third of the employer contributions for a year which are deductible under paragraph (10) of section 404(a) are allocated to the group of employees consisting of officers, shareholders owning more than 10 percent of the employer’s stock (determined under subparagraph (B)(iv)), or employees described in subparagraph (B)(iii), the limitations imposed by this section shall not apply to—

“(i) forfeitures of employer securities under an employee stock ownership plan (as described in section 4975(e)(7)) if such securities were acquired with the proceeds of a loan (as described in section 404(a)(10)(A)), or

“(ii) employer contributions to such an employee stock ownership plan which are deductible under section 404(a)(10)(B) and charged against the participant’s account.”

(2) **EFFECTIVE DATE.**—The amendment made by this subsection shall apply to years beginning after December 31, 1981.

**SEC. 334. CASH DISTRIBUTIONS FROM AN EMPLOYEE STOCK OWNERSHIP PLAN.**

Section 409A(h)(2) (relating to right to demand employer securities) is amended—

(1) by adding at the end thereof the following new sentence: “In the case of an employer whose charter or bylaws restrict the ownership of substantially all outstanding employer securities to employees or to a trust described in section 401(a), a plan which otherwise meets the requirements of this subsection or section 4975(e)(7) shall not be considered to have failed to meet the requirements of section 401(a) merely because it does not permit a participant to exercise the right described in paragraph (1)(A) if such plan provides that participants entitled to a distribution from the plan shall have a right to receive such distribution in cash.”; and

(2) by striking out “this section” in the first sentence thereof and inserting in lieu thereof “this subsection”.

**SEC. 335. PUT OPTION FOR STOCK BONUS PLANS.**

Section 401(a)(23) (relating to cash distribution option for stock bonus plans) is amended by striking out “409A(h)(2)” and inserting in lieu thereof “409A(h), except that in applying section 409A(h) for purposes of this paragraph, the term ‘employer securities’ shall include any securities of the employer held by the plan”.

**SEC. 336. PUT OPTION REQUIREMENTS FOR BANKS; PUT OPTION PERIOD.**

Section 409A(h) (relating to put options for employee stock ownership plans) is amended by adding at the end thereof the following new paragraphs:

“(3) **SPECIAL RULE FOR BANKS.**—In the case of a plan established and maintained by a bank (as defined in section 581) which is prohibited by law from redeeming or purchasing its own securities, the requirements of paragraph (1)(B) shall not apply if the plan provides that participants entitled to a distri-

bution from the plan shall have a right to receive a distribution in cash.

**“(4) PUT OPTION PERIOD.**—An employer shall be deemed to satisfy the requirements of paragraph (1)(B) if it provides a put option for a period of at least 60 days following the date of distribution of stock of the employer and, if the put option is not exercised within such 60-day period, for an additional period of at least 60 days in the following plan year (as provided in regulations promulgated by the Secretary).”

**SEC. 337. DISTRIBUTION OF EMPLOYER SECURITIES FROM A TAX CREDIT EMPLOYEE STOCK OWNERSHIP PLAN IN THE CASE OF A SALE OF EMPLOYER ASSETS OR STOCK.**

**(a) IN GENERAL.**—Section 409A(d) (relating to distribution of employer securities) is amended by striking out the last sentence thereof and inserting in lieu thereof the following: “To the extent provided in the plan, the preceding sentence shall not apply in the case of—

“(1) death, disability, or separation from service;

“(2) a transfer of a participant to the employment of an acquiring employer from the employment of the selling corporation in the case of—

“(A) a sale to the acquiring employer of substantially all of the assets used by the selling corporation in a trade or business conducted by the selling corporation, or

“(B) the sale of substantially all of the stock of a subsidiary of the employer, or

“(3) with respect to the stock of a selling corporation, a disposition of such selling corporation’s interest in a subsidiary when the participant continues employment with such subsidiary.”

**(b) EFFECTIVE DATE.**—The amendments made by this section shall apply to distributions described in section 409A(d) of the Internal Revenue Code of 1954 (or any corresponding provision of prior law) made after March 29, 1975.

**SEC. 338. PASS THROUGH OF VOTING RIGHTS ON EMPLOYER SECURITIES.**

**(a) IN GENERAL.**—Paragraph (22) of section 401(a) (relating to qualified pension, profit-sharing, and stock bonus plans) is amended to read as follows:

“(22) if a defined contribution plan (other than a profit-sharing plan)—

“(A) is established by an employer whose stock is not publicly traded, and

“(B) after acquiring securities of the employer, more than 10 percent of the total assets of the plan are securities of the employer,

any trust forming part of such plan shall not constitute a qualified trust under this section unless the plan meets the requirements of subsection (e) of section 409A.”

(b) **EFFECTIVE DATE.**—The amendment made by this section shall apply to acquisitions of securities after December 31, 1979.

**SEC. 339. EFFECTIVE DATE.**

Except as otherwise provided, the amendments made by this subtitle shall apply to taxable years beginning after December 31, 1981.

## **TITLE IV—ESTATE AND GIFT TAX PROVISIONS**

### **Subtitle A—Increase in Unified Credit; Rate Reduction; Unlimited Marital Deduction**

**SEC. 401. INCREASE IN UNIFIED CREDIT.**

(a) **CREDIT AGAINST ESTATE TAX.**—

(1) **IN GENERAL.**—Subsection (a) of section 2010 (relating to unified credit against estate tax) is amended by striking out “\$47,000” and inserting in lieu thereof “\$192,800”.

(2) **CONFORMING AMENDMENTS.**—

(A) Subsection (b) of section 2010 is amended to read as follows:

“(b) **PHASE-IN OF CREDIT.**—

“In the case of decedents dying in:

1982.....	\$62,800
1983.....	79,300
1984.....	96,300
1985.....	121,800
1986.....	155,800.”

Subsection (a) shall be applied by substituting for ‘\$192,800’ the following amount:

(B) Subsection (a) of section 6018 (relating to estate tax returns by executors) is amended—

(i) by striking out “\$175,000” in paragraph (1) and inserting in lieu thereof “\$600,000”; and

(ii) by striking out paragraph (3) and inserting in lieu thereof the following:

“(3) **PHASE-IN OF FILING REQUIREMENT AMOUNT.**—

“In the case of decedents dying in:

1982.....	\$225,000
1983.....	275,000
1984.....	325,000
1985.....	400,000
1986.....	500,000.”

Paragraph (1) shall be applied by substituting for ‘\$600,000’ the following amount:

**(b) CREDIT AGAINST GIFT TAX.—**

(1) **IN GENERAL.**—Paragraph (1) of section 2505(a) (relating to unified credit against gift tax) is amended by striking out “\$47,000” and inserting in lieu thereof “\$192,800”.

(2) **CONFORMING AMENDMENT.**—Subsection (b) of section 2505 is amended to read as follows:

**“(b) PHASE-IN OF CREDIT.—**

<b>“In the case of gifts made in:</b>	<b>Subsection (a)(1) shall be applied by substituting for ‘\$192,800’ the following amount:</b>
1982.....	\$62,800
1983.....	79,300
1984.....	96,300
1985.....	121,800
1986.....	155,800.”

**(c) EFFECTIVE DATES.—The amendments made—**

(1) by subsection (a) shall apply to the estates of decedents dying after December 31, 1981, and

(2) by subsection (b) shall apply to gifts made after such date.

**SEC. 402. REDUCTION IN MAXIMUM RATES OF TAX.**

(a) **50 PERCENT MAXIMUM RATE.**—Subsection (c) of section 2001 (relating to rate schedule) is amended by striking out the item beginning “Over \$2,500,000” and all that follows and inserting in lieu thereof the following new item:

“Over \$2,500,000..... \$1,025,800, plus 50% of the excess over \$2,500,000.”

(b) **PHASE-IN OF 50 PERCENT MAXIMUM RATE.**—Subsection (c) of section 2001 is amended—

(1) by striking out “(c) RATE SCHEDULE.—” and inserting in lieu thereof the following:

**“(c) RATE SCHEDULE.—**

“(1) **IN GENERAL.**—”, and

(2) by adding at the end thereof the following new paragraph:

**“(2) PHASE-IN OF 50 PERCENT MAXIMUM RATE.—**

“(A) **IN GENERAL.**—In the case of decedents dying, and gifts made, before 1985, there shall be substituted for the last item in the schedule contained in paragraph (1) the items determined under this paragraph.

“(B) **FOR 1982.**—In the case of decedents dying, and gifts made, in 1982, the substitution under this paragraph shall be as follows:

“Over \$2,500,000 but not over \$3,000,000.	\$1,025,800, plus 53% of the excess over \$2,500,000.
Over \$3,000,000 but not over \$3,500,000 ...	\$1,290,800, plus 57% of the excess over \$3,000,000.
Over \$3,500,000 but not over \$4,000,000 ...	\$1,575,800, plus 61% of the excess over \$3,500,000.
Over \$4,000,000.....	\$1,880,800, plus 65% of the excess over \$4,000,000.

“(C) **FOR 1983.**—In the case of decedents dying, and gifts made, in 1983, the substitution under this paragraph shall be as follows:

“Over \$2,500,000 but not over \$3,000,000.	\$1,025,800, plus 53% of the excess over \$2,500,000.
Over \$3,000,000 but not over \$3,500,000 ...	\$1,290,800, plus 57% of the excess over \$3,000,000.



Over \$3,500,000..... \$1,575,800, plus 60% of the excess over \$3,500,000.

**“(D) FOR 1984.—In the case of decedents dying, and gifts made, in 1984, the substitution under this paragraph shall be as follows:**

“Over \$2,500,000 but not over \$3,000,000. \$1,025,800, plus 53% of the excess over \$2,500,000.  
Over \$3,000,000..... \$1,290,800, plus 55% of the excess over \$3,000,000.”

**(c) ADJUSTMENT IN COMPUTATION OF TAX FOR GIFTS MADE AFTER DECEMBER 31, 1976.—Paragraph (2) of section 2001(b) is amended to read as follows:**

**“(2) the aggregate amount of tax which would have been payable under chapter 12 with respect to gifts made by the decedent after December 31, 1976, if the rate schedule set forth in subsection (c) (as in effect at the decedent’s death) had been applicable at the time of such gifts.”**

**(d) EFFECTIVE DATE.—The amendments made by this section shall apply to estates of decedents dying after, and gifts made after, December 31, 1981.**

#### **SEC. 403. UNLIMITED MARITAL DEDUCTION.**

##### **(a) ESTATE TAX DEDUCTION.—**

**(1) IN GENERAL.—Section 2056 (relating to bequests, etc., to surviving spouses) is amended—**

**(A) by striking out subsection (c) and redesignating subsection (d) as subsection (c); and**

**(B) by striking out “subsections (b) and (c)” in subsection (a) and inserting in lieu thereof “subsection (b)”.**

##### **(2) CONFORMING AMENDMENTS.—**

**(A) Paragraph (2) of section 2012(b) (relating to credit for gift tax) is amended to read as follows:**

**“(2) if a deduction with respect to such gift is allowed under section 2056(a) (relating to marital deduction), then by the amount of such value, reduced as provided in paragraph (1); and”.**

**(B) Paragraph (5) of section 2602(c) (relating to coordination with estate tax) is amended by striking out subparagraph (A) and redesignating subparagraphs (B) and (C) as subparagraphs (A) and (B), respectively.**

**(C) Subparagraph (A) of section 691(c)(3) (relating to special rules for generation-skipping transfers) is amended by striking out “section 2602(c)(5)(C)” and inserting in lieu thereof “section 2602(c)(5)(B)”.**

##### **(b) GIFT TAX DEDUCTION.—**

**(1) IN GENERAL.—Subsection (a) of section 2523 (relating to gift to spouse) is amended to read as follows:**

**“(a) ALLOWANCE OF DEDUCTION.—Where a donor who is a citizen or resident transfers during the calendar year by gift an interest in property to a donee who at the time of the gift is the donor’s spouse, there shall be allowed as a deduction in computing taxable gifts for the calendar year an amount with respect to such interest equal to its value.”**

**(2) TECHNICAL AMENDMENT.—Section 2523 is amended by striking out subsection (f).**

**(3) CONFORMING AMENDMENTS.—**

(A) So much of section 6019 (relating to gift tax returns) as follows the heading and precedes subsection (b) is amended to read as follows:

“Any individual who in any calendar year makes any transfer by gift other than—

“(1) a transfer which under subsection (b) or (e) of section 2503 is not to be included in the total amount of gifts for such year, or

“(2) a transfer of an interest with respect to which a deduction is allowed under section 2523, shall make a return for such year with respect to the gift tax imposed by subtitle B.”

(B) Paragraph (2) of section 2035(b) is amended by inserting “(other than by reason of section 6019(a)(2))” after “section 6019”.

**(c) ESTATE TAX ON PROPERTY HELD JOINTLY BY HUSBAND AND WIFE.**

(1) **IN GENERAL.**—Paragraph (2) of section 2040(b) (defining qualified joint interest) is amended to read as follows:

“(2) **QUALIFIED JOINT INTEREST DEFINED.**—For purposes of paragraph (1), the term ‘qualified joint interest’ means any interest in property held by the decedent and the decedent’s spouse as—

“(A) tenants by the entirety, or

“(B) joint tenants with right of survivorship, but only if the decedent and the spouse of the decedent are the only joint tenants.”

(2) **TECHNICAL AMENDMENT.**—Subsection (a) of section 2040 is amended by striking out “joint tenants” each place it appears and inserting in lieu thereof “joint tenants with right of survivorship”.

**(3) CONFORMING AMENDMENTS.—**

(A) Subsections (c), (d), and (e) of section 2040 are hereby repealed.

(B) Section 2515 (relating to tenancies by the entirety in real property), section 2515A (relating to tenancies by the entirety in personal property), and subsection (c) of section 6019 (relating to gift tax return) are hereby repealed.

(C) The table of sections for subchapter B of chapter 12 (relating to transfers) is amended by striking out the items relating to sections 2515 and 2515A.

**(d) ELECTION TO HAVE CERTAIN LIFE INTERESTS QUALIFY FOR MARITAL DEDUCTION.—**

(1) **ESTATE TAX.**—Subsection (b) of section 2056 is amended by adding at the end thereof the following new paragraphs:

“(7) **ELECTION WITH RESPECT TO LIFE ESTATE FOR SURVIVING SPOUSE.**—

“(A) **IN GENERAL.**—In the case of qualified terminable interest property—

“(i) for purposes of subsection (a), such property shall be treated as passing to the surviving spouse, and

“(ii) for purposes of paragraph (1)(A), no part of such property shall be treated as passing to any person other than the surviving spouse.

**“(B) QUALIFIED TERMINABLE INTEREST PROPERTY DEFINED.—**For purposes of this paragraph—

**“(i) IN GENERAL.—**The term ‘qualified terminable interest property’ means property—

**“(I) which passes from the decedent,**

**“(II) in which the surviving spouse has a qualifying income interest for life, and**

**“(III) to which an election under this paragraph applies.**

**“(ii) QUALIFYING INCOME INTEREST FOR LIFE.—**The surviving spouse has a qualifying income interest for life if—

**“(I) the surviving spouse is entitled to all the income from the property, payable annually or at more frequent intervals, and**

**“(II) no person has a power to appoint any part of the property to any person other than the surviving spouse.**

Subclause (II) shall not apply to a power exercisable only at or after the death of the surviving spouse.

**“(iii) PROPERTY INCLUDES INTEREST THEREIN.—**The term ‘property’ includes an interest in property.

**“(iv) SPECIFIC PORTION TREATED AS SEPARATE PROPERTY.—**A specific portion of property shall be treated as separate property.

**“(v) ELECTION.—**An election under this paragraph with respect to any property shall be made by the executor on the return of tax imposed by section 2001. Such an election, once made, shall be irrevocable.

**“(8) SPECIAL RULE FOR CHARITABLE REMAINDER TRUSTS.—**

**“(A) IN GENERAL.—**If the surviving spouse of the decedent is the only noncharitable beneficiary of a qualified charitable remainder trust, paragraph (1) shall not apply to any interest in such trust which passes or has passed from the decedent to such surviving spouse.

**“(B) DEFINITIONS.—**For purposes of subparagraph (A)—

**“(i) NONCHARITABLE BENEFICIARY.—**The term ‘noncharitable beneficiary’ means any beneficiary of the qualified charitable remainder trust other than an organization described in section 170(c).

**“(ii) QUALIFIED CHARITABLE REMAINDER TRUST.—**The term ‘qualified charitable remainder trust’ means a charitable remainder annuity trust or charitable remainder unitrust (described in section 664).”

**(2) GIFT TAX.—**Section 2523 is amended by adding at the end thereof the following new subsections:

**“(f) ELECTION WITH RESPECT TO LIFE ESTATE FOR DONEE SPOUSE.—**

**“(1) IN GENERAL.—**In the case of qualified terminable interest property—

**“(A) for purposes of subsection (a), such property shall be treated as transferred to the donee spouse, and**

**“(B) for purposes of subsection (b)(1), no part of such property shall be considered as retained in the donor or transferred to any person other than the donee spouse.**

**“(2) QUALIFIED TERMINABLE INTEREST PROPERTY.—**For purposes of this subsection, the term ‘qualified terminable interest property’ means any property—

“(A) which is transferred by the donor spouse,

“(B) in which the donee spouse has a qualifying income interest for life, and

“(C) to which an election under this subsection applies.

**“(3) CERTAIN RULES MADE APPLICABLE.—**For purposes of this subsection, the rules of clauses (ii), (iii), and (iv) of section 2056(b)(7)(B) shall apply.

**“(4) ELECTION.—**An election under this subsection with respect to any property shall be made on the return of the tax imposed by section 2501 for the calendar year in which the interest was transferred. Such an election, once made, shall be irrevocable.

**“(g) SPECIAL RULE FOR CHARITABLE REMAINDER TRUSTS.—**

**“(1) IN GENERAL.—**If, after the transfer, the donee spouse is the only noncharitable beneficiary (other than the donor) of a qualified remainder trust, subsection (b) shall not apply to the interest in such trust which is transferred to the donee spouse.

**“(2) DEFINITIONS.—**For purposes of paragraph (1), the term ‘noncharitable beneficiary’ and ‘qualified charitable remainder trust’ have the meanings given to such terms by section 2056(b)(8)(B).”

**(3) TREATMENT OF SPOUSE.—**

**(A) INCLUSION IN GROSS ESTATE.—**

**(i) IN GENERAL.—**Part III of subchapter A of chapter 11 is amended by redesignating sections 2044 and 2045 as sections 2045 and 2046, respectively, and by inserting after section 2043 the following new section:

**“SEC. 2044. CERTAIN PROPERTY FOR WHICH MARITAL DEDUCTION WAS PREVIOUSLY ALLOWED.**

**“(a) GENERAL RULE.—**The value of the gross estate shall include the value of any property to which this section applies in which the decedent had a qualifying income interest for life.

**“(b) PROPERTY TO WHICH THIS SECTION APPLIES.—**This section applies to any property if—

“(1) a deduction was allowed with respect to the transfer of such property to the decedent—

“(A) under section 2056 by reason of subsection (b)(7) thereof, or

“(B) under section 2523 by reason of subsection (f) thereof, and

“(2) section 2519 (relating to dispositions of certain life estates) did not apply with respect to a disposition by the decedent of part or all of such property.”

**(ii) The table of sections for part III of subchapter A of chapter 11 is amended by redesignating the items relating to sections 2044 and 2045 as sections 2045 and 2046, respectively, and by inserting after the item relating to section 2043 the following new item:**

**“Sec. 2044. Certain property for which marital deduction was previously allowed.”**

**(B) GIFT TAX.—**

(i) *IN GENERAL.*—Subchapter B of chapter 11 (relating to transfers) is amended by adding at the end thereof the following new section:

**“SEC. 2519. DISPOSITIONS OF CERTAIN LIFE ESTATES.**

“(a) *GENERAL RULE.*—Any disposition of all or part of a qualifying income interest for life in any property to which this section applies shall be treated as a transfer of such property.

“(b) *PROPERTY TO WHICH THIS SUBSECTION APPLIES.*—This section applies to any property if a deduction was allowed with respect to the transfer of such property to the donor—

“(1) under section 2056 by reason of subsection (b)(7) thereof,  
or

“(2) under section 2523 by reason of subsection (f) thereof.”

(ii) The table of sections for subchapter B of chapter 11 is amended by adding at the end thereof the following new item:

“Sec. 2519. Dispositions of certain life estates.”

(4)(A) Subchapter C of chapter 11 is amended by inserting after section 2207 the following new section:

**“SEC. 2207A. RIGHT OF RECOVERY IN THE CASE OF CERTAIN MARITAL DEDUCTION PROPERTY.**

“(a) *RECOVERY WITH RESPECT TO ESTATE TAX.*—

“(1) *IN GENERAL.*—If any part of the gross estate consists of property the value of which is includible in the gross estate by reason of section 2044 (relating to certain property for which marital deduction was previously allowed), the decedent’s estate shall be entitled to recover from the person receiving the property the amount by which—

“(A) the total tax under this chapter which has been paid, exceeds

“(B) the total tax under this chapter which would have been payable if the value of such property had not been included in the gross estate.

“(2) *DECEDENT MAY OTHERWISE DIRECT BY WILL.*—Paragraph (1) shall not apply if the decedent otherwise directs by will.

“(b) *RECOVERY WITH RESPECT TO GIFT TAX.*—If for any calendar year tax is paid under chapter 12 with respect to any person by reason of property treated as transferred by such person under section 2519, such person shall be entitled to recover from the person receiving the property the amount by which—

“(1) the total tax for such year under chapter 12, exceeds

“(2) the total tax which would have been payable under such chapter for such year if the value of such property had not been taken into account for purposes of chapter 12.

“(c) *MORE THAN ONE RECIPIENT OF PROPERTY.*—For purposes of this section, if there is more than one person receiving the property, the right of recovery shall be against each such person.

“(d) *TAXES AND INTEREST.*—In the case of penalties and interest attributable to additional taxes described in subsections (a) and (b), rules similar to subsections (a), (b), and (c) shall apply.”

(B) The table of sections for subchapter C of chapter 11 is amended by inserting after the item relating to section 2207 the following new item:

*"Sec. 2207A. Right of recovery in the case of certain marital deduction property."*

**(e) EFFECTIVE DATES.—**

(1) *Except as otherwise provided in this subsection, the amendments made by this section shall apply to the estates of decedents dying after December 31, 1981.*

(2) *The amendments made by paragraphs (1), (2), and (3)(A) of subsection (b), subparagraphs (B) and (C) of subsection (c)(3), and paragraphs (2) and (3)(B) of subsection (d) shall apply to gifts made after December 31, 1981.*

(3) *If—*

(A) *the decedent dies after December 31, 1981,*

(B) *by reason of the death of the decedent property passes from the decedent or is acquired from the decedent under a will executed before the date which is 30 days after the date of the enactment of this Act, or a trust created before such date, which contains a formula expressly providing that the spouse is to receive the maximum amount of property qualifying for the marital deduction allowable by Federal law,*

(C) *the formula referred to in subparagraph (B) was not amended to refer specifically to an unlimited marital deduction at any time after the date which is 30 days after the date of enactment of this Act, and before the death of the decedent, and*

(D) *the State does not enact a statute applicable to such estate which construes this type of formula as referring to the marital deduction allowable by Federal law as amended by subsection (a),*

*then the amendment made by subsection (a) shall not apply to the estate of such decedent.*

## **Subtitle B—Other Estate Tax Provisions**

### **SEC. 421. VALUATION OF CERTAIN FARM, ETC., REAL PROPERTY.**

**(a) INCREASE IN LIMITATION.—***Paragraph (2) of section 2032A(a) (relating to limitation) is amended to read as follows:*

*"(2) LIMIT ON AGGREGATE REDUCTION IN FAIR MARKET VALUE.—The aggregate decrease in the value of qualified real property taken into account for purposes of this chapter which results from the application of paragraph (1) with respect to any decedent shall not exceed the applicable limit set forth in the following table:*

<i>"In the case of decedents dying in:</i>	<i>The applicable limit is:</i>
<i>1981.....</i>	<i>\$600,000</i>
<i>1982.....</i>	<i>700,000</i>
<i>1983 or thereafter.....</i>	<i>750,000."</i>

**(b) DEFINITION OF QUALIFIED REAL PROPERTY.—**

(1) **REQUIRED USE CAN BE BY MEMBER OF FAMILY.—***Paragraph (1) of section 2032A(b) (defining qualified real property) is amended by inserting "by the decedent or a member of the decedent's family" after "qualified use" each place it appears.*

(2) **SPECIAL RULES FOR DECEDENTS WHO ARE RETIRED OR DISABLED AND FOR SURVIVING SPOUSES.**—Subsection (b) of section 2032A is amended by adding at the end thereof the following new paragraphs:

“(4) **DECEDENTS WHO ARE RETIRED OR DISABLED.**—

“(A) **IN GENERAL.**—If, on the date of the decedent’s death, the requirements of paragraph (1)(C)(ii) with respect to the decedent for any property are not met, and the decedent—

“(i) was receiving old-age benefits under title II of the Social Security Act for a continuous period ending on such date, or

“(ii) was disabled for a continuous period ending on such date,

then paragraph (1)(C)(ii) shall be applied with respect to such property by substituting ‘the date on which the longer of such continuous periods began’ for ‘the date of the decedent’s death’ in paragraph (1)(C).

“(B) **DISABLED DEFINED.**—For purposes of subparagraph (A), an individual shall be disabled if such individual has a mental or physical impairment which renders him unable to materially participate in the operation of the farm or other business.

“(C) **COORDINATION WITH RECAPTURE.**—For purposes of subsection (c)(6)(B)(i), if the requirements of paragraph (1)(C)(ii) are met with respect to any decedent by reason of subparagraph (A), the period ending on the date on which the continuous period taken into account under subparagraph (A) began shall be treated as the period immediately before the decedent’s death.

“(5) **SPECIAL RULES FOR SURVIVING SPOUSES.**—

“(A) **IN GENERAL.**—If property is qualified real property with respect to a decedent (hereinafter in this paragraph referred to as the ‘first decedent’) and such property was acquired from or passed from the first decedent to the surviving spouse of the first decedent, for purposes of applying this subsection and subsection (c) in the case of the estate of such surviving spouse, active management of the farm or other business by the surviving spouse shall be treated as material participation by such surviving spouse in the operation of such farm or business.

“(B) **SPECIAL RULE.**—For the purposes of subparagraph (A), the determination of whether property is qualified real property with respect to the first decedent shall be made without regard to subparagraph (D) of paragraph (1) and without regard to whether an election under this section was made.”

(c) **DISPOSITIONS AND FAILURES TO USE FOR QUALIFIED USE.**—

(1) **10-YEAR RECAPTURE PERIOD.**—

(A) **IN GENERAL.**—Paragraph (1) of section 2032A(c) (relating to tax treatment of dispositions and failures to use for qualified use) is amended by striking out “15 years” and inserting in lieu thereof “10 years”.

(B) **CONFORMING AMENDMENTS.**—

(i) Subsection (c) of section 2032A is amended by striking out paragraph (3) and redesignating para-

graphs (4) through (7) as paragraphs (3) through (6), respectively.

(ii) Subparagraph (A) of paragraph (2) of section 2032A(h) (relating to treatment of replacement property) is amended by striking out all that follows "involuntarily converted" and inserting in lieu thereof the following: "; except that with respect to such qualified replacement property the 10-year period under paragraph (1) of subsection (c) shall be extended by any period, beyond the 2-year period referred to in section 1033(a)(2)(B)(i), during which the qualified heir was allowed to replace the qualified real property,".

(iii) Subparagraph (C) of such paragraph (2) is amended by striking out "(7)" and inserting in lieu thereof "(6)".

**(2) CESSATION OF QUALIFIED USE.—**

**(A) IN GENERAL.—**Subsection (c) of section 2032A is amended by adding at the end thereof the following new paragraph:

**"(7) SPECIAL RULES.—**

**"(A) NO TAX IF USE BEGINS WITHIN 2 YEARS.—**If the date on which the qualified heir begins to use the qualified real property (hereinafter in this subparagraph referred to as the commencement date) is before the date 2 years after the decedent's death—

"(i) no tax shall be imposed under paragraph (1) by reason of the failure by the qualified heir to so use such property before the commencement date, and

"(ii) the 10-year period under paragraph (1) shall be extended by the period after the decedent's death and before the commencement date.

**"(B) ACTIVE MANAGEMENT BY ELIGIBLE QUALIFIED HEIR TREATED AS MATERIAL PARTICIPATION.—**For purposes of paragraph (6)(B)(ii), the active management of a farm or other business by—

"(i) an eligible qualified heir, or

"(ii) a fiduciary of an eligible qualified heir described in clause (ii) or (iii) of subparagraph (C),

shall be treated as material participation by such eligible qualified heir in the operation of such farm or business. In the case of an eligible qualified heir described in clause (ii), (iii), or (iv) of subparagraph (C), the preceding sentence shall apply only during periods during which such heir meets the requirements of such clause.

**"(C) ELIGIBLE QUALIFIED HEIR.—**For purposes of this paragraph, the term 'eligible qualified heir' means a qualified heir who—

"(i) is the surviving spouse of the decedent,

"(ii) has not attained the age of 21,

"(iii) is disabled (within the meaning of subsection (b)(4)(B)), or

"(iv) is a student.

**"(D) STUDENT.—**For purposes of subparagraph (C), an individual shall be treated as a student with respect to periods during any calendar year if (and only if) such individu-



*al is a student (within the meaning of section 151(e)(4)) for such calendar year."*

**(B) CONFORMING AMENDMENTS.—**

*(i) Subsection (e) of section 2032A (relating to definitions and special rules) is amended by adding at the end thereof the following new paragraph:*

*"(12) ACTIVE MANAGEMENT.—The term 'active management' means the making of the management decisions of a business (other than the daily operating decisions)."*

*(ii) Paragraph (6) of section 2032A(c) (as redesignated by paragraph (1)) is amended by striking out "3 years or more" and inserting in lieu thereof "more than 3 years".*

**(d) EXCHANGE OF QUALIFIED REAL PROPERTY.—**

*(1) IN GENERAL.—Section 2032A (relating to valuation of certain farm, etc., real property) is amended by adding at the end thereof the following new subsection:*

**"(i) EXCHANGES OF QUALIFIED REAL PROPERTY.—**

**"(1) TREATMENT OF PROPERTY EXCHANGED.—**

*"(A) EXCHANGES SOLELY FOR QUALIFIED EXCHANGE PROPERTY.—If an interest in qualified real property is exchanged solely for an interest in qualified exchange property in a transaction which qualifies under section 1031, no tax shall be imposed by subsection (c) by reason of such exchange.*

*"(B) EXCHANGES WHERE OTHER PROPERTY RECEIVED.—If an interest in qualified real property is exchanged for an interest in qualified exchange property and other property in a transaction which qualifies under section 1031, the amount of the tax imposed by subsection (c) by reason of such exchange shall be the amount of tax which (but for this subparagraph) would have been imposed on such exchange under subsection (c)(1), reduced by an amount which—*

*"(i) bears the same ratio to such tax, as*

*"(ii) the fair market value of the other property bears to the fair market value of the qualified real property exchanged.*

*For purposes of clause (ii) of the preceding sentence, fair market value shall be determined as of the time of the exchange.*

**"(2) TREATMENT OF QUALIFIED EXCHANGE PROPERTY.—For purposes of subsection (c)—**

*"(A) any interest in qualified exchange property shall be treated in the same manner as if it were a portion of the interest in qualified real property which was exchanged,*

*"(B) any tax imposed by subsection (c) by reason of the exchange shall be treated as a tax imposed on a partial disposition, and*

*"(C) paragraph (6) of subsection (c) shall be applied by treating material participation with respect to the exchanged property as material participation with respect to the qualified exchange property.*

**"(3) QUALIFIED EXCHANGE PROPERTY.—For purposes of this subsection, the term 'qualified exchange property' means real**

property which is to be used for the qualified use set forth in subparagraph (A), (B), or (C) of subsection (b)(2) under which the real property exchanged therefor originally qualified under subsection (a).”

**(2) CONFORMING AMENDMENTS.—**

(A) Paragraph (1) of section 2032A(f) (relating to statute of limitations) is amended—

(i) by inserting “or exchange” after “conversion”,

(ii) by inserting “or (i)” after “(h)”, and

(iii) by inserting “or of the exchange of property” after “replace”.

(B) Paragraph (2) of section 6324B(c) (relating to special liens) is amended by inserting “and qualified exchange property (within the meaning of section 2032A(i)(3))” before the period at the end thereof.

**(e) ELECTION REQUIREMENT OF SPECIAL RULES FOR INVOLUNTARY CONVERSIONS REPEALED.—**

(1) **IN GENERAL.**—Section 2032A(h) (relating to special rules for involuntary conversions of qualified real property) is amended—

(A) by striking out “and the qualified heir makes an election under this subsection” in paragraph (1)(A); and

(B) by striking out paragraph (5).

(2) **CONFORMING AMENDMENT.**—Paragraph (1) of section 2032A(f) is amended by striking out “to which an election under subsection (h)” and inserting in lieu thereof “to which subsection (h)”.

**(f) METHOD OF VALUING FARMS.—**

(1) Paragraph (7) of section 2032A(e) (relating to method of valuing farms) is amended by redesignating subparagraph (B) as subparagraph (C) and by inserting after subparagraph (A) the following new subparagraph:

“(B) **VALUE BASED ON NET SHARE RENTAL IN CERTAIN CASES.—**

“(i) **IN GENERAL.**—If there is no comparable land from which the average annual gross cash rental may be determined but there is comparable land from which the average net share rental may be determined, subparagraph (A)(i) shall be applied by substituting ‘average net share rental’ for ‘average gross cash rental’.

“(ii) **NET SHARE RENTAL.**—For purposes of this paragraph, the term ‘net share rental’ means the excess of—

“(I) the value of the produce received by the lessor of the land on which such produce is grown, over

“(II) the cash operating expenses of growing such produce which, under the lease, are paid by the lessor.”

(2) Subparagraph (C) of section 2032A(e)(7) (as redesignated by paragraph (1)) is amended by inserting after “determined” the following: “and that there is no comparable land from which the average net share rental may be determined”.

**(g) BASIS INCREASE WHERE RECAPTURE.**—Subsection (c) of section 1016 (relating to adjustments to basis) is amended to read as follows:

**“(c) INCREASE IN BASIS OF PROPERTY ON WHICH ADDITIONAL ESTATE TAX IS IMPOSED.—**

**“(1) TAX IMPOSED WITH RESPECT TO ENTIRE INTEREST.—**If an additional estate tax is imposed under section 2032A(c)(1) with respect to any interest in property and the qualified heir makes an election under this subsection with respect to the imposition of such tax, the adjusted basis of such interest shall be increased by an amount equal to the excess of—

**“(A) the fair market value of such interest on the date of the decedent’s death (or the alternate valuation date under section 2032, if the executor of the decedent’s estate elected the application of such section), over**

**“(B) the value of such interest determined under section 2032A(a).**

**“(2) PARTIAL DISPOSITIONS.—**

**“(A) IN GENERAL.—**In the case of any partial disposition for which an election under this subsection is made, the increase in basis under paragraph (1) shall be an amount—

**“(i) which bears the same ratio to the increase which would be determined under paragraph (1) (without regard to this paragraph) with respect to the entire interest, as**

**“(ii) the amount of the tax imposed under section 2032A(c)(1) with respect to such disposition bears to the adjusted tax difference attributable to the entire interest (as determined under section 2032A(c)(2)(B)).**

**“(B) PARTIAL DISPOSITION.—**For purposes of subparagraph (A), the term ‘partial disposition’ means any disposition or cessation to which subsection (c)(2)(D), (h)(1)(B), or (i)(1)(B) of section 2032A applies.

**“(3) TIME ADJUSTMENT MADE.—**Any increase in basis under this subsection shall be deemed to have occurred immediately before the disposition or cessation resulting in the imposition of the tax under section 2032A(c)(1).

**“(4) SPECIAL RULE IN THE CASE OF SUBSTITUTED PROPERTY.—**If the tax under section 2032A(c)(1) is imposed with respect to qualified replacement property (as defined in section 2032A(h)(3)(B)) or qualified exchange property (as defined in section 2032A(i)(3)), the increase in basis under paragraph (1) shall be made by reference to the property involuntarily converted or exchanged (as the case may be).

**“(5) ELECTION.—**

**“(A) IN GENERAL.—**An election under this subsection shall be made at such time and in such manner as the Secretary shall by regulations prescribe. Such an election, once made, shall be irrevocable.

**“(B) INTEREST ON RECAPTURED AMOUNT.—**If an election is made under this subsection with respect to any additional estate tax imposed under section 2032A(c)(1), for purposes of section 6601 (relating to interest on underpayments), the last date prescribed for payment of such tax shall be deemed to be the last date prescribed for payment of the tax

imposed by section 2001 with respect to the estate of the decedent (as determined for purposes of section 6601).”

**(h) SPECIAL RULES FOR WOODLANDS.—**

**(1) VALUE OF TIMBER INCLUDED IN VALUATION; ACTIVE MANAGEMENT TREATED AS MATERIAL PARTICIPATION.—**Subsection (e) of section 2032A is amended by adding at the end thereof the following new paragraph:

**“(13) SPECIAL RULES FOR WOODLANDS.—**

**“(A) IN GENERAL.—**In the case of any qualified woodland with respect to which the executor elects to have this subparagraph apply, trees growing on such woodland shall not be treated as a crop.

**“(B) QUALIFIED WOODLAND.—**The term ‘qualified woodland’ means any real property which—

“(i) is used in timber operations, and

“(ii) is an identifiable area of land such as an acre or other area for which records are normally maintained in conducting timber operations.

**“(C) TIMBER OPERATIONS.—**The term ‘timber operations’ means—

“(i) the planting, cultivating, caring for, or cutting of trees, or

“(ii) the preparation (other than milling) of trees for market.

**“(D) ELECTION.—**An election under subparagraph (A) shall be made on the return of the tax imposed by section 2001. Such election shall be made in such manner as the Secretary shall by regulations prescribe. Such an election, once made, shall be irrevocable.”

**(2) RECAPTURE UPON DISPOSITION OF TIMBER.—**Paragraph (2) of section 2032A(c) (relating to amount of additional tax) is amended by adding at the end thereof the following new subparagraph:

**“(E) SPECIAL RULE FOR DISPOSITION OF TIMBER.—**In the case of qualified woodland to which an election under subsection (e)(13)(A) applies, if the qualified heir disposes of (or severs) any standing timber on such qualified woodland—

“(i) such disposition (or severance) shall be treated as a disposition of a portion of the interest of the qualified heir in such property, and

“(ii) the amount of the additional tax imposed by paragraph (1) with respect to such disposition shall be an amount equal to the lesser of—

“(I) the amount realized on such disposition (or, in any case other than a sale or exchange at arm’s length, the fair market value of the portion of the interest disposed or severed), or

“(II) the amount of additional tax determined under this paragraph (without regard to this subparagraph) if the entire interest of the qualified heir in the qualified woodland had been disposed of, less the sum of the amount of the additional tax imposed with respect to all prior transactions involving such woodland to which this subparagraph applied.

*For purposes of the preceding sentence, the disposition of a right to sever shall be treated as the disposition of the standing timber. The amount of additional tax imposed under paragraph (1) in any case in which a qualified heir disposes of his entire interest in the qualified woodland shall be reduced by any amount determined under this subparagraph with respect to such woodland."*

(i) **DEFINITION OF FAMILY MEMBER.**—Paragraph (2) of section 2032A(e) (defining member of family) is amended to read as follows:

*"(2) MEMBER OF FAMILY.—The term 'member of the family' means, with respect to any individual, only—*

*"(A) an ancestor of such individual,*

*"(B) the spouse of such individual,*

*"(C) a lineal descendant of such individual, of such individual's spouse, or of a parent of such individual, or*

*"(D) the spouse of any lineal descendant described in subparagraph (C).*

*For purposes of the preceding sentence, a legally adopted child of an individual shall be treated as the child of such individual by blood."*

(j) **MISCELLANEOUS AMENDMENTS.**—

(1) **PROPERTY TRANSFERRED TO CERTAIN DISCRETIONARY TRUSTS.**—Subsection (g) of section 2032A (relating to application of section 2032A and section 6324B to interests in partnerships, corporations, and trusts) is amended by adding at the end thereof the following new sentence: *"For purposes of the preceding sentence, an interest in a discretionary trust all the beneficiaries of which are qualified heirs shall be treated as a present interest."*

(2) **PROPERTY PURCHASED FROM DECEDENT'S ESTATE ELIGIBLE FOR SPECIAL VALUATION.**—

(A) **IN GENERAL.**—Paragraph (9) of section 2032A(e) is amended by striking out subparagraphs (B) and (C) and inserting in lieu thereof the following:

*"(B) such property is acquired by any person from the estate, or*

*"(C) such property is acquired by any person from a trust (to the extent such property is includible in the gross estate of the decedent)."*

(B) **NONRECOGNITION OF GAIN.**—The section heading and subsections (a) and (b) of section 1040 are amended to read as follows:

**"SEC. 1040. TRANSFER OF CERTAIN FARM, ETC., REAL PROPERTY.**

*"(a) GENERAL RULE.—If the executor of the estate of any decedent transfers to a qualified heir (within the meaning of section 2032A(e)(1)) any property with respect to which an election was made under section 2032A, then gain on such transfer shall be recognized to the estate only to the extent that, on the date of such exchange, the fair market value of such property exceeds the value of such property for purposes of chapter 11 (determined without regard to section 2032A).*

*"(b) SIMILAR RULE FOR CERTAIN TRUSTS.—To the extent provided in regulations prescribed by the Secretary, a rule similar to the rule provided in subsection (a) shall apply where the trustee of a trust (any portion of which is included in the gross estate of the decedent)*

transfers property with respect to which an election was made under section 2032A.”

(C) **CLERICAL AMENDMENT.**—The table of sections for part III of subchapter O of chapter 1 is amended by striking out the item relating to section 1040 and inserting in lieu thereof the following:

“Sec. 1040. Transfer of certain farm, etc., real property.”

(3) **ELECTION MAY BE MADE ON LATE RETURNS.**—Paragraph (1) of section 2032A(d) (relating to election) is amended to read as follows:

“(1) **ELECTION.**—The election under this section shall be made on the return of the tax imposed by section 2001. Such election shall be made in such manner as the Secretary shall by regulations prescribe. Such an election, once made, shall be irrevocable.”

(4) **TREATMENT OF REPLACEMENT PROPERTY.**—Subsection (e) of section 2032A is amended by adding at the end thereof the following new paragraph:

“(14) **TREATMENT OF REPLACEMENT PROPERTY ACQUIRED IN SECTION 1031 OR 1033 TRANSACTIONS.**—

“(A) **IN GENERAL.**—In the case of any qualified replacement property, any period during which there was ownership, qualified use, or material participation with respect to the replaced property by the decedent or any member of his family shall be treated as a period during which there was such ownership, use, or material participation (as the case may be) with respect to the qualified replacement property.

“(B) **LIMITATION.**—Subparagraph (A) shall not apply to the extent that the fair market value of the qualified replacement property (as of the date of its acquisition) exceeds the fair market value of the replaced property (as of the date of its disposition).

“(C) **DEFINITIONS.**—For purposes of this paragraph—

“(i) **QUALIFIED REPLACEMENT PROPERTY.**—The term ‘qualified replacement property’ means any real property which is—

“(I) acquired in an exchange which qualifies under section 1031, or

“(II) the acquisition of which results in the non-recognition of gain under section 1033.

Such term shall only include property which is used for the same qualified use as the replaced property was being used before the exchange.

“(ii) **REPLACED PROPERTY.**—The term ‘replaced property’ means—

“(I) the property transferred in the exchange which qualifies under section 1031, or

“(II) the property compulsorily or involuntarily converted (within the meaning of section 1033).”

(k) **EFFECTIVE DATES.**—

(1) **IN GENERAL.**—Except as otherwise provided in this subsection, the amendments made by this section shall apply with respect to the estates of decedents dying after December 31, 1981.

(2) **INCREASE IN LIMITATION.**—The amendment made by subsection (a) shall apply with respect to the estates of decedents dying after December 31, 1980.

(3) **SUBSECTION (d).**—The amendments made by subsection (d) shall apply with respect to exchanges after December 31, 1981.

(4) **SUBSECTION (e).**—The amendments made by subsection (e) shall apply with respect to involuntary conversions after December 31, 1981.

(5) **CERTAIN AMENDMENTS MADE RETROACTIVE TO 1976.**—

(A) **IN GENERAL.**—The amendments made by subsections (b)(1), (c)(2), (j)(1), and (j)(2) shall apply with respect to the estates of decedents dying after December 31, 1976.

(B) **TIMELY ELECTION REQUIRED.**—Subparagraph (A) shall only apply in the case of an estate if a timely election under section 2032A was made with respect to such estate. If the time for making an election under section 2032A with respect to any estate would have otherwise expired after July 28, 1980, the time for making such election shall not expire before the date 6 months after the date of the enactment of this Act.

(C) **REINSTATEMENT OF ELECTIONS.**—If any election under section 2032A was revoked before the date of the enactment of this Act, such election may be reinstated within 6 months after the date of the enactment of this Act.

(D) **STATUTE OF LIMITATIONS.**—If on the date of the enactment of this Act (or at any time within 6 months after such date of enactment) the making of a credit or refund of any overpayment of tax resulting from the amendments described in subparagraph (A) is barred by any law or rule of law, such credit or refund shall nevertheless be made if claim therefor is made before the date 6 months after such date of enactment.

**SEC. 422. COORDINATION OF EXTENSIONS OF TIME FOR PAYMENT OF ESTATE TAX WHERE ESTATE CONSISTS LARGELY OF INTEREST IN CLOSELY HELD BUSINESS.**

(a) **ELIGIBILITY REQUIREMENTS.**—

(1) **IN GENERAL.**—Paragraph (1) of section 6166(a) (relating to alternate extension of time for payment of estate tax where estate consists largely of interest in closely held business) is amended by striking out “65 percent” and inserting in lieu thereof “35 percent”.

(2) **INTERESTS IN 2 OR MORE CLOSELY HELD BUSINESSES.**—Subsection (c) of section 6166 (relating to interests in 2 or more closely held businesses) is amended by striking out “more than 20 percent” and inserting in lieu thereof “20 percent or more”.

(b) **COORDINATION WITH SECTION 303.**—

(1) **IN GENERAL.**—Subparagraph (A) of section 303(b)(2) (relating to relationship of stock to decedent’s estate) is amended by striking out “50 percent” and inserting in lieu thereof “35 percent”.

(2) **CONFORMING AMENDMENT.**—Subparagraph (B) of section 303(b)(2) is amended to read as follows:

“(B) **SPECIAL RULE FOR STOCK IN 2 OR MORE CORPORATIONS.**—For purposes of subparagraph (A), stock of 2 or more corporations, with respect to each of which there is in-

cluded in determining the value of the decedent's gross estate 20 percent or more in value of the outstanding stock, shall be treated as the stock of a single corporation. For purposes of the 20-percent requirement of the preceding sentence, stock which, at the decedent's death, represents the surviving spouse's interest in property held by the decedent and the surviving spouse as community property or as joint tenants, tenants by the entirety, or tenants in common shall be treated as having been included in determining the value of the decedent's gross estate."

**(c) ACCELERATION OF PAYMENT.—**

**(1) AMOUNT OF DISPOSITION.—**Subparagraph (A) of section 6166(g)(1) (relating to acceleration of payment in the case of disposition of interest or withdrawal of funds from business) is amended to read as follows:

"(A) If—

"(i)(I) any portion of an interest in a closely held business which qualifies under subsection (a)(1) is distributed, sold, exchanged, or otherwise disposed of, or

"(II) money and other property attributable to such an interest is withdrawn from such trade or business, and

"(ii) the aggregate of such distributions, sales, exchanges, or other dispositions and withdrawals equals or exceeds 50 percent of the value of such interest,

then the extension of time for payment of tax provided in subsection (a) shall cease to apply, and the unpaid portion of the tax payable in installments shall be paid upon notice and demand from the Secretary."

**(2) FAILURE TO MAKE PAYMENTS.—**Paragraph (3) of section 6166(g) (relating to failure to pay installments) is amended to read as follows:

**"(3) FAILURE TO MAKE PAYMENT OF PRINCIPAL OR INTEREST.—**

"(A) **IN GENERAL.—**Except as provided in subparagraph (B), if any payment of principal or interest under this section is not paid on or before the date fixed for its payment by this section (including any extension of time), the unpaid portion of the tax payable in installments shall be paid upon notice and demand from the Secretary.

"(B) **PAYMENT WITHIN 6 MONTHS.—**If any payment of principal or interest under this section is not paid on or before the date determined under subparagraph (A) but is paid within 6 months of such date—

"(i) the provisions of subparagraph (A) shall not apply with respect to such payment,

"(ii) the provisions of section 6601(j) shall not apply with respect to the determination of interest on such payment, and

"(iii) there is imposed a penalty in an amount equal to the product of—

"(I) 5 percent of the amount of such payment, multiplied by

"(II) the number of months (or fractions thereof) after such date and before payment is made.



*The penalty imposed under clause (iii) shall be treated in the same manner as a penalty imposed under subchapter B of chapter 68.*"

**(3) NO DISQUALIFICATION IN CASE OF SUBSEQUENT DEATHS.—** Subparagraph (D) of section 6166(g)(1) is amended by adding at the end thereof the following new sentence: "A similar rule shall apply in the case of a series of subsequent transfers of the property by reason of death so long as each transfer is to a member of the family (within the meaning of section 267(c)(4)) of the transferor in such transfer."

**(d) REPEAL OF SECTION 6166A.—**Section 6166A (relating to extension of time for payment of estate tax where estate consists largely of interest in a closely held business) is hereby repealed.

**(e) TECHNICAL AMENDMENTS.—**

(1) Sections 303(b)(1)(C), 2204(c), and 6161(a)(2)(B) are each amended by striking out "or 6166A" each place it appears.

(2) Paragraph (2) of section 2011(c) is amended by striking out "6161, 6166 or 6166A" and inserting in lieu thereof "6161 or 6166".

(3) Subsections (a) and (b) of section 2204 are each amended by striking out "6166 or 6166A" and inserting in lieu thereof "or 6166".

(4) Subsection (b) of section 2621 is amended—

(A) by striking out "sections 6166 and 6166A (relating to extensions" and inserting in lieu thereof "section 6166 (relating to extension", and

(B) by striking out "SECTIONS 6166 AND 6166A" in the subsection heading and inserting in lieu thereof "SECTION 6166".

(5)(A) Subsection (a) of section 6166 is amended by striking out paragraph (4).

(B) The section heading for section 6166 is amended by striking out "ALTERNATE".

(C) The table of sections for subchapter B of chapter 62 is amended by striking out the items relating to sections 6166 and 6166A and inserting in lieu thereof the following:

*"Sec. 6166. Extension of time for payment of estate tax where estate consists largely of interest in closely held business."*

(6)(A) Subsections (a), (c)(2), and (e) of section 6324A are each amended by striking out "or 6166A" each place it appears.

(B) Paragraphs (3) and (5) of section 6324A(d) are each amended by striking out "or 6166A(h)".

(C) The section heading for section 6324A is amended by striking out "OR 6166A".

(D) The table of sections for subchapter C of chapter 64 is amended by striking out "or 6166A" in the item relating to section 6324A.

(7) Subsection (d) of section 6503 is amended by striking out "6163, 6166, or 6166A" and inserting in lieu thereof "6163 or 6166".

(8) Subsection (a) of section 7403 is amended by striking out "or 6166A(h)".

**(f) EFFECTIVE DATE.—**

(1) *IN GENERAL.*—Except as provided in paragraph (2), the amendments made by this section shall apply to the estates of decedents dying after December 31, 1981.

(2) *ACCELERATION BY REASON OF SUBSEQUENT DEATH.*—The amendment made by subsection (c)(3) shall apply to transfers after December 31, 1981.

**SEC. 423. TREATMENT OF CERTAIN CONTRIBUTIONS OF WORKS OF ART, ETC.**

(a) *ESTATE TAX.*—Subsection (e) of section 2055 (relating to disallowance of deduction in certain cases) is amended by adding at the end thereof the following new paragraph:

“(4) *WORKS OF ART AND THEIR COPYRIGHTS TREATED AS SEPARATE PROPERTIES IN CERTAIN CASES.*—

“(A) *IN GENERAL.*—In the case of a qualified contribution of a work of art, the work of art and the copyright on such work of art shall be treated as separate properties for purposes of paragraph (2).

“(B) *WORK OF ART DEFINED.*—For purposes of this paragraph, the term ‘work of art’ means any tangible personal property with respect to which there is a copyright under Federal law.

“(C) *QUALIFIED CONTRIBUTION DEFINED.*—For purposes of this paragraph, the term ‘qualified contribution’ means any transfer of property to a qualified organization if the use of the property by the organization is related to the purpose or function constituting the basis for its exemption under section 501.

“(D) *QUALIFIED ORGANIZATION DEFINED.*—For purposes of this paragraph, the term ‘qualified organization’ means any organization described in section 501(c)(3) other than a private foundation (as defined in section 509). For purposes of the preceding sentence, a private operating foundation (as defined in section 4942(j)(3)) shall not be treated as a private foundation.”

(b) *GIFT TAX.*—Subsection (c) of section 2522 is amended by adding at the end thereof the following new paragraph:

“(3) Rules similar to the rules of section 2055(e)(4) shall apply for purposes of paragraph (2).”

(c) *EFFECTIVE DATES.*—

(1) *SUBSECTION (a).*—The amendment made by subsection (a) shall apply to the estates of decedents dying after December 31, 1981.

(2) *SUBSECTION (b).*—The amendment made by subsection (b) shall apply to transfers after December 31, 1981.

**SEC. 424. GIFTS MADE WITHIN 3 YEARS OF DECEDENT'S DEATH NOT INCLUDED IN GROSS ESTATE.**

(a) *GENERAL RULE.*—Section 2035 (relating to adjustments for gifts made within 3 years of decedent's death) is amended by adding at the end thereof the following new subsection:

“(d) *DECEDENTS DYING AFTER 1981.*—

“(1) *IN GENERAL.*—Except as otherwise provided in this subsection, subsection (a) shall not apply to the estate of a decedent dying after December 31, 1981.

“(2) *EXCEPTIONS FOR CERTAIN TRANSFERS.*—Paragraph (1) shall not apply to a transfer of an interest in property which is

included in the value of the gross estate under section 2036, 2037, 2038, 2041, or 2042 or would have been included under any of such sections if such interest had been retained by the decedent.

**"(3) 3-YEAR RULE RETAINED FOR CERTAIN PURPOSES.—**Paragraph (1) shall not apply for purposes of—

**"(A) section 303(b) (relating to distributions in redemption of stock to pay death taxes),**

**"(B) section 2032A (relating to special valuation of certain farm, etc., real property),**

**"(C) section 6166 (relating to extension of time for payment of estate tax where estate consists largely of interest in closely held business), and**

**"(D) subchapter C of chapter 64 (relating to lien for taxes)."**

**(b) EFFECTIVE DATE.—**The amendment made by subsection (a) shall apply to the estates of decedents dying after December 31, 1981.

**SEC. 425. BASIS OF CERTAIN APPRECIATED PROPERTY TRANSFERRED TO DECEDENT BY GIFT WITHIN 1 YEAR OF DEATH.**

**(a) GENERAL RULE.—**Section 1014 (relating to basis of property acquired from a decedent) is amended by adding at the end thereof the following new subsection:

**"(e) APPRECIATED PROPERTY ACQUIRED BY DECEDENT BY GIFT WITHIN 1 YEAR OF DEATH.—**

**"(1) IN GENERAL.—**In the case of a decedent dying after December 31, 1981, if—

**"(A) appreciated property was acquired by the decedent by gift during the 1-year period ending on the date of the decedent's death, and**

**"(B) such property is acquired from the decedent by (or passes from the decedent to) the donor of such property (or the spouse of such donor),**

**the basis of such property in the hands of such donor (or spouse) shall be the adjusted basis of such property in the hands of the decedent immediately before the death of the decedent.**

**"(2) DEFINITIONS.—**For purposes of paragraph (1)—

**"(A) APPRECIATED PROPERTY.—**The term 'appreciated property' means any property if the fair market value of such property on the day it was transferred to the decedent by gift exceeds its adjusted basis.

**"(B) TREATMENT OF CERTAIN PROPERTY SOLD BY ESTATE.—**In the case of any appreciated property described in subparagraph (A) of paragraph (1) sold by the estate of the decedent or by a trust of which the decedent was the grantor, rules similar to the rules of paragraph (1) shall apply to the extent the donor of such property (or the spouse of such donor) is entitled to the proceeds from such sale."

**(b) EFFECTIVE DATE.—**The amendment made by subsection (a) shall apply to property acquired after the date of the enactment of this Act by decedents dying after December 31, 1981.

**SEC. 426. DISCLAIMERS.**

**(a) IN GENERAL.—**Subsection (c) of section 2518 (relating to disclaimers) is amended by adding at the end thereof the following new paragraph:

**“(3) CERTAIN TRANSFERS TREATED AS DISCLAIMERS.**—For purposes of subsection (a), a written transfer of the transferor’s entire interest in the property—

“(A) which meets requirements similar to the requirements of paragraphs (2) and (3) of subsection (b), and

“(B) which is to a person or persons who would have received the property had the transferor made a qualified disclaimer (within the meaning of subsection (b)),

shall be treated as a qualified disclaimer.”

(b) **EFFECTIVE DATE.**—The amendment made by subsection (a) shall apply to transfers creating an interest in the person disclaiming made after December 31, 1981.

**SEC. 427. REPEAL OF DEDUCTION FOR BEQUESTS, ETC., TO CERTAIN MINOR CHILDREN.**

(a) **IN GENERAL.**—Section 2057 (relating to bequests, etc., to certain minor children) is hereby repealed.

(b) **CLERICAL AMENDMENT.**—The table of sections for part IV of subchapter A of chapter 11 is amended by striking out the item relating to section 2057.

(c) **EFFECTIVE DATE.**—The amendments made by this section shall apply to estates of decedents dying after December 31, 1981.

**SEC. 428. POSTPONEMENT OF GENERATION-SKIPPING TAX EFFECTIVE DATE.**

Section 2006(c) of the Tax Reform Act of 1976 (relating to the effective dates of generation-skipping provisions), as amended by section 702(n)(1) of the Revenue Act of 1978 is amended by striking out “January 1, 1982” in paragraph (2)(B) of such section and inserting in lieu thereof “January 1, 1983”.

**SEC. 429. CREDIT AGAINST ESTATE TAX FOR TRANSFER TO SMITHSONIAN**

Upon transfer to the Smithsonian Institution, within thirty days following the date of the enactment of this Act, of all right, title, and interests held by the Dorothy Meserve Kunhardt trust and the estate of Dorothy Meserve Kunhardt in the collection of approximately seven thousand two hundred and fifty Mathew Brady glass plate negatives and the Alexander Gardner imperial portrait print of Abraham Lincoln, there shall be allowed as a credit, effective as of the date upon which the return was due to be filed, against the tax imposed by section 2001 (relating to the imposition of estate tax) on such estate an amount equal to the lesser of—

(1) such tax,

(2) the fair market value of such negatives and such print, or

(3) \$700,000.

### **Subtitle C—Other Gift Tax Provisions**

**SEC. 441. INCREASE IN ANNUAL GIFT TAX EXCLUSION; UNLIMITED EXCLUSION FOR CERTAIN TRANSFERS.**

(a) **INCREASE IN ANNUAL EXCLUSION.**—Subsection (b) of section 2503 (relating to annual gift tax exclusion) is amended by striking out “\$3,000” and inserting in lieu thereof “\$10,000”.

(b) **UNLIMITED EXCLUSION FOR CERTAIN TRANSFERS.**—Section 2503 (defining taxable gifts) is amended by adding at the end thereof the following new subsection:

“(e) **EXCLUSION FOR CERTAIN TRANSFERS FOR EDUCATIONAL EXPENSES OR MEDICAL EXPENSES.**—

*“(1) IN GENERAL.—Any qualified transfer shall not be treated as a transfer of property by gift for purposes of this chapter.*

*“(2) QUALIFIED TRANSFER.—For purposes of this subsection, the term ‘qualified transfer’ means any amount paid on behalf of an individual—*

*“(A) as tuition to an educational organization described in section 170(b)(1)(A)(ii) for the education or training of such individual, or*

*“(B) to any person who provides medical care (as defined in section 213(e)) with respect to such individual as payment for such medical care.”*

*(c) EFFECTIVE DATES.—*

*(1) IN GENERAL.—Except as provided in paragraph (2), the amendments made by this section shall apply to transfers after December 31, 1981.*

*(2) TRANSITIONAL RULE.—If—*

*(A) an instrument executed before the date which is 30 days after the date of the enactment of this Act provides for a power of appointment which may be exercised during any period after December 31, 1981,*

*(B) such power of appointment is expressly defined in terms of, or by reference to, the amount of the gift tax exclusion under section 2503(b) of the Internal Revenue Code of 1954 (or the corresponding provision of prior law),*

*(C) the instrument described in subparagraph (A) has not been amended on or after the date which is 30 days after the date of the enactment of this Act, and*

*(D) the State has not enacted a statute applicable to such gift under which such power of appointment is to be construed as being defined in terms of, or by reference to, the amount of the exclusion under such section 2503(b) after its amendment by subsection (a),*

*then the amendment made by subsection (a) shall not apply to such gift.*

#### **SEC. 442. TIME FOR PAYMENT OF GIFT TAXES.**

*(a) AMENDMENTS TO SUBCHAPTER A OF CHAPTER 12.—*

*(1) SECTION 2501.—Subsection (a) of section 2501 (relating to imposition of gift tax) is amended by striking out “calendar quarter” each place it appears and inserting in lieu thereof “calendar year”.*

*(2) SECTION 2502.—Section 2502 (relating to rate of tax) is amended to read as follows:*

#### **“SEC. 2502. RATE OF TAX.**

*“(a) COMPUTATION OF TAX.—The tax imposed by section 2501 for each calendar year shall be an amount equal to the excess of—*

*“(1) a tentative tax, computed in accordance with the rate schedule set forth in section 2001(c), on the aggregate sum of the taxable gifts for such calendar year and for each of the preceding calendar periods, over*

*“(2) a tentative tax, computed in accordance with such rate schedule, on the aggregate sum of the taxable gifts for each of the preceding calendar periods.*

*“(b) PRECEDING CALENDAR PERIOD.—Whenever used in this title in connection with the gift tax imposed by this chapter, the term ‘preceding calendar period’ means—*

“(1) calendar years 1932 and 1970 and all calendar years intervening between calendar year 1932 and calendar year 1970,

“(2) the first calendar quarter of calendar year 1971 and all calendar quarters intervening between such calendar quarter and the first calendar quarter of calendar year 1982, and

“(3) all calendar years after 1981 and before the calendar year for which the tax is being computed.

For purposes of paragraph (1), the term ‘calendar year 1932’ includes only that portion of such year after June 6, 1932.

“(c) **TAX TO BE PAID BY DONOR.**—The tax imposed by section 2501 shall be paid by the donor.”

(3) **SECTION 2503.**—

(A) Subsection (a) of section 2503 is amended to read as follows:

“(a) **GENERAL DEFINITION.**—The term ‘taxable gifts’ means the total amount of gifts made during the calendar year, less the deductions provided in subchapter C (section 2522 and following).”

(B) The first sentence of subsection (b) of section 2503 is amended to read as follows: “In the case of gifts (other than gifts of future interests in property) made to any person by the donor during the calendar year, the first \$10,000 of such gifts to such person shall not, for purposes of subsection (a), be included in the total amount of gifts made during such year.”

(4) **SECTION 2504.**—

(A) Subsection (a) of section 2504 is amended to read as follows:

“(a) **IN GENERAL.**—In computing taxable gifts for preceding calendar periods for purposes of computing the tax for any calendar year—

“(1) there shall be treated as gifts such transfers as were considered to be gifts under the gift tax laws applicable to the calendar period in which the transfers were made,

“(2) there shall be allowed such deductions as were provided for under such laws, and

“(3) the specific exemption in the amount (if any) allowable under section 2521 (as in effect before its repeal by the Tax Reform Act of 1976) shall be applied in all computations in respect of preceding calendar periods ending before January 1, 1977, for purposes of computing the tax for any calendar year.”

(B) Subsection (b) of section 2504 is amended—

(i) by striking out “preceding calendar years and calendar quarters” and inserting in lieu thereof “preceding calendar periods”,

(ii) by striking out “the years and calendar quarters” and inserting in lieu thereof “the periods”,

(iii) by striking out “such years and calendar quarters” and inserting in lieu thereof “such preceding calendar periods”, and

(iv) by striking out “PRECEDING YEARS AND QUARTERS” in the subsection heading and inserting in lieu thereof “PRECEDING CALENDAR PERIODS”.

(C) Subsection (c) of section 2504 is amended—

(i) by striking out "preceding calendar year or calendar quarter" each place it appears and inserting in lieu thereof "preceding calendar period",

(ii) by striking out "under this chapter for any calendar quarter" and inserting in lieu thereof "under this chapter for any calendar year",

(iii) by striking out "section 2502(c)" and inserting in lieu thereof "section 2502(b)", and

(iv) by striking out "PRECEDING CALENDAR YEARS AND QUARTERS" in the subsection heading and inserting in lieu thereof "PRECEDING CALENDAR PERIODS".

(D) The section heading for section 2504 is amended by striking out "PRECEDING YEARS AND QUARTERS" and inserting in lieu thereof "PRECEDING CALENDAR PERIODS".

(E) The table of sections for subchapter A of chapter 12 is amended by striking out "preceding years and quarters" in the item relating to section 2504 and inserting in lieu thereof "preceding calendar periods".

(5) SECTION 2505.—

(A) Subsection (a) of section 2505 is amended—

(i) by striking out "each calendar quarter" and inserting in lieu thereof "each calendar year", and

(ii) by striking out "preceding calendar quarters" and inserting in lieu thereof "preceding calendar periods".

(B) Subsection (d) of section 2505 is amended by striking out "calendar quarter" each place it appears and inserting in lieu thereof "calendar year".

(b) AMENDMENTS TO SUBCHAPTER B OF CHAPTER 12.—

(1) SECTION 2512.—Subsection (b) of section 2512 is amended by striking out "calendar quarter" and inserting in lieu thereof "calendar year".

(2) SECTION 2513.—

(A) Section 2513(a) is amended by striking out "calendar quarter" each place it appears and inserting in lieu thereof "calendar year".

(B) Paragraph (2) of section 2513(b) is amended by striking out "calendar quarter" in the matter preceding subparagraph (A) and inserting in lieu thereof "calendar year".

(C) Subparagraph (A) of subsection (b)(2) of section 2513 is amended to read as follows:

"(A) The consent may not be signified after the 15th day of April following the close of such year, unless before such 15th day no return has been filed for such year by either spouse, in which case the consent may not be signified after a return for such year is filed by either spouse."

(D) Subparagraph (B) of subsection (b)(2) of section 2513 is amended—

(i) by striking out "the consent" and inserting in lieu thereof "The consent", and

(ii) by striking out "such calendar quarter" and inserting in lieu thereof "such year".

(E) Subsection (c) of section 2513 is amended—

(i) by striking out "calendar quarter" and inserting in lieu thereof "calendar year", and

(ii) by striking out "15th day of the second month following the close of such quarter" and inserting in lieu "15th day of April following the close of such year".

(F) Subsection (d) of section 2513 is amended—

(i) by striking out "any calendar quarter" and inserting in lieu thereof "any calendar year", and

(ii) by striking out "such calendar quarter" and inserting in lieu thereof "such year".

(c) AMENDMENT TO SUBCHAPTER C OF CHAPTER 12.—Section 2522 is amended by striking out "quarter" each place it appears and inserting in lieu thereof "year".

(d) MISCELLANEOUS AMENDMENTS.—

(1) Paragraph (2) of subsection (d) of section 1015 (relating to increased basis for gift tax paid) is amended—

(A) by striking out "calendar quarter (or calendar year if the gift was made before January 1, 1971)" and inserting in lieu thereof "calendar year (or preceding calendar period)", and

(B) by striking out "calendar quarter or year" each place it appears and inserting in lieu thereof "calendar year or period".

(2) Section 6019 (relating to gift tax returns) is amended by striking out subsection (b).

(3) Subsection (b) of section 6075 (relating to time for filing gift tax returns) is amended to read as follows:

"(b) GIFT TAX RETURNS.—

"(1) GENERAL RULE.—Returns made under section 6019 (relating to gift taxes) shall be filed on or before the 15th day of April following the close of the calendar year.

"(2) EXTENSION WHERE TAXPAYER GRANTED EXTENSION FOR FILING INCOME TAX RETURN.—Any extension of time granted the taxpayer for filing the return of income taxes imposed by subtitle A for any taxable year which is a calendar year shall be deemed to be also an extension of time granted the taxpayer for filing the return under section 6019 for such calendar year.

"(3) COORDINATION WITH DUE DATE FOR ESTATE TAX RETURN.—Notwithstanding paragraphs (1) and (2), the time for filing the return made under section 6019 for the calendar year which includes the date of death of the donor shall not be later than the time (including extensions) for filing the return made under section 6018 (relating to estate tax returns) with respect to such donor."

(4) Paragraph (1) of section 6212(c) (relating to notice of deficiency) is amended by striking out "calendar quarter" and inserting in lieu thereof "calendar year".

(e) EFFECTIVE DATE.—The amendments made by this section shall apply with respect to gifts made after December 31, 1981.



## TITLE V—TAX STRADDLES

### SEC. 501. POSTPONEMENT OF RECOGNITION OF LOSSES, ETC.

(a) **GENERAL RULE.**—Part VII of subchapter O of chapter 1 (relating to wash sales of stock or securities) is amended by adding at the end thereof the following new section:

#### “SEC. 1092. STRADDLES.

“(a) **RECOGNITION OF LOSS IN CASE OF STRADDLES, ETC.**—

“(1) **LIMITATION ON RECOGNITION OF LOSS.**—

“(A) **IN GENERAL.**—Any loss with respect to 1 or more positions shall be taken into account for any taxable year only to the extent that the amount of such loss exceeds the unrealized gain (if any) with respect to 1 or more positions which—

“(i) were acquired by the taxpayer before the disposition giving rise to such loss,

“(ii) were offsetting positions with respect to the 1 or more positions from which the loss arose, and

“(iii) were not part of an identified straddle as of the close of the taxable year.

“(B) **CARRYOVER OF LOSS.**—Any loss which may not be taken into account under subparagraph (A) for any taxable year shall, subject to the limitations under subparagraph (A), be treated as sustained in the succeeding taxable year.

“(2) **SPECIAL RULE FOR IDENTIFIED STRADDLES.**—

“(A) **IN GENERAL.**—In the case of any straddle which is an identified straddle as of the close of any taxable year—

“(i) paragraph (1) shall not apply for such taxable year, and

“(ii) any loss with respect to such straddle shall be treated as sustained not earlier than the day on which all of the positions making up the straddle are disposed of.

“(B) **IDENTIFIED STRADDLE.**—The term ‘identified straddle’ means any straddle—

“(i) which is clearly identified on the taxpayer’s records, before the close of the day on which the straddle is acquired, as an identified straddle,

“(ii) all of the original positions of which (as identified by the taxpayer) are acquired on the same day and with respect to which—

“(I) all of such positions are disposed of on the same day during the taxable year, or

“(II) none of such positions has been disposed of as of the close of the taxable year, and

“(iii) which is not part of a larger straddle.

“(3) **UNREALIZED GAIN.**—For purposes of this subsection—

“(A) **IN GENERAL.**—The term ‘unrealized gain’ means the amount of gain which would be taken into account with respect to any position held by the taxpayer as of the close of the taxable year if such position were sold on the last business day of such taxable year at its fair market value.

“(B) **REPORTING OF GAIN.**—

**“(i) IN GENERAL.—**Each taxpayer shall disclose to the Secretary, at such time and in such manner and form as the Secretary may prescribe by regulations—

**“(I) each position (whether or not part of a straddle) which is held by such taxpayer as of the close of the taxable year and with respect to which there is unrealized gain, and**

**“(II) the amount of such unrealized gain.**

**“(ii) REPORTS NOT REQUIRED IN CERTAIN CASES.—**Clause (i) shall not apply—

**“(I) to any position which is part of an identified straddle,**

**“(II) to any position which, with respect to the taxpayer, is property described in paragraph (1) or (2) of section 1221 or to any position which is part of a hedging transaction (as defined in section 1256(e)), or**

**“(III) with respect to any taxable year if no loss on a position (including a regulated futures contract) has been sustained during such taxable year or if the only loss sustained on such position is a loss described in subclause (II).**

**“(b) CHARACTER OF GAIN OR LOSS; WASH SALES.—**Under regulations prescribed by the Secretary, in the case of gain or loss with respect to any position of a straddle, rules which are similar to the rules of subsections (a) and (d) of section 1091 and of subsections (b) and (d) of section 1233 and which are consistent with the purposes of this section shall apply.

**“(c) STRADDLE DEFINED.—**For purposes of this section—

**“(1) IN GENERAL.—**The term ‘straddle’ means offsetting positions with respect to personal property.

**“(2) OFFSETTING POSITIONS.—**

**“(A) IN GENERAL.—**A taxpayer holds offsetting positions with respect to personal property if there is a substantial diminution of the taxpayer’s risk of loss from holding any position with respect to personal property by reason of his holding 1 or more other positions with respect to personal property (whether or not of the same kind).

**“(B) ONE SIDE LARGER THAN OTHER SIDE.—**If 1 or more positions offset only a portion of 1 or more other positions, the Secretary shall by regulations prescribe the method for determining the portion of such other positions which is to be taken into account for purposes of this section.

**“(C) SPECIAL RULE FOR IDENTIFIED STRADDLES.—**In the case of any position which is not part of an identified straddle (within the meaning of subsection (a)(3)(B)), such position shall not be treated as offsetting with respect to any position which is part of an identified straddle.

**“(3) PRESUMPTION.—**

**“(A) IN GENERAL.—**For purposes of paragraph (2), 2 or more positions shall be presumed to be offsetting if—

**“(i) the positions are in the same personal property (whether established in such property or a contract for such property),**

“(ii) the positions are in the same personal property, even though such property may be in a substantially altered form,

“(iii) the positions are in debt instruments of a similar maturity or other debt instruments described in regulations prescribed by the Secretary,

“(iv) the positions are sold or marketed as offsetting positions (whether or not such positions are called a straddle, spread, butterfly, or any similar name),

“(v) the aggregate margin requirement for such positions is lower than the sum of the margin requirements for each such position (if held separately), or

“(vi) there are such other factors (or satisfaction of subjective or objective tests) as the Secretary may by regulations prescribe as indicating that such positions are offsetting.

For purposes of the preceding sentence, 2 or more positions shall be treated as described in clause (i), (ii), (iii), or (vi) only if the value of 1 or more of such positions ordinarily varies inversely with the value of 1 or more other such positions.

“(B) PRESUMPTION MAY BE REBUTTED.—Any presumption established pursuant to subparagraph (A) may be rebutted.

“(d) DEFINITIONS AND SPECIAL RULES.—For purposes of this section—

“(1) PERSONAL PROPERTY.—The term ‘personal property’ means any personal property (other than stock) of a type which is actively traded.

“(2) POSITION.—

“(A) IN GENERAL.—The term ‘position’ means an interest (including a futures or forward contract or option) in personal property.

“(B) SPECIAL RULE FOR STOCK OPTIONS.—The term ‘position’ includes any stock option which is a part of a straddle and which is an option to buy or sell stock which is actively traded, but does not include a stock option which—

“(i) is traded on a domestic exchange or on a similar foreign exchange designated by the Secretary, and

“(ii) is of a type with respect to which the maximum period during which such option may be exercised is less than the minimum period for which a capital asset must be held for gain to be treated as long-term capital gain under section 1222(3).

“(3) POSITIONS HELD BY RELATED PERSONS, ETC.—

“(A) IN GENERAL.—In determining whether 2 or more positions are offsetting, the taxpayer shall be treated as holding any position held by a related person.

“(B) RELATED PERSON.—For purposes of subparagraph (A), a person is a related person to the taxpayer if with respect to any period during which a position is held by such person, such person—

“(i) is the spouse of the taxpayer, or

“(ii) files a consolidated return (within the meaning of section 1501) with the taxpayer for any taxable year which includes a portion of such period.

**“(C) CERTAIN FLOWTHROUGH ENTITIES.**—If part or all of the gain or loss with respect to a position held by a partnership, trust, or other entity would properly be taken into account for purposes of this chapter by a taxpayer, then, except to the extent otherwise provided in regulations, such position shall be treated as held by the taxpayer.

**“(4) SPECIAL RULE FOR REGULATED FUTURES CONTRACTS.**—In the case of a straddle—

“(A) at least 1 (but not all) of the positions of which are regulated futures contracts, and

“(B) with respect to which the taxpayer has elected not to have the provisions of section 1256 apply, the provisions of this section shall apply to any regulated futures contract and any other position making up such straddle.

**“(5) REGULATED FUTURES CONTRACT.**—The term ‘regulated futures contract’ has the same meaning given such term by section 1256(b).

**“(e) EXCEPTION FOR HEDGING TRANSACTIONS.**—This section shall not apply in the case of any hedging transaction (as defined in section 1256(e)).

**“(f) CROSS REFERENCE.**—

“For provision requiring capitalization of certain interest and carrying charges where there is a straddle, see section 263(g).”

**(b) PENALTY FOR FAILURE TO DISCLOSE.**—Section 6653 (relating to failure to pay tax) is amended by adding at the end thereof the following new subsection:

**“(g) SPECIAL RULE IN CASES OF FAILURE TO REPORT UNREALIZED GAIN ON POSITION IN PERSONAL PROPERTY.**—If—

“(1) a taxpayer fails to make the report required under section 1092(a)(3)(B) in the manner prescribed by such section and such failure is not due to reasonable cause, and

“(2) such taxpayer has an underpayment of any tax attributable (in whole or in part) to the denial of a deduction of a loss with respect to any position (within the meaning of section 1092(d)(2)),

then such underpayment shall, for purposes of subsection (a), be treated as an underpayment due to negligence or intentional disregard of rules and regulations (but without intent to defraud).”

**(c) APPLICATION WITH SECTION 1233.**—Paragraph (2) of section 1233(e) (defining property to which section applies) is amended by inserting “, but does not include any position to which section 1092(b) applies” after “taxpayer” in subparagraph (A).

**(d) CLERICAL AMENDMENTS.**—

(1) The table of sections for such part VII is amended by adding at the end thereof the following new item:

“Sec. 1092. Straddles.”

(2) The heading for such part VII is amended to read as follows:

**“PART VII—WASH SALES; STRADDLES”.**

(3) The table of parts for subchapter O of chapter 1 is amended by striking out the item relating to part VII and inserting in lieu thereof the following:

“Part VII. Wash sales; straddles.”

**SEC. 502. CAPITALIZATION OF CERTAIN INTEREST AND CARRYING CHARGES IN THE CASE OF STRADDLES.**

Section 263 (relating to capital expenditures) is amended by adding at the end thereof the following new subsection:

**“(g) CERTAIN INTEREST AND CARRYING COSTS IN THE CASE OF STRADDLES.—**

**“(1) GENERAL RULE.—**No deduction shall be allowed for interest and carrying charges properly allocable to personal property which is part of a straddle (as defined in section 1092(c)). Any amount not allowed as a deduction by reason of the preceding sentence shall be chargeable to the capital account with respect to the personal property to which such amount relates.

**“(2) INTEREST AND CARRYING CHARGES DEFINED.—**For purposes of paragraph (1), the term ‘interest and carrying charges’ means the excess of—

**“(A) the sum of—**

**“(i) interest on indebtedness incurred or continued to purchase or carry the personal property, and**

**“(ii) amounts paid or incurred to insure, store, or transport the personal property, over**

**“(B) the sum of—**

**“(i) the amount of interest (including original issue discount) includible in gross income for the taxable year with respect to the property described in subparagraph (A), and**

**“(ii) any amount treated as ordinary income under section 1232(a)(4)(A) with respect to such property for the taxable year.**

**“(3) EXCEPTION FOR HEDGING TRANSACTIONS.—**This subsection shall not apply in the case of any hedging transaction (as defined in section 1256(e)).”

**SEC. 503. REGULATED FUTURES CONTRACTS MARKED TO MARKET.**

**(a) GENERAL RULE.—**Part IV of subchapter P of chapter 1 (relating to special rules for determining capital gains and losses) is amended by adding at the end thereof the following new section:

**“SEC. 1256. REGULATED FUTURES CONTRACTS MARKED TO MARKET.**

**“(a) GENERAL RULE.—**For purposes of this subtitle—

**“(1) each regulated futures contract held by the taxpayer at the close of the taxable year shall be treated as sold for its fair market value on the last business day of such taxable year (and any gain or loss shall be taken into account for the taxable year),**

**“(2) proper adjustment shall be made in the amount of any gain or loss subsequently realized for gain or loss taken into account by reason of paragraph (1),**

**“(3) any gain or loss with respect to a regulated futures contract shall be treated as—**

**“(A) short-term capital gain or loss, to the extent of 40 percent of such gain or loss, and**

**“(B) long-term capital gain or loss, to the extent of 60 percent of such gain or loss, and**

**“(4) if all the offsetting positions making up any straddle consist of regulated futures contracts to which this section applies (and such straddle is not part of a larger straddle), sections 1092 and 263(g) shall not apply with respect to such straddle.**

**“(b) REGULATED FUTURES CONTRACTS DEFINED.**—For purposes of this section, the term ‘regulated futures contract’ means a contract—

“(1) which requires delivery of personal property (as defined in section 1092(d)(1)) or an interest in such property;

“(2) with respect to which the amount required to be deposited and the amount which may be withdrawn depends on a system of marking to market; and

“(3) which is traded on or subject to the rules of a domestic board of trade designated as a contract market by the Commodity Futures Trading Commission or of any board of trade or exchange which the Secretary determines has rules adequate to carry out the purposes of this section.

**“(c) TERMINATIONS.**—The rules of paragraphs (1), (2), and (3) of subsection (a) shall also apply to the termination during the taxable year of the taxpayer’s obligation with respect to a regulated futures contract by offsetting, by taking or making delivery, or otherwise. For purposes of the preceding sentence, fair market value at the time of the termination shall be taken into account.

**“(d) ELECTIONS WITH RESPECT TO MIXED STRADDLES.**—

“(1) **ELECTION.**—The taxpayer may elect to have this section not to apply to all regulated futures contracts which are part of a mixed straddle.

“(2) **TIME AND MANNER.**—An election under paragraph (1) shall be made at such time and in such manner as the Secretary may by regulations prescribe.

“(3) **ELECTION REVOCABLE ONLY WITH CONSENT.**—An election under paragraph (1) shall apply to the taxpayer’s taxable year for which made and to all subsequent taxable years, unless the Secretary consents to a revocation of such election.

“(4) **MIXED STRADDLE.**—For purposes of this subsection, the term ‘mixed straddle’ means any straddle (as defined in section 1092(c))—

“(A) at least 1 (but not all) of the positions of which are regulated futures contracts, and

“(B) with respect to which each position forming part of such straddle is clearly identified, before the close of the day on which such position is acquired, as being part of such straddle.

**“(e) MARK TO MARKET NOT TO APPLY TO HEDGING TRANSACTIONS.**—

“(1) **SECTION NOT TO APPLY.**—Subsection (a) shall not apply in the case of a hedging transaction.

“(2) **DEFINITION OF HEDGING TRANSACTION.**—For purposes of this subsection, the term ‘hedging transaction’ means any transaction if—

“(A) such transaction is entered into by the taxpayer in the normal course of the taxpayer’s trade or business primarily—

“(i) to reduce risk of price change or currency fluctuations with respect to property which is held or to be held by the taxpayer, or

“(ii) to reduce risk of interest rate or price changes or currency fluctuations with respect to borrowings made or to be made, or obligations incurred or to be incurred, by the taxpayer,

“(B) the gain or loss on such transactions is treated as ordinary income or loss, and

“(C) before the close of the day on which such transaction was entered into, the taxpayer clearly identifies such transaction as being a hedging transaction.

“(3) SPECIAL RULE FOR SYNDICATES.—

“(A) IN GENERAL.—Notwithstanding paragraph (2), the term ‘hedging transaction’ shall not include any transaction entered into by or for a syndicate.

“(B) SYNDICATE DEFINED.—For purposes of subparagraph (A), the term ‘syndicate’ means any partnership or other entity (other than a corporation which is not an electing small business corporation within the meaning of section 1371(b)) if more than 35 percent of the losses of such entity during the taxable year are allocable to limited partners or limited entrepreneurs (within the meaning of section 464(e)(2)).

“(C) HOLDINGS ATTRIBUTABLE TO ACTIVE MANAGEMENT.—For purposes of subparagraph (B), an interest in an entity shall not be treated as held by a limited partner or a limited entrepreneur (within the meaning of section 464(e)(2))—

“(i) for any period if during such period such interest is held by an individual who actively participates at all times during such period in the management of such entity,

“(ii) for any period if during such period such interest is held by the spouse, children, grandchildren, and parents of an individual who actively participates at all times during such period in the management of such entity,

“(iii) if such interest is held by an individual who actively participated in the management of such entity for a period of not less than 5 years,

“(iv) if such interest is held by the estate of an individual who actively participated in the management of such entity or is held by the estate of an individual if with respect to such individual such interest was at any time described in clause (ii), or

“(v) if the Secretary determines that such interest should be treated as held by an individual who actively participates in the management of such entity, and that such entity and such interest are not used (or to be used) for tax-avoidance purposes.

For purposes of this subparagraph, a legally adopted child of an individual shall be treated as a child of such individual by blood.

“(4) SPECIAL RULE FOR BANKS.—In the case of a bank (as defined in section 581), subparagraph (A) of paragraph (2) shall be applied without regard to clause (i) or (ii) thereof.

“(f) SPECIAL RULES.—

“(1) DENIAL OF CAPITAL GAINS TREATMENT FOR PROPERTY IDENTIFIED AS PART OF A HEDGING TRANSACTION.—For purposes of this title, gain from any property shall in no event be considered as gain from the sale or exchange of a capital asset if such property was at any time personal property (as defined in sec-

tion 1092(d)(1)) identified under subsection (e)(2)(C) by the taxpayer as being part of a hedging transaction.

“(2) **SUBSECTION (A)(3) NOT TO APPLY TO ORDINARY INCOME PROPERTY.**—Paragraph (3) of subsection (a) shall not apply to any gain or loss which, but for such paragraph, would be ordinary income or loss.”

(b) **CLERICAL AMENDMENT.**—The table of sections for part IV of subchapter P of chapter 1 is amended by adding at the end thereof the following new item:

“Sec. 1256. Regulated futures contracts marked to market.”

**SEC. 504. CARRYBACK OF LOSSES FROM REGULATED FUTURES CONTRACTS TO OFFSET PRIOR GAINS FROM SUCH CONTRACTS.**

Section 1212 (relating to capital loss carrybacks and carryovers) is amended by adding at the end thereof the following new subsection:

“(c) **CARRYBACK OF LOSSES FROM REGULATED FUTURES CONTRACTS TO OFFSET PRIOR GAINS FROM SUCH CONTRACTS.**—

“(1) **IN GENERAL.**—If a taxpayer (other than a corporation) has a net commodity futures loss for the taxable year and elects to have this subsection apply to such taxable year, the amount of such net commodity futures loss—

“(A) shall be a carryback to each of the 3 taxable years preceding the loss year, and

“(B) to the extent that, after the application of paragraphs (2) and (3), such loss is allowed as a carryback to any such preceding taxable year—

“(i) 40 percent of the amount so allowed shall be treated as a short-term capital loss from regulated futures contracts, and

“(ii) 60 percent of the amount so allowed shall be treated as a long-term capital loss from regulated futures contracts.

“(2) **AMOUNT CARRIED TO EACH TAXABLE YEAR.**—The entire amount of the net commodity futures loss for any taxable year shall be carried to the earliest of the taxable years to which such loss may be carried back under paragraph (1). The portion of such loss which shall be carried to each of the 2 other taxable years to which such loss may be carried back shall be the excess (if any) of such loss over the portion of such loss which, after the application of paragraph (3), was allowed as a carryback for any prior taxable year.

“(3) **AMOUNT WHICH MAY BE USED IN ANY PRIOR TAXABLE YEAR.**—An amount shall be allowed as a carryback under paragraph (1) to any prior taxable year only to the extent—

“(A) such amount does not exceed the net commodity futures gain for such year, and

“(B) the allowance of such carryback does not increase or produce a net operating loss (as defined in section 172(c)) for such year.

“(4) **NET COMMODITY FUTURES LOSS.**—For purposes of paragraph (1), the term ‘net commodity futures loss’ means the lesser of—

“(A) the net capital loss for the taxable year determined by taking into account only gains and losses from regulated futures contracts and positions to which section 1256 applies, or



“(B) the sum of the amounts which, but for paragraph (6)(A), would be treated as capital losses in the succeeding taxable year under subparagraphs (A) and (B) of subsection (b)(1).

“(5) NET COMMODITY FUTURES GAIN.—For purposes of paragraph (1)—

“(A) IN GENERAL.—The term ‘net commodity futures gain’ means the lesser of—

“(i) the capital gain net income for the taxable year determined by taking into account only gains and losses from regulated futures contracts, or

“(ii) the capital gain net income for the taxable year.

“(B) SPECIAL RULE.—The net commodity futures gain for any taxable year before the loss year shall be computed without regard to the net commodity futures loss for the loss year or for any taxable year thereafter.

“(6) COORDINATION WITH CARRYFORWARD PROVISIONS OF SUBSECTION (b)(1).—

“(A) CARRYFORWARD AMOUNT REDUCED BY AMOUNT USED AS CARRYBACK.—For purposes of applying subsection (b)(1), if any portion of the net commodity futures loss for any taxable year is allowed as a carryback under paragraph (1) to any preceding taxable year—

“(i) 40 percent of the amount allowed as a carryback shall be treated as a short-term capital gain for the loss year, and

“(ii) 60 percent of the amount allowed as a carryback shall be treated as a long-term capital gain for the loss year.

“(B) CARRYOVER LOSS RETAINS CHARACTER AS ATTRIBUTABLE TO REGULATED FUTURES CONTRACT.—Any amount carried forward as a short-term or long-term capital loss to any taxable year under subsection (b)(1) (after the application of subparagraph (A)) shall, to the extent attributable to losses from regulated futures contracts, be treated as loss from regulated futures contracts for such taxable year.

“(7) OTHER DEFINITIONS AND SPECIAL RULES.—For purposes of this subsection—

“(A) REGULATED FUTURES CONTRACT.—The term ‘regulated futures contract’ means any regulated futures contract (as defined in section 1256(b)) to which section 1256 applies.

“(B) EXCLUSION FOR ESTATES AND TRUSTS.—This subsection shall not apply to any estate or trust.”

**SEC. 505. CERTAIN GOVERNMENTAL OBLIGATIONS ISSUED AT DISCOUNT TREATED AS CAPITAL ASSETS.**

(a) GENERAL RULE.—Section 1221 (defining capital asset) is amended by striking out paragraph (5) and by redesignating paragraph (6) as paragraph (5).

(b) TREATMENT OF AMOUNTS RECEIVED ON SALE OR OTHER DISPOSITION.—Subsection (a) of section 1232 (relating to bonds and other evidences of indebtedness) is amended by adding at the end thereof the following new paragraph:

“(4) CERTAIN SHORT-TERM GOVERNMENT OBLIGATIONS.—

“(A) IN GENERAL.—On the sale or exchange of any short-term Government obligation, any gain realized which does

not exceed an amount equal to the ratable share of the acquisition discount shall be treated as ordinary income. Gain in excess of such amount shall be considered gain from the sale or exchange of a capital asset held less than a year.

“(B) **SHORT-TERM GOVERNMENT OBLIGATION.**—For purposes of this paragraph, the term ‘short-term Government obligation’ means any obligation of the United States or any of its possessions, or of a State or any political subdivision thereof, or of the District of Columbia which is issued on a discount basis and payable without interest at a fixed maturity date not exceeding 1 year from the date of issue. Such term does not include any obligation the interest on which is not includible in gross income under section 109 (relating to certain governmental obligations).

“(C) **ACQUISITION DISCOUNT.**—For purposes of this paragraph, the term ‘acquisition discount’ means the excess of the stated redemption price at maturity over the taxpayer’s basis for the obligation.

“(D) **RATABLE SHARE.**—For purposes of this paragraph the ratable share of the acquisition discount is an amount which bears the same ratio to such discount as—

“(i) the number of days which the taxpayer held the obligation, bears to

“(ii) the number of days after the date the taxpayer acquired the obligation and up to (and including) the date of its maturity.”

**(c) TECHNICAL AMENDMENTS.—**

(1) Subparagraph (D) of section 1231(b)(1) is amended by striking out “paragraph (6)” and inserting in lieu thereof “paragraph (5)”.

(2) Subparagraph (B) of section 341(c)(2) is amended by striking out “(and governmental obligations described in section 1221(5))”.

**SEC. 506. PROMPT IDENTIFICATION OF SECURITIES BY DEALERS IN SECURITIES.**

**(a) IN GENERAL.**—Subsection (a) of section 1236 (relating to dealers in securities) is amended—

(1) by striking out “before the expiration of the 30th day after the date of its acquisition” and inserting in lieu thereof “before the close of the day on which it was acquired (before the close of the following day in the case of an acquisition before January 1, 1982)”, and

(2) by striking out “expiration of such 30th day” and inserting in lieu thereof “close of such day”.

**(b) SPECIAL RULE FOR FLOOR SPECIALISTS.**—Section 1236 (relating to dealers in securities) is amended by adding at the end thereof the following new subsection:

“(d) **SPECIAL RULE FOR FLOOR SPECIALISTS.**—

“(1) **IN GENERAL.**—In the case of a floor specialist (but only with respect to acquisitions, in connection with his duties on an exchange, of stock in which the specialist is registered with the exchange), subsection (a) shall be applied—

“(A) by inserting ‘the 7th business day following’ before ‘the day’ the first place it appears in paragraph (1) and by inserting ‘7th business’ before ‘day’ in paragraph (2), and

“(B) by striking the parenthetical phrase in paragraph (1).

“(2) **FLOOR SPECIALIST.**—The term ‘floor specialist’ means a person who is—

“(A) a member of a national securities exchange,

“(B) is registered as a specialist with the exchange, and

“(C) meets the requirements for specialists established by the Securities and Exchange Commission.”

**SEC. 507. TREATMENT OF GAIN OR LOSS FROM CERTAIN TERMINATIONS.**

(a) **GENERAL RULE.**—Part IV of subchapter P of chapter 1 (relating to special rules for determining capital gains and losses) is amended by inserting after section 1234 the following new section:

**“SEC. 1234A. GAINS OR LOSSES FROM CERTAIN TERMINATIONS.**

“Gain or loss attributable to the cancellation, lapse, expiration, or other termination of a right or obligation with respect to personal property (as defined in section 1092(d)(1)) which is (or on acquisition would be) a capital asset in the hands of the taxpayer shall be treated as gain or loss from the sale of a capital asset.”

(b) **CLERICAL AMENDMENT.**—The table of sections for part IV of subchapter P of chapter 1 is amended by inserting after the item relating to section 1234 the following new item:

“Sec. 1234A. Gains or losses from certain terminations.”

**SEC. 508. EFFECTIVE DATES.**

(a) **IN GENERAL.**—Except as otherwise provided in this section, the amendments made by this title shall apply to property acquired and positions established by the taxpayer after June 23, 1981, in taxable years ending after such date.

(b) **IDENTIFICATION REQUIREMENTS.**—

(1) **UNDER SECTION 1236 OF CODE.**—The amendments made by section 506 shall apply to property acquired by the taxpayer after the date of the enactment of this Act in taxable years ending after such date.

(2) **UNDER SECTION 1256(e)(2)(C) OF CODE.**—Section 1256(e)(2)(C) of the Internal Revenue Code of 1954 (as added by this title) shall apply to property acquired and positions established by the taxpayer after December 31, 1981, in taxable years ending after such date.

(c) **ELECTION WITH RESPECT TO PROPERTY HELD ON JUNE 23, 1981.**—If the taxpayer so elects (at such time and in such manner as the Secretary of the Treasury or his delegate shall prescribe) with respect to all regulated futures contracts or positions held by the taxpayer on June 23, 1981, the amendments made by this title shall apply to all such contracts and positions, effective for periods after such date in taxable years ending after such date. For purposes of the preceding sentence, the term “regulated futures contract” has the meaning given to such term by section 1256(b) of the Internal Revenue Code of 1954, and the term “position” has the meaning given to such term by section 1092(d)(2) of such Code.

**SEC. 509. ELECTION FOR EXTENSION OF TIME FOR PAYMENT AND APPLICATION OF SECTION 1256 FOR THE TAXABLE YEAR INCLUDING JUNE 23, 1981.**

(a) **ELECTION.**—

(1) *IN GENERAL.*—In the case of any taxable year beginning before June 23, 1981, and ending after June 22, 1981, the taxpayer may elect, in lieu of any election under section 508(c), to have this section apply to all regulated futures contracts held during such taxable year.

(2) *APPLICATION OF SECTION 1256.*—If a taxpayer elects to have the provisions of this section apply to the taxable year described in paragraph (1).—

(A) the provisions of section 1256 of the Internal Revenue Code of 1954 (other than section 1256(e)(2)(C)) shall apply to regulated futures contracts held by the taxpayer at any time during such taxable year, and

(B) for purposes of determining the rate of tax applicable to gains and losses from regulated futures contracts held at any time during such year, such gains and losses shall be treated as gain or loss from a sale or exchange occurring in a taxable year beginning in 1982.

(3) *DETERMINATION OF DEFERRED TAX LIABILITY.*—If the taxpayer makes an election under this subsection.—

(A) the taxpayer may pay part or all of the tax for such year in two or more (but not exceeding five) equal installments;

(B) the maximum amount of tax which may be paid in installments under this section shall be the excess of—

(i) the tax for such year, determined by taking into account paragraph (2), over

(ii) the tax for such year, determined by taking into account paragraph (2) and by treating all regulated futures contracts which were held by the taxpayer on the first day of the taxable year described in paragraph (1), and which were acquired before the first day of such taxable year, as having been acquired for a purchase price equal to their fair market value on the last business day of the preceding taxable year.

(4) *DATE FOR PAYMENT OF INSTALLMENT.*—

(A) If an election is made under this subsection, the first installment under subsection (a)(3)(A) shall be paid on or before the due date for filing the return for the taxable year described in paragraph (1), and each succeeding installment shall be paid on or before the date which is one year after the date prescribed for payment of the preceding installment.

(B) If a bankruptcy case or insolvency proceeding involving the taxpayer is commenced before the final installment is paid, the total amount of any unpaid installments shall be treated as due and payable on the day preceding the day on which such case or proceeding is commenced.

(5) *INTEREST ON INSTALLMENT.*—

(b) *FORM OF ELECTION.*—An election under this section shall be made not later than the time for filing the return for the taxable year described in subsection (a)(1) and shall be made in the manner and form required by regulations prescribed by the Secretary. The election shall set forth—

(A) the amount determined under subsection (a)(3)(B) and the number of installments elected by the taxpayer,

(B) each regulated futures contract held by the taxpayer on the first day of the taxable year described in subsection (a)(1), and the date such contract was acquired,

(C) the fair market value on the last business day of such taxable year for each regulated futures contract described in subparagraph (B), and

(D) such other information for purposes of carrying out the provisions of this section as may be required by such regulations.

(5) *INTEREST IMPOSED.*—For purposes of section 6601(b) of the Internal Revenue Code of 1954, the time for payment of any tax with respect to which an election is made under this subsection shall be determined without regard to this subsection.

## **TITLE VI—ENERGY PROVISIONS**

### **Subtitle A—Changes in Windfall Profit Tax**

#### **SEC. 601. \$2,500 ROYALTY CREDIT FOR 1981; EXEMPTION FOR 1982 AND THEREAFTER.**

##### **(a) \$2,500 ROYALTY CREDIT FOR 1981.—**

(1) *IN GENERAL.*—Subsection (a) of section 6429 (relating to treatment as overpayment) is amended to read as follows:

“(a) *TREATMENT AS OVERPAYMENT.*—In the case of a qualified royalty owner, that portion of the tax imposed by section 4986 which is paid in connection with qualified royalty production removed from the premises during calendar year 1981 shall be treated as an overpayment of the tax imposed by section 4986.”

(2) *INCREASE IN AMOUNT OF CREDIT.*—Paragraph (1) of section 6429(c) (relating to \$1,000 limitation on credit or refund) is amended to read as follows:

“(1) *IN GENERAL.*—The aggregate amount which may be treated as an overpayment under subsection (a) with respect to any qualified royalty owner for production removed from the premises during calendar year 1981 shall not exceed \$2,500.”

(3) *CONFORMING AMENDMENTS.*—Subsection (c) of section 6429 is amended—

(A) by striking out “\$1,000” each place it appears and inserting in lieu thereof “\$2,500”, and

(B) by striking out “qualified period” each place it appears and inserting in lieu thereof “calendar year”.

(4) *DEFINITION OF QUALIFIED ROYALTY PRODUCTION.*—Subsection (d) of section 6429 is amended by striking out paragraphs (2) and (3) and inserting in lieu thereof the following new paragraphs:

“(2) *QUALIFIED ROYALTY PRODUCTION.*—The term ‘qualified royalty production’ means, with respect to any qualified royalty owner, taxable crude oil which is attributable to an economic interest of such royalty owner other than an operating mineral interest (within the meaning of section 614(d)). Such term does not include taxable crude oil attributable to any overriding royalty interest, production payment, net profits interest, or similar interest of the qualified royalty owner which—

“(A) is created after June 9, 1981, out of an operating mineral interest in property which is proven oil or gas prop-

erty (within the meaning of section 613A(c)(9)(A)) on the date such interest is created, and

“(B) is not created pursuant to a binding contract entered into prior to June 10, 1981.

**“(3) PRODUCTION FROM TRANSFERRED PROPERTY.—**

“(A) **IN GENERAL.**—In the case of a transfer of an interest in any property, the qualified royalty production of the transferee shall not include any production attributable to an interest that has been transferred after June 9, 1981, in a transfer which—

“(i) is described in section 613A(c)(9)(A), and

“(ii) is not described in section 613A(c)(9)(B).

“(B) **EXCEPTIONS.**—Subparagraph (A) shall not apply in the case of any transfer so long as the transferor and the transferee are required by paragraph (3) or (4) of subsection (c) to share the \$2,500 amount in subsection (c)(1). The preceding sentence shall apply to the case of any property only if the production from the property was qualified royalty production of the transferor.

“(C) **TRANSFERS INCLUDE SUBLEASES.**—For purposes of this paragraph, a sublease shall be treated as a transfer.

“(D) **ESTATES.**—For purposes of this paragraph, property held by any estate shall be treated as owned both by such estate and proportionately by the beneficiaries of such estate.”

**(5) QUALIFIED FAMILY FARM CORPORATION DEFINED.**—Paragraph (4) of section 6429(d) is amended to read as follows:

“(4) **QUALIFIED FAMILY FARM CORPORATION.**—The term ‘qualified family farm corporation’ means a corporation—

“(A) all the outstanding shares of stock of which at all times during the calendar year are held by members of the same family (within the meaning of section 2032A(e)(2)), and

“(B) 80 percent in value of the assets of which (other than royalty interests described in paragraph (2)(A)) are held by the corporation at all times during such calendar year for use for farming purposes (within the meaning of section 2032A(e)(5)).”

**(6) CONFORMING AMENDMENTS.—**

(A) Paragraph (3) of section 6654(f) (relating to failure by individuals to pay estimated income tax) is amended to read as follows:

“(3) the sum of—

“(A) the credits against tax allowed by part IV of subchapter A of chapter 1, other than the credit against tax provided by section 31 (relating to tax withheld on wages), plus

“(B) to the extent allowed under regulations prescribed by the Secretary, any amount which is treated under section 6429 as an overpayment of the tax imposed by section 4986.”

(B) Paragraph (2) of section 6655(e) (relating to failure by corporation to pay estimated income tax) is amended to read as follows:

“(2) the sum of—

“(A) the credits against tax provided by part IV of subchapter A of chapter 1, plus

“(B) to the extent allowed under regulations prescribed by the Secretary, any amount which is treated under section 6429 as an overpayment of the tax imposed by section 4986.”

**(b) EXEMPTION FOR 1982 AND THEREAFTER.—**

(1) **IN GENERAL.**—Subsection (b) of section 4991 is amended by striking out “and” at the end of paragraph (3), by striking out the period at the end of paragraph (4), and inserting in lieu thereof “, and”, and by adding at the end thereof the following new paragraph:

“(5) exempt royalty oil.”

(2) **EXEMPT ROYALTY OIL.**—Section 4994 is amended by adding at the end thereof the following new subsection:

**“(f) EXEMPT ROYALTY OIL.]**

“(1) **IN GENERAL.**—For purposes of this chapter, the term ‘exempt royalty oil’ means that portion of the qualified royalty owner’s qualified royalty production for the quarter which does not exceed the royalty limit for such quarter.

“(2) **ROYALTY LIMIT.**—For purposes of this subsection—

“(A) **IN GENERAL.**—A qualified royalty owner’s royalty limit for any quarter is the product of—

“(i) the number of days in such quarter, multiplied by

“(ii) the limitation in barrels determined under the following table:

<b>“In the case of qualified royalty production during:</b>	<b>The limitation in barrels is:</b>
1982 .....	2
1983 .....	2
1984 .....	2
1985 and thereafter.....	3

“(B) **PRODUCTION EXCEEDS LIMITATION.**—If a qualified royalty owner’s qualified royalty production for any quarter exceeds the royalty limitation for such quarter, such royalty owner may allocate such limit to any qualified royalty production which he selects.

**“(3) DEFINITIONS.—**

“(A) **IN GENERAL.**—The terms ‘qualified royalty owner’ and ‘qualified royalty production’ have the meanings given to such terms by section 6429; except that the reference to qualified taxable crude oil in section 6429(d) shall be treated as a reference to oil which would have been taxable crude oil but for this section.

“(B) **ALLOCATION.**—Rules similar to the rules of paragraphs (2), (3), and (4) of section 6429(c) shall apply to the limitation determined under subsection (b)(1).”

(3) **ADJUSTMENTS TO WITHHOLDING.**—Subsection (a) of section 4995 is amended by adding at the end thereof the following new paragraph:

“(9) **ADJUSTMENTS TO TAKE INTO ACCOUNT ROYALTY EXEMPTION.**—The Secretary shall prescribe such regulations as may be necessary so that the withholding required under this subsection shall be reduced to take into account the exemption provided by section 4991(b)(5) (relating to exempt royalty oil).

and he may prescribe such other regulations as may be necessary to administer such exemption.”

**(c) EFFECTIVE DATES.—**

(1) Except as provided in paragraph (2), subsection (a) shall take effect on January 1, 1981.

(2) The amendments made by paragraph (6) of subsection (a) shall take effect on January 1, 1980.

(3) The amendments made by subsection (b) shall apply to oil removed after December 31, 1981.

**SEC. 602. REDUCTION IN TAX IMPOSED ON NEWLY DISCOVERED OIL.**

**(a) IN GENERAL.—**Paragraph (3) of section 4987(b) (relating to applicable percentage) is amended to read as follows:

“(3) **TIER 3 OIL.—**

“(A) **IN GENERAL.—**The applicable percentage for tier 3 oil which is not newly discovered oil is 30 percent.

“(B) **NEWLY DISCOVERED OIL.—**The applicable percentage for newly discovered oil shall be determined in accordance with the following table:

“For taxable periods beginning in:	The applicable percentage is:
1982 .....	27½
1983 .....	25
1984 .....	22½
1985 .....	20
1986 and thereafter .....	15 ”.

**(b) EFFECTIVE DATE.—**The amendment made by this section shall apply to taxable periods beginning after December 31, 1981.

**SEC. 603. EXEMPT INDEPENDENT PRODUCER STRIPPER WELL OIL.**

**(a) IN GENERAL.—**Subsection (b) of section 4991 (as amended by section 601(b)) is amended by striking out “and” at the end of paragraph (4), by striking out the period at the end of paragraph (5), and inserting in lieu thereof “, and”, and by adding at the end thereof the following new paragraph:

“(6) exempt stripper well oil.”

**(b) EXEMPT STRIPPER WELL OIL.—**Section 4994 (as amended by section 601(b)) is amended by adding at the end thereof the following new subsection:

“(g) **EXEMPT STRIPPER WELL OIL.—**

“(1) **IN GENERAL.—**For purposes of this chapter, the term ‘exempt stripper well oil’ means any oil—

“(A) the producer of which is an independent producer (within the meaning of section 4992(b)(1)),

“(B) which is from a stripper well property within the meaning of the June 1979 energy regulations, and

“(C) which is attributable to the independent producer’s working interest in the stripper well property.

“(2) **LIMITATION FOR CERTAIN TRANSFERRED PROPERTIES.—**Exempt stripper well oil does not include production attributable to an interest in any property which at any time after July 22, 1981, was owned by a person other than an independent producer (within the meaning of section 4992(b)(1)).”

**(c) CONFORMING AMENDMENT.—**Paragraph (2) of section 4492(c) (defining independent producer amount) is amended by adding at the end thereof the following new sentence:



“For purposes of the preceding sentence, tier 1 oil and tier 2 oil shall be treated as not including exempt stripper well oil.”

(d) **EFFECTIVE DATE.**—The amendments made by this section shall apply to oil removed from the premises after December 31, 1982.

**SEC. 604. EXEMPTION FROM WINDFALL PROFIT TAX OF OIL PRODUCED FROM INTERESTS HELD BY OR FOR THE BENEFIT OF RESIDENTIAL CHILD CARE AGENCIES.**

(a) **EXEMPTION OF CHILD CARE AGENCIES FROM TAX.**—Subparagraph (A) of section 4994(b)(1) (relating to charitable interests exempt from windfall profit tax) is amended by redesignating clause (ii) as clause (iii) and by adding after clause (i) the following new clause:

“(ii) held by an organization described in section 170(c)(2) which is organized and operated primarily for the residential placement, care, or treatment of delinquent, dependent, orphaned, neglected, or handicapped children, or”.

(b) **PERIOD INTEREST REQUIRED TO BE HELD.**—

(1) **IN GENERAL.**—Subparagraph (B) of section 4994(b)(1) is amended to read as follows:

“(B) such interest was held on January 21, 1980, and at all times thereafter before the last day of the taxable period, by the organization described in clause (i) or (ii) of subparagraph (A), or subclause (I) of subparagraph (A)(iii).”

(2) **INTERESTS HELD FOR THE BENEFIT OF CHILD CARE AGENCIES.**—Paragraph (2) of section 4994(b) is amended—

(A) by striking out “paragraph (1)(A)(ii)” and inserting in lieu thereof “clause (ii) or (iii) of paragraph (1)(A)”, and  
(B) by striking out “paragraph (1)(A)(i)” each place it appears and inserting in lieu thereof “clause (i) or (ii) of paragraph (1)(A)”.

(c) **CONFORMING AMENDMENTS.**—

(1) Clause (i) of section 4994(b)(1)(A) is amended by striking out “or” at the end thereof.

(2) Subclause (II) of section 4994(b)(1)(A)(ii) is amended by inserting “or (ii)” after “clause (i)”.

(d) **EFFECTIVE DATE.**—The amendments made by this section shall apply to taxable periods beginning after December 31, 1980.

**Subtitle B—Miscellaneous Provision**

**SEC. 611. APPLICATION OF CREDIT FOR PRODUCING NATURAL GAS FROM A NONCONVENTIONAL SOURCE WITH THE NATURAL GAS POLICY ACT OF 1978.**

(a) **IN GENERAL.**—Subsection (e) of section 44D (relating to the credit for producing fuel from a nonconventional source) is amended to read as follows:

“(e) **APPLICATION WITH THE NATURAL GAS POLICY ACT OF 1978.**—

“(1) **NO CREDIT IF SECTION 107 OF THE NATURAL GAS POLICY ACT OF 1978 IS UTILIZED.**—Subsection (a) shall apply with respect to any natural gas described in subsection (c)(1)(B)(i) which is sold during the taxable year only if such natural gas is sold at a lawful price which is determined without regard to

the provisions of section 107 of the Natural Gas Policy Act of 1978 and subtitle B of title I of such Act.

“(2) **TREATMENT OF THIS SECTION.**—For purposes of section 107(d) of the Natural Gas Policy Act of 1978, this section shall not be treated as allowing any credit, exemption, deduction, or comparable adjustment applicable to the computation of any Federal tax.”.

(b) **EFFECTIVE DATE.**—The amendment made by this section shall apply to taxable years ending after December 31, 1979.

## **TITLE VII—ADMINISTRATIVE PROVISIONS**

### **Subtitle A—Prohibition of Disclosure of Audit Methods**

#### **SEC. 701. PROHIBITION OF DISCLOSURE OF METHODS FOR SELECTION OF TAX RETURNS FOR AUDITS.**

(a) **GENERAL RULE.**—Paragraph (2) of section 6103(b) (defining return information) is amended by adding at the end thereof the following new sentence: “Nothing in the preceding sentence, or in any other provision of law, shall be construed to require the disclosure of standards used or to be used for the selection of returns for examination, or data used or to be used for determining such standards, if the Secretary determines that such disclosure will seriously impair assessment, collection, or enforcement under the internal revenue laws.”

(b) **EFFECTIVE DATE.**—The amendment made by subsection (a) shall apply to disclosures after July 19, 1981.

### **Subtitle B—Changes in Interest Rate for Overpayments and Underpayments**

#### **SEC. 711. CHANGES IN RATE OF INTEREST FOR OVERPAYMENTS AND UNDERPAYMENTS.**

(a) **ANNUAL ADJUSTMENT TO RATE OF INTEREST.**—Subsection (b) of section 6621 (relating to adjustment of interest rate) is amended by striking out the last sentence thereof.

(b) **RATE OF INTEREST TO BE BASED ON 100 PERCENT OF PRIME RATE.**—Subsection (c) of section 6621 is amended by striking out “90 percent of”.

(c) **NEW RATE TO TAKE EFFECT ON JANUARY 1 OF EACH YEAR AFTER 1982.**—Subsection (b) of section 6621 is amended by striking out “February 1” and inserting in lieu thereof “January 1”.

(d) **EFFECTIVE DATES.**—

(1) **FOR SUBSECTIONS (a) AND (b).**—The amendments made by subsections (a) and (b) shall apply to adjustments made after the date of the enactment of this Act.

(2) **FOR SUBSECTION (c).**—The amendment made by subsection (c) shall apply to adjustments made for periods after 1982.

## **Subtitle C—Changes in Certain Penalties and in Requirements Relating to Returns**

### **SEC. 721. CHANGES IN PENALTIES FOR FALSE INFORMATION WITH RESPECT TO WITHHOLDING.**

(a) **CIVIL PENALTY.**—Section 6682 (relating to false information with respect to withholding allowances based on itemized deductions) is amended to read as follows:

**“SEC. 6682. FALSE INFORMATION WITH RESPECT TO WITHHOLDING.**

**“(a) CIVIL PENALTY.**—In addition to any criminal penalty provided by law, if—

**“(1) any individual makes a statement under section 3402 which results in a decrease in the amounts deducted and withheld under chapter 24, and**

**“(2) as of the time such statement was made, there was no reasonable basis for such statement,**  
such individual shall pay a penalty of \$500 for such statement.

**“(b) EXCEPTION.**—The Secretary may waive (in whole or in part) the penalty imposed under subsection (a) if the taxes imposed with respect to the individual under subtitle A for the taxable year are equal to or less than the sum of—

**“(1) the credits against such taxes allowed by part IV of subchapter A of chapter 1, and**

**“(2) the payments of estimated tax which are considered payments on account of such taxes.**

**“(c) DEFICIENCY PROCEDURES NOT TO APPLY.**—Subchapter B of chapter 63 (relating to deficiency procedures for income, estate, gift, and certain excise taxes) shall not apply in respect to the assessment or collection of any penalty imposed by subsection (a).”

(b) **CRIMINAL PENALTY.**—Section 7205 (relating to fraudulent withholding exemption certificate or failure to supply information) is amended by striking out “\$500” and inserting in lieu thereof “\$1,000”.

(c) **CLERICAL AMENDMENT.**—The table of sections for subchapter B of chapter 68 is amended by striking out the item relating to section 6682 and inserting in lieu thereof the following:

*“Sec. 6682. False information with respect to withholding.”*

(d) **EFFECTIVE DATE.**—The amendments made by this section shall apply to acts and failures to act after December 31, 1981.

### **SEC. 722. ADDITIONS TO TAX IN THE CASE OF VALUATION OVERSTATEMENTS, INCREASE IN NEGLIGENCE PENALTY.**

(a) **VALUATION OVERSTATEMENTS.**—

**(1) IN GENERAL.**—Subchapter A of chapter 68 (relating to additions to tax) is amended by redesignating section 6659 as section 6660 and by inserting after section 6658 the following new section:

**“SEC. 6659. ADDITION TO TAX IN THE CASE OF VALUATION OVERSTATEMENTS FOR PURPOSES OF THE INCOME TAX.**

**“(a) ADDITION TO THE TAX.**—If—

**“(1) an individual, or**

**“(2) a closely held corporation or a personal service corporation,**

has an underpayment of the tax imposed by chapter 1 for the taxable year which is attributable to a valuation overstatement, then

there shall be added to the tax an amount equal to the applicable percentage of the underpayment so attributable.

“(b) **APPLICABLE PERCENTAGE DEFINED.**—For purposes of subsection (a), the applicable percentage shall be determined under the following table:

If the valuation claimed is the following percent of the correct valuation—	The applicable percentage is—
150 percent or more but not more than 200 percent.....	10
More than 200 percent but not more than 250 percent.....	20
More than 250 percent.....	30

“(c) **VALUATION OVERSTATEMENT DEFINED.**—

“(1) **IN GENERAL.**—For purposes of this section, there is a valuation overstatement if the value of any property, or the adjusted basis of any property, claimed on any return exceeds 150 percent of the amount determined to be the correct amount of such valuation or adjusted basis (as the case may be).

“(2) **PROPERTY MUST HAVE BEEN ACQUIRED WITHIN LAST 5 YEARS.**—This section shall not apply to any property which, as of the close of the taxable year for which there is a valuation overstatement, has been held by the taxpayer for more than 5 years.

“(d) **UNDERPAYMENT MUST BE AT LEAST \$1,000.**—This section shall not apply if the underpayment for the taxable year attributable to the valuation overstatement is less than \$1,000.

“(e) **AUTHORITY TO WAIVE.**—The Secretary may waive all or any part of the addition to the tax provided by this section on a showing by the taxpayer that there was a reasonable basis for the valuation or adjusted basis claimed on the return and that such claim was made in good faith.

“(f) **OTHER DEFINITIONS.**—For purposes of this section—

“(1) **UNDERPAYMENT.**—The term ‘underpayment’ has the meaning given to such term by section 6653(c)(1).

“(2) **CLOSELY HELD CORPORATION.**—The term ‘closely held corporation’ means any corporation described in section 465(a)(1)(C).

“(3) **PERSONAL SERVICE CORPORATION.**—The term ‘personal service corporation’ means any corporation which is a service organization (within the meaning of section 414(m)(3)).”

(2) **CLERICAL AMENDMENT.**—The table of sections for subchapter A of chapter 68 is amended by striking out the last item and inserting in lieu thereof the following:

“Sec. 6659. Addition to tax in the case of valuation overstatements for purposes of the income tax.

“Sec. 6660. Applicable rules.”

(3) **TECHNICAL AMENDMENT.**—Subsection (c) of section 5684 (relating to penalties for the payment and collection of liquor taxes) and subsection (d) of section 5761 (relating to civil penalties) are each amended by striking out “6659” in the heading and text thereof and inserting in lieu thereof “6660”.

(4) **EFFECTIVE DATE.**—The amendments made by this subsection shall apply to returns filed after December 31, 1981.

(b) **INCREASE IN NEGLIGENCE PENALTY.**—

(1) **IN GENERAL.**—Subsection (a) of section 6653 (relating to failure to pay tax) is amended to read as follows:

**“(a) NEGLIGENCE OR INTENTIONAL DISREGARD OF RULES AND REGULATIONS WITH RESPECT TO INCOME, GIFT, OR WINDFALL PROFIT TAXES.—**

**“(1) IN GENERAL.—**If any part of any underpayment (as defined in subsection (c)(1)) of any tax imposed by subtitle A, by chapter 12 of subtitle B, or by chapter 45 (relating to windfall profit tax) is due to negligence or intentional disregard of rules or regulations (but without intent to defraud), there shall be added to the tax an amount equal to 5 percent of the underpayment.

**“(2) ADDITIONAL AMOUNT FOR PORTION ATTRIBUTABLE TO NEGLIGENCE, ETC.—**There shall be added to the tax (in addition to the amount determined under paragraph (1)) an amount equal to 50 percent of the interest payable under section 6601—

**“(A)** with respect to the portion of the underpayment described in paragraph (1) which is attributable to the negligence or intentional disregard referred to in paragraph (1), and

**“(B)** for the period beginning on the last date prescribed by law for payment of such underpayment (determined without regard to any extension) and ending on the date of the assessment of the tax.”

**(2) EFFECTIVE DATE.—**The amendment made by paragraph (1) shall apply to taxes the last date prescribed for payment of which is after December 31, 1981.

**SEC. 723. CHANGES IN REQUIREMENTS RELATING TO INFORMATION RETURNS.**

**(a) INCREASES IN PENALTIES FOR FAILURE TO FILE CERTAIN RETURNS OR FURNISH CERTAIN STATEMENTS.—**

**(1) CERTAIN RETURNS.—**Paragraph (1) of section 6652(a) (relating to failure to file certain information returns, registration statements, etc.) is amended to read as follows:

**“(1)** to file a statement of the aggregate amount of payments to another person required by—

**“(A)** section 6041(a) or (b) (relating to certain information at source),

**“(B)** section 6042(a)(1) (relating to payments of dividends aggregating \$10 or more),

**“(C)** section 6044(a)(1) (relating to payments of patronage dividends aggregating \$10 or more),

**“(D)** section 6049(a)(1) (relating to payments of interest aggregating \$10 or more),

**“(E)** section 6050A(a) (relating to reporting requirements of certain fishing boat operators), or

**“(F)** section 6051(d) (relating to information returns with respect to income tax withheld), or”.

**(2) CERTAIN STATEMENTS.—**Section 6678 (relating to failure to furnish certain statements) is amended by striking out “or” at the end of paragraph (1), by inserting “or” at the end of paragraph (2), and by inserting after paragraph (2) the following new paragraph:

**“(3)** to furnish a statement under—

**“(A)** section 6050A(b) (relating to statements furnished by certain fishing boat operators),

“(B) section 6050C (relating to information regarding windfall profit tax on crude oil),

“(C) section 6051 (relating to information returns with respect to income tax withheld) if the statement is required to be furnished to the employee, or

“(D) section 6053(b) (relating to statements furnished by employers with respect to tips),  
on the date prescribed therefor to a person with respect to whom such a statement is required.”

(3) **RETENTION OF EXISTING PENALTIES FOR FAILURE TO FILE CERTAIN STATEMENTS.**—Subsection (b) of section 6652 is amended to read as follows:

“(b) **OTHER RETURNS.**—In the case of each failure to file a statement of a payment to another person required under the authority of—

“(1) section 6042(a)(2) (relating to payments of dividends aggregating less than \$10),

“(2) section 6044(a)(2) (relating to payments of patronage dividends aggregating less than \$10),

“(3) section 6049(a)(2) (relating to payments of interest aggregating less than \$10), or

“(4) section 6049(a)(3) (relating to other payments of interest by corporations),

on the date prescribed therefor (determined with regard to any extension of time for filing), unless it is shown that such failure is due to reasonable cause and not to willful neglect, there shall be paid (upon notice and demand by the Secretary and in the same manner as tax) by the person failing to so file the statement, \$1 for each such statement not so filed, but the total amount imposed on the delinquent person for all such failures during the calendar year shall not exceed \$1,000.”

(4) **CLERICAL AMENDMENT.**—The subsection heading of subsection (a) of section 6652 is amended by inserting “**INFORMATION AT SOURCE,**” before “**PAYMENTS OF DIVIDENDS**”.

(b) **REQUIREMENT OF STATEMENTS TO BE FURNISHED TO PERSONS WITH RESPECT TO WHOM INFORMATION IS FURNISHED ON PAYMENTS OF \$600 OR MORE.**—

(1) **IN GENERAL.**—Section 6041 (relating to information at source) is amended by redesignating subsection (d) as subsection (e) and by inserting after subsection (c) the following new subsection:

“(d) **STATEMENTS TO BE FURNISHED TO PERSONS WITH RESPECT TO WHOM INFORMATION IS FURNISHED.**—Every person making a return under subsection (a) shall furnish to each person whose name is set forth in such return a written statement showing—

“(1) the name, address, and identification number of the person making such return, and

“(2) the aggregate amount of payments to the person shown on the return.

The written statement required under the preceding sentence shall be furnished to the person on or before January 31 of the year following the calendar year for which the return under subsection (a) was made. To the extent provided in regulations prescribed by the Secretary, this subsection shall also apply to persons making returns under subsection (b).”

(2) **PENALTY FOR FAILURE TO FURNISH STATEMENT.**—Paragraph (1) of section 6678 (relating to failure to furnish certain statements) is amended—

(A) by inserting “6041(d),” before “6042(c),” and

(B) by inserting “6041(a),” before “6042(a)(1).”

(c) **EFFECTIVE DATE.**—The amendments made by this section shall apply to returns and statements required to be furnished after December 31, 1981.

**SEC. 724. PENALTY FOR OVERSTATED DEPOSIT CLAIMS.**

(a) **GENERAL RULE.**—Subsection (b) of section 6656 (relating to failure to make deposit of taxes) is amended to read as follows:

“(b) **OVERSTATED DEPOSIT CLAIMS.**—

“(1) **IMPOSITION OF PENALTY.**—Any person who makes an overstated deposit claim shall be subject to a penalty equal to 25 percent of such claim.

“(2) **OVERSTATED DEPOSIT CLAIM DEFINED.**—For purposes of this subsection, the term ‘overstated deposit claim’ means the excess of—

“(A) the amount of tax under this title which any person claims, in a return filed with the Secretary, that such person has deposited in a government depository under section 6302(c) for any period, over

“(B) the aggregate amount such person has deposited in a government depository under section 6302(c), for such period, on or before the date such return is filed.

“(3) **PENALTY NOT IMPOSED IN CERTAIN CASES.**—The penalty under paragraph (1) shall not apply if it is shown that the excess described in paragraph (2) is due to reasonable cause and not due to willful neglect.

“(4) **PENALTY IN ADDITION TO OTHER PENALTIES.**—The penalty under paragraph (1) shall be in addition to any other penalty provided by law.”

(b) **CLERICAL AMENDMENTS.**—

(1) The heading of section 6656 is amended by inserting “OR OVERSTATEMENT OF DEPOSITS” after “TAXES”.

(2) The table of sections for subchapter A of chapter 68 is amended by striking out the item relating to section 6656 and inserting in lieu thereof the following:

“Sec. 6656. Failure to make deposit of taxes or overstatement of deposits.”

(3) The heading of subsection (a) of section 6656 is amended by striking out “PENALTY” and inserting in lieu thereof “UNDERPAYMENT OF DEPOSITS”.

(4)(A) Section 5684 (relating to penalties relating to the payment and collection of liquor taxes) is amended by striking out subsection (b) and by redesignating subsections (c) and (d) as subsections (b) and (c), respectively.

(B) Subsection (c) of section 5684, as redesignated by subparagraph (A), is amended by redesignating paragraphs (4) and (5) as paragraphs (5) and (6), respectively, and by inserting after paragraph (3) the following new paragraph:

“(4) For penalty for failure to make deposits or for overstatement of deposits, see section 6656.”

(5) Section 5761 (relating to civil penalties) is amended by striking out subsections (c) and (d) and inserting in lieu thereof the following:

“(c) **APPLICABILITY OF SECTION 6659.**—The penalty imposed by subsection (b) shall be assessed, collected, and paid in the same manner as taxes, as provided in section 6659(a).

“(d) **CROSS REFERENCES.**—

“For penalty for failure to make deposits or for overstatement of deposits, see section 6656.”

(c) **EFFECTIVE DATE.**—The amendments made by this section shall apply to returns filed after the date of the enactment of this Act.

**SEC. 725. DECLARATION OF ESTIMATED TAX NOT REQUIRED IN CERTAIN CASES.**

(a) **GENERAL RULE.**—Section 6015 (relating to declaration of estimated tax by individuals) is amended by redesignating subsections (b) through (i) as subsections (c) through (j), respectively, and by inserting after subsection (a) the following new subsection:

“(b) **DECLARATION NOT REQUIRED IN CERTAIN CASES.**—No declaration shall be required under subsection (a) if the estimated tax (as defined in subsection (d)) is less than the amount determined in accordance with the following table:

“In the case of taxable years beginning in:

	The amount is:
1981.....	\$100
1982.....	200
1983.....	300
1984.....	400
1985 and thereafter.....	500.”

(b) **NO PENALTY FOR FAILURE TO PAY ESTIMATED TAX IN CERTAIN CASES.**—Section 6654 (relating to failure by individual to pay estimated tax) is amended by redesignating subsections (f) and (g) as subsections (g) and (h), respectively, and by inserting after subsection (e) the following new subsection:

“(f) **EXCEPTION WHERE TAX IS SMALL AMOUNT.**—

“(1) **IN GENERAL.**—No addition to tax shall be imposed under subsection (a) for any taxable year if the tax shown on the return for such taxable year (or, if no return is filed, the tax) is less than the amount determined under the following table:

“In the case of taxable years beginning in:

	The amount is:
1981.....	\$100
1982.....	200
1983.....	300
1984.....	400
1985 and thereafter.....	500.”

“(2) **SPECIAL RULE.**—For purposes of subsection (b), the amount of any installment required to be paid shall be determined without regard to subsection (b) of section 6015.”

(c) **TECHNICAL AMENDMENTS.**—

(1) Paragraph (6) of section 871(g) is amended by striking out “6015(i)” and inserting in lieu thereof “6015(j)”.

(2) Subsection (a) of section 6015 is amended by striking out the last sentence.

(3) Subsection (a) of section 6153 is amended by striking out “6015(c)” and inserting in lieu thereof “6015(d)”.



(4) Subparagraph (A) of section 7701(a)(34) is amended by striking out "6015(c)" and inserting in lieu thereof "6015(d)".

(5) Subsection (g) of such section 6654 (as redesignated by subsection (b)) is amended by striking out "subsections (b) and (d)" and inserting in lieu thereof "subsections (b), (d), and (f)".

(d) **EFFECTIVE DATE.**—The amendments made by this section shall apply to estimated tax for taxable years beginning after December 31, 1980.

### **Subtitle D—Cash Management**

#### **SEC. 731. CASH MANAGEMENT.**

(a) **IN GENERAL.**—Paragraph (1) of section 6655(h) (relating to large corporations required to pay at least 60 percent of current year tax) is amended to read as follows:

“(1) **MINIMUM PERCENTAGE.**—

“(A) **IN GENERAL.**—Except as provided in subparagraph (B), in the case of a large corporation, paragraphs (1) and (2) of subsection (d) shall not apply.

“(B) **TRANSITION RULE.**—For taxable years beginning before 1984, in the case of a large corporation, the amount treated as the estimated tax for the taxable year under paragraphs (1) and (2) of subsection (d) shall in no event be less than the applicable percentage of—

“(i) the tax shown on the return for the taxable year,  
or  
“(ii) if no return was filed, the tax for such year.

“(C) **APPLICABLE PERCENTAGE.**—For purposes of subparagraph (B), the applicable percentage shall be determined in accordance with the following table:

“If the taxable year begins in:	The applicable percentage is:
1982.....	65
1983.....	75.”

(b) **CLERICAL AMENDMENT.**—The heading of subsection (h) of section 6655 (relating to failure by corporations to pay estimated income tax) is amended by striking out “at Least 60 Percent” and inserting in lieu thereof “Minimum Percentage”.

(c) **EFFECTIVE DATE.**—The amendments made by this section shall apply to taxable years beginning after December 31, 1981.

### **Subtitle E—Financing of Railroad Retirement System**

#### **SEC. 741. INCREASES IN EMPLOYER AND EMPLOYEE TAXES.**

(a) **TAX ON EMPLOYEES.**—Section 3201 (relating to rate of tax on employees) is amended by striking out all that precedes “the rate of the tax” and inserting in lieu thereof the following:

“(a) In addition to other taxes, there is hereby imposed on the income of each employee a tax equal to 2.0 percent of so much of the compensation paid in any calendar month to such employee for services rendered by him as is not in excess of an amount equal to one-twelfth of the current maximum annual taxable ‘wages’ as defined in section 3121 for any month.

“(b) The rate of tax imposed by subsection (a) shall be increased by”.

(b) **TAX ON EMPLOYEE REPRESENTATIVES.**—Subsection (a) of section 3211 (relating to tax on employee representatives) is amended by striking out “9.5” and inserting in lieu thereof “11.75”.

(c) **TAX ON EMPLOYERS.**—The first sentence of section 3221(a) (relating to tax on employers) is amended by striking out “9.5” and inserting in lieu thereof “11.75”.

(d) **CONFORMING AMENDMENTS.**—

(1) The last sentence of section 230(c) of the Social Security Act is amended—

(A) by inserting “employee and” before “employer”,

(B) by striking out “section 3221(a)” and inserting in lieu thereof “sections 3201(a) and 3221(a)”, and

(C) by striking out “9.5” and inserting in lieu thereof “11.75”.

(2) Paragraph (1) of section 3231(e) (defining compensation) is amended by striking out “(iii)” and all that follows through “(iv)” and inserting in lieu thereof “or (iii)”.

(e) **EFFECTIVE DATE.**—The amendments made by this section shall apply to compensation paid for services rendered after September 30, 1981.

**SEC. 742. ADVANCE TRANSFER OF AMOUNTS PAYABLE UNDER SOCIAL SECURITY FINANCIAL INTERCHANGE.**

Section 15(b) of the Railroad Retirement Act of 1974 is amended by inserting “(1)” after “(b)” and by inserting at the end thereof the following new subdivision:

“(2) In any month when the Board finds that the balance in the Railroad Retirement Account is insufficient to pay annuity amounts due to be paid during the following month, the Board shall report to the Secretary of the Treasury the additional amount of money necessary in order to make such annuity payments, and the Secretary shall transfer to the credit of the Railroad Retirement Account such additional amount upon receiving such report from the Board. The total amount of money outstanding to the Railroad Retirement Account from the general fund at any time during any fiscal year shall not exceed the total amount of money the Board and the Trustees of the Social Security Trust Funds estimate will be transferred to the Railroad Retirement Account pursuant to section 7(c)(2) of this Act with respect to such fiscal year. Whenever the Board determines that the sums in the Railroad Retirement Account are sufficient to pay annuity amounts, the Board shall request the Secretary of the Treasury to retransfer to the general fund from the Railroad Retirement Account all or any part of the amount outstanding, and the Secretary of the Treasury shall make such retransfer of the amount requested. Not later than 10 days after a transfer to the Railroad Retirement Account under section 7(c)(2) of this Act, any amount of money outstanding to the Railroad Retirement Account from the general fund under this subdivision shall be retransferred in accordance with this subdivision. Any amount retransferred shall include an amount of interest computed at a rate determined in accordance with the following two sentences: The rate of interest payable with respect to an amount outstanding for any month shall be equal to the average investment yield for the most recent auction (before such month) of United States Treasury bills with maturities of 52 weeks, deeming any amount outstanding at the beginning of a month to have been borrowed at the beginning of

such month. For this purpose the amount of interest computed in accordance with the preceding sentence but not repaid by the end of such month shall be added to the amount outstanding at the beginning of the next month."

**SEC. 743. AMENDMENTS TO SECTION 3231 CLARIFYING DEFINITION OF COMPENSATION.**

(a) Paragraph (1) of section 3231(e) (defining compensation) is amended by adding after the third sentence thereof the following new sentence: "Compensation which is paid in one calendar month but which would be payable in a prior or subsequent taxable month but for the fact that prescribed date of payment would fall on a Saturday, Sunday or legal holiday shall be deemed to have been paid in such prior or subsequent taxable month."

(b) Paragraph (2) of section 3231(e) is amended by adding at the beginning thereof the following new sentence: "A payment made by an employer to an individual through the employer's payroll shall be presumed, in the absence of evidence to the contrary, to be compensation for service rendered by such individual as an employee of the employer in the period with respect to which the payment is made."

(c) Paragraph (2) of section 3231(e), as amended by subsection (b), is amended by striking from the second sentence thereof the words "An employee" and inserting instead the words: "An employee receiving retroactive wage payments".

(d) The amendments made by this section shall apply for taxable years beginning after December 31, 1981.

## **Subtitle F—Filing Fees**

**SEC. 751. FEES FOR FILING PETITIONS.**

(a) **IN GENERAL.**—Section 7451 is amended by striking out "\$10" and inserting in lieu thereof "\$60".

(b) **EFFECTIVE DATE.**—The amendment made by this section shall apply to petitions filed after December 31, 1981.

## **TITLE VIII—MISCELLANEOUS PROVISIONS**

### **Subtitle A—Extension**

**SEC. 801. FRINGE BENEFITS.**

Section 1 of the Act entitled "An Act to prohibit the issuance of regulations on the taxation of fringe benefits, and for other purposes", approved October 7, 1978 (Public Law 95-427), is amended by striking out "May 31, 1981" each place it appears and inserting in lieu thereof "December 31, 1983".

**SEC. 802. EXCLUSION FOR PREPAID LEGAL SERVICES EXTENDED FOR 3 YEARS.**

(a) **EXTENSION.**—Section 120 (relating to amounts received under qualified group legal services plans) is amended by adding at the end thereof the following new subsection:

"(e) **TERMINATION.**—This section shall not apply to taxable years ending after December 31, 1984."

(b) **CONFORMING AMENDMENT.**—Paragraph (1) of section 2134(e) of the Tax Reform Act of 1976 (relating to effective date) is amended by striking out “, and ending before January 1, 1982”.

### **Subtitle B—Tax-Exempt Obligations**

#### **SEC. 811. TAX-EXEMPT FINANCING FOR VEHICLES USED FOR MASS COMMUTING.**

(a) **GENERAL RULE.**—Paragraph (4) of section 103(b) (relating to industrial development bonds) is amended by striking out “or” at the end of subparagraph (G), by striking out the period at the end of subparagraph (H) and inserting in lieu thereof “, or”, and by inserting after subparagraph (H) the following new subparagraph:

“(I) qualified mass commuting vehicles.”

(b) **DEFINITION OF QUALIFIED MASS COMMUTING VEHICLES.**—Subsection (b) of section 103 is amended by redesignating paragraph (9) as paragraph (10) and by inserting after paragraph (8) the following new paragraph:

“(9) **QUALIFIED MASS COMMUTING VEHICLES.**—

“(A) **IN GENERAL.**—For purposes of paragraph (4)(I), the term ‘qualified mass commuting vehicle’ means any bus, subway car, rail car, or similar equipment—

“(i) which is leased to a mass transit system wholly owned by 1 or more governmental units (or agencies or instrumentalities thereof), and

“(ii) which is used by such system in providing mass commuting services.

“(B) **TERMINATION.**—Paragraph (4)(I) shall not apply to any obligation issued after December 31, 1984.”

(c) **EFFECTIVE DATE.**—The amendments made by this section shall apply to obligations issued after the date of the enactment of this Act.

#### **SEC. 812. OBLIGATIONS OF CERTAIN VOLUNTEER FIRE DEPARTMENTS.**

(a) **IN GENERAL.**—Section 103 (relating to interest on certain governmental obligations) is amended by redesignating subsection (i) as subsection (J) and by inserting after subsection (H) the following new subsection:

“(i) **OBLIGATIONS OF CERTAIN VOLUNTEER FIRE DEPARTMENTS.**—

“(1) **IN GENERAL.**—An obligation of a volunteer fire department shall be treated as an obligation of a political subdivision of a State if—

“(A) such department is a qualified volunteer fire department with respect to an area within the jurisdiction of such political subdivision, and

“(B) such obligation is issued as part of an issue substantially all of the proceeds of which are to be used for the acquisition, construction, reconstruction, or improvement of a firehouse or firetruck used or to be used by such department.

“(2) **QUALIFIED VOLUNTEER FIRE DEPARTMENT.**—For purposes of this subsection, the term ‘qualified volunteer fire department’ means, with respect to a political subdivision of a State, any organization—

“(A) which is organized and operated to provide firefighting or emergency medical services for persons in an area

*(within the jurisdiction of such political subdivision) which is not provided with any other firefighting services,*

*“(B) which is required (by written agreement) by the political subdivision to furnish firefighting services in such area.”*

**(b) EFFECTIVE DATE.—**

**(1) IN GENERAL.—***The amendment made by subsection (a) shall apply to obligations issued after December 31, 1980.*

**(2) SPECIAL RULE FOR CERTAIN OBLIGATIONS ISSUED BEFORE EFFECTIVE DATE.—**

**(A) IN GENERAL.—***Interest on any obligation described in subparagraph (B) shall be excluded from gross income.*

**(B) OBLIGATION TO WHICH PARAGRAPH APPLIES.—***For purposes of subparagraph (A), an obligation is described in this subparagraph if the obligation—*

*(i) was issued after December 31, 1969, and before January 1, 1981, to the First Bank and Trust Company of Indianapolis, Indiana,*

*(ii) was issued by a qualified volunteer fire department (within the meaning of section 103(i)(2) of the Internal Revenue Code of 1954), and*

*(iii) was issued for the acquisition, construction, reconstruction, or improvement of firefighting property.*

*An obligation shall be treated as described in this subparagraph only for the period which is held by the First Bank and Trust Company of Indianapolis, Indiana.*

**(C) FIREFIGHTING PROPERTY.—***For purposes of subparagraph (B), the term ‘firefighting property’ means property—*

*(i) which is of a character subject to the allowance for depreciation, and*

*(ii)(I) which is used in the training for the performance of, or in the performance of, firefighting or ambulance services, or*

*(II) which is exclusively used to house the property described in subclause (I).*

## **Subtitle C—Excise Taxes**

### **SEC. 821. EXTENSION OF TELEPHONE EXCISE TAX.**

**(a) IN GENERAL.—***The table contained in paragraph (2) of section 4251(a) (relating to imposition of tax on communications) is amended by striking out the last line and inserting in lieu thereof the following:*

*“During 1982, 1983, or 1984..... 1”.*

**(b) CONFORMING AMENDMENT.—***Subsection (b) of section 4251 is amended by striking out “1983” and inserting in lieu thereof “1985”*

### **SEC. 822. EXCLUSION OF CERTAIN SERVICES FROM FEDERAL UNEMPLOYMENT TAX ACT.**

**(a) IN GENERAL.—***Section 3306(c) (relating to the definition of employment under the Federal Unemployment Tax Act) is amended—*

*(1) by striking out “or” at the end of paragraph (17);*

*(2) by redesignating paragraph (18) as paragraph (19); and*

*(3) by inserting after paragraph (17) the following new paragraph:*

“(18) service described in section 3121(b)(20); or”.

(b) **EFFECTIVE DATE.**—The amendments made by subsection (a) shall be effective with respect to remuneration paid during 1981.

**SEC. 823. PRIVATE FOUNDATION DISTRIBUTIONS.**

(c) **GENERAL RULE.**—

(1) Paragraph (1) of section 4942(d) (defining distributable amount) is amended by striking out “or the adjusted net income (whichever is higher)”.

(2) Paragraph (3)(A) of section 4942(j) (defining operating foundation) is amended to read as follows:

“(A) which makes qualifying distributions (within the meaning of paragraph (1) or (2) of subsection (g)) directly for the active conduct of the activities constituting the purpose or function for which it is organized and operated equal to substantially all of the lesser of—

“(i) its adjusted net income (as defined in subsection (f), and

“(ii) its minimum investment return; and”.

(3) Paragraph (3) of section 4942(j) is amended by adding at the end thereof the following new sentence: “Notwithstanding the provisions of subparagraph (A), if the qualifying distributions (within the meaning of paragraph (1) or (2) of subsection (g)) of an organization for the taxable year exceed the minimum investment return for the taxable year, clause (ii) of subparagraph (A) shall not apply unless substantially all of such qualifying distributions are made directly for the active conduct of the activities constituting the purpose or function for which it is organized and operated.”

(b) **EFFECTIVE DATE.**—The amendments made by this section shall apply to taxable years beginning after December 31, 1981.

### **Subtitle D—Other Provisions**

**SEC. 831. TECHNICAL AMENDMENTS RELATING TO DISPOSITIONS OF INVESTMENT IN UNITED STATES REAL PROPERTY.**

(a) **GENERAL RULE.**—

(1) Paragraph (1)(A)(i) of section 897(c) (defining United States real property interests) is amended by striking out “United States” and inserting in lieu thereof “United States or the Virgin Islands”.

(2) Section 862(a) (relating to income from sources without the United States) is amended—

(A) by striking out “and” at the end of paragraph (5),

(B) by striking out the period at the end of paragraph (6) and inserting in lieu thereof a semicolon,

(C) by striking out “Underwriting” in paragraph (7) and inserting in lieu thereof “underwriting”,

(D) by striking out the period at the end of paragraph (7) and inserting in lieu thereof “; and”, and

(E) by adding at the end thereof the following new paragraph:

“(8) gains, profits, and income from the disposition of a United States real property interest (as defined in section 897(c)) when the real property is located in the Virgin Islands.”

(3) Section 6039C (relating to returns with respect to United States real property interests) is amended by adding at the end thereof the following new subsection:

**“(f) SPECIAL RULE FOR UNITED STATES INTEREST AND VIRGIN ISLANDS INTEREST.**—A nonresident alien individual or foreign corporation subject to tax under section 897(a) shall pay any tax and file any return required by this title—

“(1) to the United States, in the case of any interest in real property located in the United States and an interest (other than an interest solely as a creditor) in a domestic corporation (with respect to the United States) described in section 897(c)(1)(A)(ii), and

“(2) to the Virgin Islands, in the case of an interest in real property located in the Virgin Islands and an interest (other than an interest solely as a creditor) in a domestic corporation (with respect to the Virgin Islands) described in section 897(c)(1)(A)(ii).

(b) **PARTNERSHIP ASSETS.**—Paragraph (4)(B) of section 897(c) is amended to read as follows:

**“(B) ASSETS HELD BY PARTNERSHIPS, ETC.**—Under regulations prescribed by the Secretary, assets held by a partnership, trust, or estate shall be treated as held proportionately by its partners or beneficiaries. Any asset treated as held by a partner or beneficiary by reason of this subparagraph which is used or held for use by the partnership, trust, or estate in a trade or business shall be treated as so used or held by the partner or beneficiary. Any asset treated as held by a partner or beneficiary by reason of this subparagraph shall be so treated for purposes of applying this subparagraph successively to partnerships, trusts, or estates which are above the first partnership, trust, or estate in a chain thereof.”

(c) **NONRECOGNITION RULES OVERRIDDEN IN CERTAIN CASES.**—Subparagraph (B) of section 897(d)(1) is amended to read as follows:

**“(B) EXCEPTIONS.**—Gain shall not be recognized under subparagraph (A)—

“(i) if—

“(I) at the time of the receipt of the distributed property, the distributee would be subject to taxation under this chapter on a subsequent disposition of the distributed property, and

“(II) the basis of the distributed property in the hands of the distributee is no greater than the adjusted basis of such property before the distribution, increased by the amount of gain (if any) recognized by the distributing corporation, or

“(ii) if such nonrecognition is provided in regulations prescribed by the Secretary under subsection (e)(2).”

(d) **FOREIGN CORPORATION PERMITTED TO ELECT TO BE TREATED AS A DOMESTIC CORPORATION.**—Subsection (i) of section 897 is amended to read as follows:

**“(i) ELECTION BY FOREIGN CORPORATION TO BE TREATED AS DOMESTIC CORPORATION.**—

“(1) **IN GENERAL.**—If—

*“(A) a foreign corporation holds a United States real property interest, and*

*“(B) under any treaty obligation of the United States the foreign corporation is entitled to nondiscriminatory treatment with respect to that interest,*

*then such foreign corporation may make an election to be treated as a domestic corporation for purposes of this section and section 6039C.*

*“(2) REVOCATION ONLY WITH CONSENT.—Any election under paragraph (1), once made, may be revoked only with the consent of the Secretary.*

*“(3) MAKING OF ELECTION.—An election under paragraph (1) may be made only—*

*“(A) if all of the owners of all classes of interests (other than interests solely as a creditor) in the foreign corporation at the time of the election consent to the making of the election and agree that gain, if any, from the disposition of such interest after June 18, 1980, which would be taken into account under subsection (a) shall be taxable notwithstanding any provision to the contrary in a treaty to which the United States is a party, and*

*“(B) subject to such other conditions as the Secretary may prescribe by regulations with respect to the corporation or its shareholders.*

*In the case of a class of interest (other than an interest solely as a creditor) which is regularly traded on an established securities market, the consent described in subparagraph (A) need only be made by any person if such person held more than 5 percent of such class of interest at some time during the shorter of the periods described in subsection (c)(1)(A)(ii). The constructive ownership rules of subsection (c)(6)(C) shall apply in determining whether a person held more than 5 percent of a class of interest.*

*“(4) EXCLUSIVE METHOD OF CLAIMING NONDISCRIMINATION.—The election provided by paragraph (1) shall be the exclusive remedy for any person claiming discriminatory treatment with respect to this section and section 6039C.”*

*(e) REPORTING REQUIRED FOR CERTAIN INDIRECT HOLDINGS.—Paragraph (4)(C) of section 6039C(b) is amended to read as follows:*

*“(C) INDIRECT HOLDINGS.—For purposes of determining whether an entity to which this subsection applies has a substantial investor in United States real property, the assets of any person shall include the person’s pro rata share of the United States real property interest held by any corporation (whether domestic or foreign) if the person’s pro rata share of the United States real property interests exceeded \$50,000.”*

*(f) CERTAIN CONTRIBUTIONS TO CAPITAL.—Section 897 is amended by adding at the end thereof the following new subsection:*

*“(j) CERTAIN CONTRIBUTIONS TO CAPITAL.—Except to the extent otherwise provided in regulations, gain shall be recognized by a nonresident alien individual or foreign corporation on the transfer of a United States real property interest to a foreign corporation if the transfer is made as paid in surplus or as a contribution to capital, in the amount of the excess of—*



“(1) the fair market value of such property transferred, over

“(2) the sum of—

“(A) the adjusted basis of such property in the hands of the transferor, plus

“(B) the amount of gain, if any, recognized to the transferor under any other provision at the time of the transfer.”

(g) **PRE-ENACTMENT ACQUISITIONS.**—Section 897 is amended by adding at the end thereof the following new subsections:

(h) **FOREIGN CORPORATIONS ACQUIRED BEFORE ENACTMENT.**—If—

“(1) a foreign corporation adopts, or has adopted, a plan of liquidation described in section 334(b)(2)(A), and

“(2) the 12-month period described in section 334(b)(2)(B) for the acquisition by purchase of the stock of the foreign corporation, began after December 31, 1979, and before November 26, 1980,

then such foreign corporation may make an election to be treated, for the period following June 18, 1980, as a domestic corporation pursuant to section 897(i)(1). Notwithstanding an election under the preceding sentence, any selling shareholder of such corporation shall be considered to have sold the stock of a foreign corporation.

“(1) **SPECIAL RULE FOR CERTAIN UNITED STATES SHAREHOLDERS OF LIQUIDATING FOREIGN CORPORATIONS.**—If a corporation adopts a plan of complete liquidation and if, solely by reason of section 897(d), section 337(a) does not apply to sales or exchanges, or section 336 does not apply to distributions, of United States real property interests by such corporation, then, in the case of any shareholder who is a United States citizen or resident and who has held stock in such corporation continuously since June 18, 1980, for the first taxable year of such shareholder in which he receives a distribution in complete liquidation with respect to such stock—

“(1) the amount realized by such shareholder on the distribution shall be increased by his proportionate share of the amount by which the tax imposed by this subtitle on such corporation would have been reduced if section 897(d) had not been applicable, and

“(2) for purposes of this title, such shareholder shall be deemed to have paid, on the last day prescribed by law for the payment of the tax imposed by this subtitle on such shareholder for such taxable year, an amount of tax equal to the amount of the increase described in paragraph (1).”

(h) **TREATY.**—Paragraph (2)(B) of section 1125 of the Foreign Investment Real Property Tax Act of 1980 is amended to read as follows:

“(B) the new treaty is signed on or after January 1, 1981, and before January 1, 1985,

then paragraph (1) shall be applied with respect to obligations under the old treaty by substituting for ‘December 31, 1984’ the date (not later than 2 years after the new treaty was signed) specified in the new treaty (or accompanying exchange of notes).”

(i) **EFFECTIVE DATES.**—The amendments made by this section shall apply to dispositions after June 18, 1980, in taxable years ending after such date.

**SEC. 832. MODIFICATION OF FOREIGN INVESTMENT COMPANY PROVISIONS.**

*(a) IN GENERAL.—Paragraph (2) of section 1246(a) (defining ratable share) is amended by striking out subparagraph (B) and inserting in lieu thereof the following:*

*“(B) excluding such earnings and profits attributable to—*

*“(i) any amount previously included in the gross income of such taxpayer under section 951 (but only to the extent the inclusion of such amount did not result in an exclusion of any other amount from gross income under section 959), or*

*“(ii) any taxable year during which such corporation was not a foreign investment company but only if—*

*“(I) such corporation was not a foreign investment company at any time before such taxable year, and*

*“(II) such corporation was treated as a foreign investment company solely by reason of subsection (b)(2).”*

*(b) EFFECTIVE DATE.—The amendment made by subsection (a) shall apply to sales or exchanges after the date of the enactment of this Act in taxable years ending after such date.*

And the Senate agree to the same.

BOB DOLE,  
BOB PACKWOOD,  
BILL ROTH,  
JOHN C. DANFORTH,  
RUSSELL B. LONG,  
HARRY F. BYRD, Jr.,  
LLOYD BENTSEN,

*Managers on the Part of the Senate.*

DAN ROSTENKOWSKI,  
SAM GIBBONS,  
J. J. PICKLE,  
CHARLES B. RANGEL,  
PETE STARK,  
BARBER B. CONABLE, Jr.,  
JOHN J. DUNCAN,  
WILLIAM ARCHER,

*Managers on the Part of the House.*

## **JOINT EXPLANATORY STATEMENT OF THE COMMITTEE OF CONFERENCE**

The Managers on the part of the House and Senate at the conference on the disagreeing votes of the two Houses on the amendment of the Senate to the bill (H.R. 4242) to encourage economic growth through reduction of tax rates submit the following joint statement to the House and the Senate as an explanation of the effect of the action agreed upon by the Managers and recommended in the accompanying report:

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## I. EXPLANATION OF CONFERENCE AGREEMENT

### A. Individual Income Tax Reductions

#### 1. Individual rate reductions

*House bill.*—Under present law, individual income tax rates begin at 14 percent on taxable income above \$3,400 on a joint return and \$2,400 on a single return. The rates range up to 70 percent on taxable incomes, in excess of \$215,400 on a joint return, and \$108,300 on a single return.

The highest marginal rate is 70 percent on taxable income in excess of \$215,400 on a joint return and \$108,300 on a single return. However, the top rate on personal service income is limited to 50 percent (the maximum tax). This rate applies above \$60,000 on a joint return and \$41,500 on a single return.

A deduction from gross income is allowed for 60 percent of any net capital gain for the year. The remaining 40 percent of any net capital gain is taxed at the ordinary rates up to 70 percent. Thus, the top effective tax rate on capital gains is 28 percent (70 percent rate times the 40 percent included in taxable income).

The capital gains deduction generally applies to assets held more than one year.

The House bill provides for cumulative across-the-board reductions of 23 percent by 1984 on the following schedule:

	<i>Percent</i>
1981 .....	1¼
1982 .....	10
1983 .....	19
1984 .....	23

Withholding changes take place on October 1, 1981, July 1, 1982, and July 1, 1983. The bill makes several other withholding changes to give the Secretary the authority to issue regulations, which would permit workers to adjust their withholding to more closely match their tax liability.

The House bill reduces the top marginal rate from 70 percent to 50 percent (and, thus, the maximum effective rate on capital gains from 28 percent to 20 percent) in 1982 and repeals the maximum tax in 1982.

A special alternative tax for 1981 provides that a maximum 20-percent rate on net capital gains will apply to sales or exchanges occurring after June 8, 1981. Thus, this provision does not apply to taxable receipts after June 8, 1981, of proceeds of sales or exchanges which occurred prior to that date.

The holding period for long-term capital gain or loss treatment is reduced to 6 months for taxable years beginning after December 31, 1981.

*Senate amendment.*—The Senate amendment is the same as the House bill, except (1) that the alternative tax for capital gains for individuals applies to sales and exchanges after June 9, 1981, and (2) there is no provision reducing the holding period for capital gains.

*Conference agreement.*—The conference agreement is the same as the Senate amendment, except for technical changes.

## 2. Deduction for two-earner married couples

**House bill.**—Under present law, married taxpayers generally are treated as a single taxpaying unit. If married taxpayers elect to file separate rather than joint returns, they usually pay a higher tax. The differing rate schedules for single and married taxpayers give rise to a marriage penalty when two single wage earners of relatively equal income marry each other.

The House bill allows couples filing a joint return a deduction in computing adjusted gross income equal to a percentage of the lower earning spouse's qualified earned income (up to \$30,000 of income). In 1982, the percentage will be 5 percent (up to a \$1,500 maximum deduction) and in 1983 and subsequent years the percentage will be 10 percent (up to a \$3,000 maximum deduction).

**Senate amendment.**—Same as House bill.

**Conference agreement.**—The conference agreement is the same as the House bill and the Senate amendment.

## 3. Indexing

**House bill.**—Under present law, the individual income tax is based on various fixed amounts including the amounts that define the tax brackets, the zero bracket amount, and the personal exemption. These amounts are set by statute and are not adjusted for inflation.

Under the House bill, the income tax brackets, zero bracket amount, and personal exemption are adjusted for inflation (as measured by the Consumer Price Index), starting in 1985.

**Senate amendment.**—Same as House bill.

**Conference agreement.**—The conference agreement is the same as the House bill and the Senate amendment.

## 4. Individuals eligible for earned income credit

**House bill.**—No provision.

**Senate amendment.**—Under present law, individuals eligible for the earned income credit include all married individuals entitled to a dependency exemption for a child, surviving spouses, and heads of households who maintain a household for a child. In each case, the child must reside with the taxpayer in the United States.

Under the Senate amendment, an individual would not be eligible for the credit unless he or she is a citizen of the United States or an alien admitted as a permanent resident.

**Conference agreement.**—The conference agreement follows the House bill.

## 5. Child and dependent care credit

**House bill.**—No provision.

**Senate amendment.**—Under present law, there is a tax credit for 20 percent of expenditures for the care of children and other dependents incurred in connection with the taxpayer's employment, up to a maximum of \$2,000 of expenditures for each of the taxpayer's first two dependents.

The Senate amendment provides a refundable child care credit equal to 30 percent of employment-related expenses of taxpayers with incomes of \$10,000 or less. The credit will be reduced by one percent for each \$2,000, or fraction thereof, of income above \$10,000. For taxpayers with adjusted gross income above \$28,000,



the credit rate will be 20 percent. The maximum amount of employment-related expenses taken into account will be increased to \$2,400 (one dependent) and \$4,800 (two or more dependents). Expenditures for out-of-home, noninstitutional care of a disabled spouse or dependent are made eligible for the credit. Expenditures for services provided by a dependent care center not in compliance with State or local regulations will not be eligible for the credit.

The Senate amendment also provides that child care provided by an employer under a written nondiscriminatory plan will not be included in an employee's gross income. In addition, employers will be entitled to a credit equal to 50 percent of the cost of any employer-provided child and dependent care.

**Conference agreement.**—The conference agreement follows the Senate amendment with several modifications. Under the conference agreement, the increased child care credit will not be refundable. In addition, employers will not be entitled to a tax credit for employer-provided child and dependent care.

In general, the provision is effective in taxable years beginning after December 31, 1981. The phase-down of the credit percentage applies to remuneration paid after December 31, 1981.

#### 6. Charitable contributions deduction for nonitemizers

**House bill.**—Under present law, charitable contributions may be deducted from adjusted gross income in determining taxable income. Thus, in order for an individual taxpayer to deduct charitable contributions, the taxpayer must itemize deductions. Present law also provides that charitable contributions are allowable as deductions only if verified under Treasury regulations.

The House bill allows all taxpayers to deduct allowable charitable contributions whether or not they itemize deductions.

The deduction would be a percentage of contributions up to a fixed dollar amount of contributions as follows:

Year	Percentage	Cap
1982	25	\$100
1983	25	100
1984	25	100
1985	50	.....
1986	100	.....
1987	Provisions expires.	.....

**Senate amendment.**—The Senate amendment is similar to the House bill with the following limitations:

Year	Percentage	Cap
1982	25	\$100
1983	25	100
1984	25	.....
1985	50	.....
1986	100	.....
1987	Provision expires.	.....

**Conference agreement.**—The conference agreement generally follows the Senate amendment with the addition of a \$300 contribution cap in 1984 (\$75 maximum deduction). In addition, the confer-

ees intend that the Secretary promulgate new regulations providing substantiation requirements for claiming the deduction. The contribution cap is the same for married taxpayers filing joint returns and single taxpayers. The cap is one-half the applicable amount for married taxpayers filing separately.

The provision is effective for taxable years beginning after December 31, 1981, and applies to contributions made after that date. The provision will not apply to contributions made after December 31, 1986.

## 7. Gain on sale of residence

### *a. Replacement period for rollover of gain on sale of residence*

**House bill.**—Present law provides for the deferral of recognition or rollover, of gain on the sale of a taxpayer's principal residence if a new principal residence is purchased and used by the taxpayer within a period beginning 18 months before, and ending 18 months after, the sale. This rule applies only to the extent that the purchase price of the replacement residence equals or exceeds the sale price of residence sold.

The House bill extends the 18-month replacement period of present law to 2 years. This change is effective for sales and exchanges of principal residences after July 20, 1981, and for such sales and exchanges with respect to which the 18-month rollover period has not expired on or before July 20, 1981. It is not effective for sales and exchanges of principal residences with respect to which the 18-month rollover period has expired by July 21, 1981.

**Senate amendment.**—No provision.

**Conference agreement.**—The conference agreement follows the House bill.

### *b. Exclusion of gain on sale of residence*

**House bill.**—Present law allows individuals who have attained the age of 55 to elect a one-time exclusion of up to \$100,000 of gain on the sale of their principal residence (Code sec. 121). Generally, the individual must have owned and used the property as a principal residence for three years or more out of the five-year period preceding the sale.

The House bill increases from \$100,000 to \$125,000 the amount of gain excludable from gross income on the sale or exchange of a principal residence by an individual who has attained the age of 55.

The House bill is effective on sales and exchanges of a principal residence after July 20, 1981.

**Senate amendment.**—No provision.

**Conference agreement.**—The conference agreement follows the House bill.

### *c. Sale of residence by handicapped individual*

**House bill.**—No provision

**Senate amendment.**—Present law allows individuals who have attained the age of 55 to elect a one-time exclusion of up to \$100,000 of gain on the sale of their principal residence. Generally, the individual must have owned and used the property as a principal residence for three years or more out of the five-year period preceding the sale. The Senate amendment extends the one-time election to taxpayers in situations involving serious handicaps.

**Conference agreement.**—The conference agreement follows the House bill.

## 8. Foreign earned income

**House bill.**—Present law provides a variety of deductions and exclusions for income earned abroad. The House bill modifies the eligibility standards of present law and replaces the present system of deductions for excess living costs with an exclusion of a portion of foreign earned income. The *bona fide* residence test remains in its present form. However, an individual also is eligible for the special provisions if he is present in a foreign country or countries for 330 full days in any period of 12 consecutive months (rather than 510 days in any period of 18 consecutive months as under present law). Individuals meeting these requirements generally may elect to exclude foreign earned income attributable to the period of foreign residence or presence at an annual rate for taxable years beginning on or after January 1, 1982, of \$75,000. This amount is increased \$5,000 a year over the next four years to \$95,000. Thus, at the end of the phase-in period a taxpayer will be able to exclude up to \$95,000. In the case of a married couple, the exemption is computed separately for each qualifying individual. The definition of earned income is identical to present law.

Once a taxpayer has elected to exclude foreign earned income the election remains in effect for that year and all future years. The election may be revoked with the consent of the Commissioner. In addition the election may be revoked by the taxpayer without consent. However, if the election is revoked without consent, the taxpayer cannot again elect until the sixth taxable year following the taxable year for which the revocation was made.

If a taxpayer who elects to exclude foreign earned income becomes a resident of the United States and then, a number of years later, moves abroad again, the election remains in effect. Accordingly, that individual would not have to reelect the exclusion for that later year. If that individual does not want to be subject to the exclusion, he would have to revoke the election and would be barred from reelecting the exclusion for five years. However, the Commissioner might, in determining whether to consent to a revocation of the election, take into account U.S. residence for a period of a number of years.

In addition to the exclusion described above, an individual may elect to exclude a portion of his income or, in the case of housing amounts not provided by an employer, elect to deduct an amount for housing, based on his housing expenses. This exclusion is equal to the excess of the taxpayer's "housing expenses" over a base housing amount. The term "housing expenses" means the reasonable expenses paid or incurred during the taxable year by, or on behalf of, the individual for housing for the individual (and for his spouse and dependents, if they reside with him) in a foreign country. The term includes expenses attributable to the housing, such as utilities and insurance, but does not include interest and taxes, which are separately deductible. If the taxpayer maintains a second household outside the United States for his spouse and dependents who do not reside with him because of adverse living conditions, then the housing expenses of the second household also are eligible for the exclusion. Housing expenses are not treated as reasonable to the extent they are lavish or extravagant under the circumstances.

The base housing amount is 16 percent of the salary of an employee of the United States whose salary grade is step 1 of grade GS-14. Currently, this salary is \$37,871 so the current base housing amount would be \$6,059.

Housing costs attributable to amounts provided by an employer of the individual in the course of his employment are excluded from gross income of the employee. Amounts not attributed to an employer are to be allowed as a deduction in computing adjusted gross income of the employee. The amount of the deduction is limited, subject to a special carryover rule, to the foreign earned income of the individual which is not otherwise excluded from gross income under this provision. For example, if an individual who is not an employee has foreign earned income in 1982 of \$100,000 and qualifying housing expenses in excess of the base amount of \$20,000, the individual may elect and then deduct \$75,000 under the general exclusion plus \$20,000 for the excess housing cost exclusion. If, however, that individual had no foreign earned income for the year, then he could not deduct any amount attributable to the housing expenses for the year. However, the special carryover rule may allow the individual to deduct all or a portion of his unused housing expenses in the next taxable year.

The bill provides that an individual who is not an employee and who qualifies for the foreign earned income exclusion, but who has housing expenses in excess of earned income for a year can carry those expenses forward only to the next taxable year and deduct them in that year subject to the limitation in the next year. In determining how much of the carried forward housing expenses could be used in that next year the carried over amounts could be used only after the housing expenses incurred in that year.<sup>1</sup>

Deductions and credits attributable to excluded income are not allowed. For example, foreign taxes paid on excluded income may not be credited against U.S. taxes.

As under present law, pensions, and annuities, and income from certain trusts are not excludable.

The bill extends the benefits of the exclusion to individuals who receive compensation from the U.S. or any agency thereof, but who are not employees of the U.S. or any agency thereof. Thus, for example, the bill extends the exclusion to certain overseas independent contractors and teachers at certain schools for U.S. dependents who are not employees of the U.S. or any agency thereof.

The bill retains with certain modifications the present rule that in the case of an individual who is furnished lodging in a camp located in a foreign country by or on behalf of his employer the camp shall be considered part of the business premises of the employer for purposes of section 119, relating to the exclusion from income of the value of meals and lodging furnished by the employer. To qualify as a camp, the lodging must be furnished for the convenience of the employer because the place at which the services are rendered in a remote area where satisfactory housing is not otherwise available on the open market. The lodging must also be located, as near

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<sup>1</sup> For example, assume that A, a U.S. citizen, is a bona fide resident of a foreign country for all of 1983. The citizen has no foreign earned income and his housing cost amount (his foreign housing expenses over the base amount) is \$30,000. A gets no deduction for housing costs in 1983. In 1984 A has foreign earned income of \$150,000 and his housing cost amount is again \$30,000. A would be entitled to an exclusion of \$85,000 plus a deduction of his \$30,000 housing cost amount paid in 1984. In addition, A would be permitted to deduct the \$30,000 of his unused housing costs carried over from 1983.

as practicable, in the vicinity of the site at which the individual performs the services and must also be in a common area, or enclave, which is not available to the public and which normally accommodates 10 or more employees. This provision differs from present law primarily in that the camp does not have to be in a hardship area and need not constitute substandard lodging.

The bill retains the present rules under which an individual is allowed pro rata benefits in certain cases where civil unrest or similar adverse conditions require an individual to leave the foreign country before meeting the time requirements.

The bill authorizes the Secretary of the Treasury to issue such regulations as may be necessary or appropriate to carry out the purposes of this provisions, including regulations providing rules for cases in which both spouses have foreign earned income or file separate returns.

The present rule extending the period within which capital gain on the sale of a principal residence must be rolled over to qualify for exemption from tax is retained.

The provision does not affect the treatment of amounts received since December 31, 1962, which are attributable to services performed on or before December 31, 1962, and with respect to which there existed on March 12, 1962, a right (whether forfeitable or nonforfeitable) to receive such amounts. Accordingly, these amounts will continue (as they have since 1962) to be subject to section 911 as in effect before amendment by the Revenue Act of 1962.

Finally, the provision of the Foreign Earned Income Act of 1978 requiring the Secretary of report biannually to the Congress on the operation and effects of sections 911 and 912 is changed to require the report as soon as practicable after enactment and each fourth calendar year thereafter.

**Senate amendment.**—The Senate amendment is the same as the House bill except that the foreign earned income excluded is the first \$50,000 plus one-half of the next \$50,000, the election is annual, and the housing exclusion is not limited to earned income.

**Conference agreement.**—The conference agreement follows the House bill.

## B. Capital Cost Recovery Provisions

### 9. Capital cost recovery provisions—general concept

**House bill.**—Present law is designed to allocate depreciation deductions over the period the asset is used in business so that deductions for the cost of an asset are matched with the income produced by the asset.

Under the House bill, the present law Asset Depreciation Range (ADR) system is terminated for recovery property placed in service after December 31, 1980, and replaced with the Accelerated Cost Recovery System (ACRS). Under ACRS, the cost of an asset is recovered over a predetermined period shorter than the useful life of the asset or the period the asset is used to produce income.

**Senate amendment.**—The Senate amendment is the same as the House bill.

**Conference agreement.**—The conference agreement follows the House bill and Senate amendment. To make clear that the repair allowance rules under the ADR system do not apply to recovery property, the conference agreement provides for the repeal of section 263(e).

### 10. Eligible property

**House bill.**—Under present law, assets used in a trade or business or for the production of income are depreciable if they are subject to wear and tear, decay or decline from natural causes or obsolescence. Assets that do not decline in value on a predictable basis or that do not have a determinable useful life, such as land, goodwill, and stock, are not depreciable.

Under the House bill, most tangible depreciable property (real and personal) is covered by the accelerated cost recovery system (ACRS). However, ACRS does not apply to (1) property not depreciated in terms of years (except certain railroad property), and (2) property amortized (e.g., leasehold improvements and low-income rehabilitation expenditures).

**Senate amendment.**—The Senate amendment is the same as the House bill, except all racehorses and other horses over 11 years old are not eligible property. Thus, excluded horses are subject to present law rules. The useful life for an excluded racehorse will be determined on the basis of all facts and circumstances. The useful life for other horses over 11 years old will be determined under the ADR system.

**Conference agreement.**—In general, the conference agreement follows the House bill and Senate amendment. However, under the conference agreement, all horses are eligible for ACRS.

### 11. Useful lives and methods

#### a. Personal property useful lives and methods

**House bill.**—Under present law, a principal method used to determine useful lives for personal property is the Asset Depreciation Range (ADR) system.

Under the ADR system, the Treasury, on the Basis of actual industry experience, specifies a midpoint life for equipment used in most industries. Taxpayers may elect lives 20 percent longer or shorter than the midpoint life. ADR midpoint lives for equipment range from 2.5 years for certain special manufacturing tools to 50 years for certain public utility equipment.

For assets not eligible for ADR and for taxpayers who do not elect ADR, useful lives are determined according to the facts and circumstances pertaining to each asset or by agreement between the taxpayer and the IRS.

The House bill provides that eligible personal property (and certain real property) is recovered over 3, 5, 10, or 15 years. The classification of property by recovery period is as follows:

3 years .....	Autos, light-duty trucks, R&D equipment and personal property with an ADR midpoint life of 4 years or less.
5 years .....	Most other equipment except long-lived public utility property. Also includes single purpose agricultural structures and petroleum storage facilities, which are designated as section 1245 property under the bill.
10 years .....	Public utility property with an ADR midpoint life greater than 18 but not greater than 25 years; railroad tank cars; and real property with an ADR midpoint life of 12.5 years or less (e.g., theme park structures).
15 years .....	Public utility property with an ADR midpoint life exceeding 25 years.

Under a flexibility provision, taxpayers may elect to use one of two longer recovery periods as set forth below:

*Optional periods*

Property:

3-year property .....	5 and 12 years
5-year property .....	12 and 25 years
10-year property .....	25 and 35 years
15-year property .....	35 and 45 years.

Under present law, taxpayers may use the straight-line method, a declining balance method at a rate up to 200-percent of the straight-line rate, or the sum of the years-digits method with respect to new personal property. For used personal property, taxpayers may use either the straight-line method or a declining balance method at a rate up to 150-percent of the straight-line rate.

Under the House bill, taxpayers have the option to use the straight-line method over the regular or optional longer recovery period or a prescribed accelerated method over the regular recovery period. The prescribed accelerated method for property placed in service in the following years is based on depreciation methods as set forth below, using a half-year convention and no salvage value limitation:

*Prescribed method*

Year property placed in service:

1981-1984 .....	150 percent declining balance, changing to straight-line
1985 .....	175 percent declining balance, changing to SYD

*Prescribed method*

After 1985 ..... 200 percent declining balance changing to SYD.

**Senate amendment.**—The Senate amendment is generally the same as the House bill, except residential, manufactured homes and certain public utility property are included in the 10-year class and certain pollution control equipment is included in the 3-year class. Residential mobile homes that are section 1250 property are included in the 10-year class instead of the 15-year real property class. Electric utility coal-fired burners and boilers that either replace, or are conversions of, oil- or gas-fired burners or boilers are included in the 10-year class instead of the 15-year public utility property class. Related equipment necessary to convert such burners or boilers to coal use, such as fuel-handling equipment, are also included in the 10-year class. Replacement and converted coal-fired burners and boilers (and related conversion equipment) used in a major fuel-burning installation are included in the 10-year class to the extent such equipment is not otherwise 3-year, 5-year, or 10-year property. Qualified pollution control equipment is in the 3-year class if installed in connection with coal-fired burners and boilers that are replacements or conversions of burners or boilers in electric utility powerplants and major fuel-burning installations.

**Conference agreement.**—The conference agreement generally follows the House bill and Senate amendment, except with respect to the treatment of horses and coal utilization property. Residential manufactured homes that are section 1250 property are included in the 10-year class. Race horses over 2 years old when placed in service by the taxpayer and other horses over 12 years old when placed in service by the taxpayer are included in the 3-year class. Other horses are included in the 5-year class. Qualified pollution control equipment related to coal utilization property is not included in the 3-year class. Such property, to the extent it is not amortized under section 169, is included in the 5-year class or 15-year public utility property class, depending on whether such property is public utility property. Burners and boilers using coal (including lignite) as a primary fuel (and related necessary equipment) that either replace or are conversions of oil- or gas-fired burners or boilers are included in the 10-year class only if such equipment is used in an public utility powerplant.

### ***b. Real property***

**House bill.**—Present IRS guideline lives range from 40 to 60 years for real property, but actual lives claimed under a facts and circumstances approach may be shorter. Non-residential property may be depreciated using a 150 percent declining balance method (if new) or the straight-line method. New residential property may be depreciated using straight-line, the 200 percent declining balance method, or the sum of the years-digits method. Used residential may use up to the 125 percent declining balance method (if 20 years useful life is remaining) or straight-line. Taxpayer may use different lives for each separate component of a building, such as plumbing, wiring, etc. (component depreciation) or use a single life for the building and all components (composite depreciation).



Under the House bill, real property is assigned a 15-year recovery period, but taxpayers may elect a 35- or 45-year extended recovery period.

For all real property, taxpayers have the option to use (1) an accelerated method (200 percent declining balance to straight-line) over the 15-year recovery period, or (2) straight-line over either the 15-year period or the optional extended period chosen. Composite depreciation is required.

**Senate amendment.**—The Senate amendment is the same as the House bill except that (1) residential property other than low-income housing is depreciated using the 150-percent declining balance method, and (2) nonresidential property is depreciated using the 150-percent declining balance method, except that the 175-percent declining balance method applies in 1985–1990.

**Conference agreement.**—The conference agreement follows the House bill and Senate amendment, except that real property other than low-income housing is depreciated using the 175-percent declining balance method, changing to the straight-line method to maximize acceleration.

## 12. Special depreciation for small business

**House bill.**—Under present law, there are no special provisions specifically applicable to the depreciation of assets by a small business. Present law, however, does provide a deduction for “bonus” first-year depreciation in an amount not exceeding 20 percent of the cost of eligible property (sec. 179). The cost of the property that may be taken into account may not exceed \$10,000 (\$20,000 for individuals who file a joint return). Thus, the maximum additional first-year depreciation deduction is limited to \$2,000 (\$4,000 for individuals filing a joint return).

The House bill repeals section 179 and replaces it with an election to immediately deduct (expense) the cost of new or used personal property up to \$5,000 per year in 1982 and 1983, \$7,500 in 1984 and 1985, and \$10,000 in years after 1985.

**Senate amendment.**—The Senate amendment is the same as the House provision.

**Conference agreement.**—The conference agreement follows the House bill and Senate amendment.

## 13. Recapture of depreciation

**House bill.**—Under present law, gain on the disposition of personal property is treated as ordinary income rather than capital gain to the extent of prior depreciation taken (sec. 1245). Gain on the disposition of real property is treated as ordinary income rather than capital gain only to the extent prior depreciation taken exceeds what would have been allowable if straight-line depreciation had been used (sec. 1250). In the case of installment sales of personal and real property, the recognition of any gain realized can be deferred (sec. 453).

Under the House bill, the treatment of personal property is unchanged, except that the recognition of gain cannot be deferred by installment sales treatment to the extent a deduction was taken for the property under the special expensing election. The treatment of residential real property is not changed. The treatment of nonresidential real property is unchanged if the straight-line depreciation method is used. However, for nonresidential real property depreci-

ated under an accelerated method, gain is treated as ordinary income to the extent of all prior depreciation taken.

**Senate amendment.**—The Senate amendment is the same as the House provision.

**Conference agreement.**—The conference agreement follows the House bill and Senate amendment.

#### 14. Flexibility

**House bill.**—Under present law, taxpayers have several options that permit flexibility in computing depreciation deductions and net operating losses. Taxpayers have an option to use a useful life 20 percent shorter or longer than the ADR midpoint life. There is an option to use straight-line or accelerated methods, where allowed. In determining the date of additions to and retirements from a depreciation account, taxpayers have an option to use an averaging convention for personal property. In general, net operating losses and operating losses of certain insurance companies may be carried back three years and forward seven years.

Under the House bill taxpayers have an option to use one of two additional recovery periods that are longer than the recovery period prescribed for each class of property. In addition, taxpayers have an option to use an accelerated or straight-line method over the regular recovery period.

As under the present Treasury regulations for the ADR system, each member of an affiliated group of corporations generally may make its own flexibility elections with respect to property it places in service. However, if the affiliated group files a consolidated tax return, the availability of separate elections will depend on the applicable consolidated return regulations prescribed by the Treasury. The provisions of this bill do not curtail Treasury authority to prescribe consolidated return rules, including those relating to cost recovery elections.

Further, although a transferee of property, in general, may elect a recovery period or method different from that elected by the transferor, appropriate restrictions are imposed to prevent the use of asset transfers as a mechanism to change the recovery period or method for property acquired in an intercompany transfer from another member of an affiliated group or in certain other related party transfers and nonrecognition transactions. For transfers subject to these restrictions, the transferee must “step into the shoes” of the transferor with respect to the recovery period and method of the transferred property. This rule applies only to the extent the basis in the transferee’s hands equals the transferor’s adjusted basis. For example, assume the transferor elected to use a 12-year life for 5-year property and the straight-line method. Assume also that the transfer occurred 5 years after the property was placed in service. The transferee must depreciate the property using the straight-line method over the remaining 7 years. Transactions subject to this rule are sale-leasebacks and transfers between other related persons as defined in the anti-churning rules and transactions described in section 332 (other than a transaction to which section 334(b)(2) applies), 351, 361, 371(a), 374(a), 721, or 731.

An averaging convention for personal property is built into the proposed recovery percentages. The NOL carry back is extended, in general, to 20 years. However, NOLs of a financial institution are

carried back 10 years and carried forward 5 years as under present law.

**Senate amendment.**—The Senate amendment follows the House bill except the NOL carryover period is extended to 10 years rather than 20 years. In addition, the carryover period for operating losses that receive an 8-year carryover under present law due to the inability of the taxpayer to carry back losses against any year the taxpayer was a real estate investment trust (REIT) is extended from 8 to 11 years. The carryover period for financial institutions remains at 5 years, and the carryover period for Cuban expropriation losses remains at 20 years.

**Conference agreement.**—The conference agreement follows the House bill and Senate amendment, except the NOL carryover period is extended to 15 years. Net operating losses of a financial institution are carried back 10 years and forward 5 years as under present law. The carryover period for Cuban expropriation losses remains at 20 years.

### 15. Earnings and profits

**House bill.**—Distributions by a corporation to its shareholders are taxable as dividends only to the extent the distribution is out of current or accumulated earnings and profits. Earnings and profits for U.S. corporations are computed, under present law, using straight-line depreciation over the useful life of property. The 20-percent ADR useful life variance may be used to determine the useful life for this purpose. Under the House bill, earnings and profits for U.S. corporations are based on straight-line depreciation over extended recovery periods as set forth below:

#### *Extended recovery period*

Property:	<i>Years</i>
3-year property.....	5
5-year property.....	12
10-year property.....	25
15-year property.....	35

If, to compute the recovery deduction under section 168, a taxpayer uses a recovery period longer than the applicable extended recovery period described above, the taxpayer must use such longer period in lieu of the regular extended period to compute earnings and profits. Thus, if a taxpayer elects to use the optional 25-year recovery period to compute the recovery deduction for 5-year property placed in service in a taxable year, the taxpayer must use the 25-year period to compute earnings and profits with respect to such property.

**Senate amendment.**—The Senate amendment is generally the same as the House bill, except the special rule relating to the use of recovery periods longer than the prescribed extended recovery period does not apply.

**Conference agreement.**—The conference agreement generally follows both the House bill and Senate amendment, except a longer recovery period to compute earnings and profits is required if such longer period is used to compute the recovery deduction.

### 16. Depreciation of assets held outside the United States

**House bill.**—Under present law, property used predominantly outside the United States may be depreciated using useful lives

based on facts and circumstances or the guideline lives under the ADR system, but the 20-percent useful life variance may not be used. Accelerated methods of depreciation generally may be used with respect to such property. The investment tax credit generally is not allowed for such property (sec. 48(a)(2)).

The House bill provides that foreign personal property is depreciated using the 200-percent declining balance method, changing to the straight-line method, over the ADR midpoint life in effect for the property on January 1, 1981, or 12 years if no ADR midpoint life is in effect at such time. Taxpayers have the option to use the straight-line method over the regular recovery period (ADR midpoint life or 12 years, whichever is applicable) or an optional recovery period.

Foreign real property is depreciated over 35 years using the 150-percent declining balance method, changing to the straight-line method. Taxpayers have the option to use the straight-line method over 35 or 45 years.

**Senate amendment.**—The Senate amendment is generally the same as the House bill, except the definition of railroad rolling stock that is considered a foreign asset is changed. Under present law, property used outside the United States for more than half the taxable year generally is considered a foreign asset. However, railroad rolling stock owned by a U.S. railroad and used both within and without the United States is not considered a foreign asset. Under the Senate amendment, rolling stock leased by a U.S. person and used to and from the United States is not considered a foreign asset. Rolling stock owned by a U.S. railroad and used to and from the United States, rather than within and without the United States, is not considered a foreign asset.

**Conference agreement.**—The conference agreement generally follows the House bill and Senate amendment, except with respect to the railroad rolling stock provisions of the Senate amendment. Under the conference agreement, railroad rolling stock used within and without the United States is not treated as a foreign asset, whether it is owned by a U.S. railroad or is leased by a U.S. person. However, this provision does not apply to rolling stock subject to a long-term lease to a foreign person. Thus, rolling stock leased on a long-term basis and used outside the United States more than half the taxable year is considered a foreign asset unless it is owned by a U.S. railroad.

## 17. Add-on minimum tax and maximum tax

**House bill.**—Under present law, a 15-percent minimum tax is imposed on a portion of a taxpayer's items of tax preference. Accelerated depreciation on leased personal property is an item of tax preference for taxpayers other than corporations (including subchapter S corporations and personal holding companies). Accelerated depreciation on real property is an item of tax preference for all taxpayers. The amount of the preference item is the excess of depreciation taken over what would have been allowable using the straight-line method over the property's useful life (the ADR midpoint life for property depreciated under the ADR system). The taxpayer's total preference items reduce the amount of personal service taxable income that is eligible for the preferential 50-percent maximum tax rate.

Under the House bill, the amount of the tax preference item for accelerated depreciation is the excess of the depreciation taken over the amount that would have been allowable using the straight-line method over prescribed periods as set forth below:

*Prescribed period*

Property:	<i>Years</i>
3-year property.....	5
5-year property.....	8
10-year property.....	15
15-real property.....	15
15-year personal property.....	22

**Senate amendment.**—The Senate amendment is the same as the provision of the House bill.

**Conference agreement.**—The conference agreement follows the House bill and Senate amendment.

## 18. Regular investment credit

### *a. Eligibility*

**House bill.**—The regular investment credit under present law applies to tangible personal property and other tangible property used in connection with manufacturing, production, or certain other activities not including distribution. Petroleum storage facilities are ineligible unless used in connection with production. Property used predominately outside the United States is not eligible. Although there is an exception permitting the credit for railroad rolling stock of a domestic railroad that is used within and without the United States, leased railroad rolling stock used within and without the United States is not eligible.

The House bill adds to eligible property facilities used for storage of petroleum and its primary products, even if used in connection with distribution. Primary products of petroleum means the primary products of oil as defined under the DISC regulations (Treas. Reg. § 1.993-3(g)(3)(i)).

**Senate amendment.**—The Senate amendment is the same as the House bill, except leased railroad rolling stock of a U.S. person used to and from the U.S. is added to eligible property. Also, the present law exception, which applies to rolling stock of a domestic railroad used “within and without” the United States, is modified so that it applies only to rolling stock used “to and from” the United States.

**Conference agreement.**—The conference agreement follows the House bill and Senate amendment, except with respect to the Senate provision for railroad rolling stock. The conference agreement adds to eligible property railroad rolling stock that is leased by a U.S. person and used within and without the United States, and retains the present law “within and without” exception for rolling stock of a domestic railroad. Leased railroad property is not eligible if it is leased on a long-term basis to a foreign person.

### *b. Amount of credit*

**House bill.**—Under present law, the amount of regular credit is determined as follows:

Estimated useful life (years):	<i>Credit (percent)</i>
Less than 3.....	0
3-4.....	3½

5-6.....	6 $\frac{2}{3}$
7 or more.....	10

Under the house bill, the regular credit amount is as follows:

Recovery period (years):	Credit (percent)
3.....	6
5, 10 and 15.....	10

**Senate amendment.**—The Senate amendment is the same as the House bill.

**Conference agreement.**—The conference agreement follows the House bill and Senate amendment.

#### **c. Used property limitation**

**House bill.**—Under present law, only \$100,000 of used property is eligible for the investment credit.

The House bill raises the limitation to \$125,000 in 1981 and to \$150,000 in 1985.

**Senate amendment.**—The Senate amendment is the same as the House bill.

**Conference agreement.**—The conference agreement follows the House bill and Senate amendment.

#### **d. Recapture of credit**

**House bill.**—Under present law, the credit is recomputed on early disposition of property as if the actual useful life had been used to determine the amount of credit.

Under the House bill, the credit is recomputed on early disposition by allowing a 2-percent credit for each year the property is held. Thus, no recapture is required for eligible 5-year, 10-year, or 15-year property actually held for at least 5 years, or for eligible 3-year property held for at least 3 years.

**Senate amendment.**—The Senate amendment is the same as the House bill.

**Conference agreement.**—The conference agreement follows the House bill and Senate amendment.

#### **e. Carryover of credit**

**House bill.**—Under present law, unused investment credits may be carried back 3 years and forward 7 years.

The House bill extends the carryover period to 20 years.

**Senate amendment.**—The Senate amendment extends the carryover period to 10 years.

**Conference agreement.**—The conference agreement extends the carryover period to 15 years.

### **19. Normalization rules for public utility property**

**House bill.**—Under present law, a public utility may use an accelerated depreciation method only if it also uses a normalization method of accounting, unless the company used flow-through accounting for accelerated depreciation in 1969. A public utility that must normalize accelerated depreciation may use the ADR system only if it normalizes certain differences between the ADR useful life and the ratemaking useful life of eligible property. Similarly, a utility that must normalize accelerated depreciation must normalize the investment tax credit. In addition, some utilities not required to normalize accelerated depreciation are required to normalize all or part of the investment credit.

Under the House bill, except as provided in relevant transition rules, normalization of accelerated depreciation, useful lives, and the investment credit is mandatory for all public utilities with respect to property depreciated under ACRS. Under transition rules, taxpayers are considered to satisfy the new normalization requirements for depreciation or the investment credit under a rate order that complies with the present law requirements if (1) the rate order was put into effect before the date of enactment of the Act and will expire by its terms, and (2) a superseding rate order is put into effect complying with the new applicable normalization requirement.

**Senate amendment.**—The Senate amendment provides normalization provisions that generally are the same as the provisions of the House bill. The Senate amendment does not provide a transition rule relating to the investment credit normalization rules. The Senate amendment contains a provision giving the Secretary authority, until Congress takes further action, to prescribe any regulations necessary or appropriate to determine whether the new depreciation normalization requirements have been met.

**Conference agreement.**—The conference agreement generally follows the House bill and Senate amendment with certain technical modifications to the transition rules. Under the conference agreement, normalization of the investment credit is mandatory but a transition rule for investment credit normalization is provided. Also the Secretary is given authority to prescribe regulations relating to the new depreciation normalization rules.

## 20. Investment credit at-risk limitation

**House bill.**—Under present law, there is no at-risk limitation on the allowance of investment credits. Under the House bill, the allowance of investment credits is subject to an at-risk limitation. The limitation applies to business activities, the losses from which are subject to limitation under the at-risk rules of section 465, engaged in by individuals, subchapter S corporations, and certain closely held corporations. The investment credit is not allowed with respect to amounts invested in qualifying property to the extent the invested amounts are not at risk, within the meaning of section 465(b) (without regard to subsection (b)(5)). An exception is provided for certain direct or guaranteed governmental loans and certain amounts borrowed from banks, savings and loan institutions, credit unions, or insurance companies. These amounts owed to qualified lenders are considered at risk even if the taxpayer is not personally required to repay the debt.

**Senate amendment.**—The Senate amendment is generally the same as the House bill, except that the exception for certain qualified lenders is expanded to include independent third party lenders, and an exception is added for seller financing in certain investments in energy property. The Senate amendment modifies the exception for qualified lenders by adding a minimum 20-percent at-risk investment requirement (determined without regard to the qualified lender exception), by requiring that the borrower and the seller or manufacturer of the property be unrelated, and by adding to the list of qualified lenders pension trusts and unrelated third parties engaged in the business of loaning money.

As under the House provision, a qualified lender may not be the person from which the taxpayer acquires the eligible property (or a

person related to such supplier) nor a person who receives a fee with respect to the taxpayer's investment (or a person related to such promoter). For purposes of determining whether a pension trust or commercial lender is related to the taxpayer, the supplier, or the promoter, a special additional related party rule is provided. Under the special additional related party rule the rules of section 267(b) and 707(b)(1) are applied, except that "more than 0 percent" is substituted for "more than 50 percent."

As under current law, the substance of a transaction rather than its form will govern whether it will be characterized as a loan, a lease, or a sale.

The Senate amendment also contains a safe harbor rule for certain loans related to certain energy property. Amounts borrowed with respect to these types of property would be considered, under certain circumstances, at risk, even though such amounts are not otherwise considered at risk under the bill. In order to qualify under the safe harbor, the taxpayer must have an investment in the property that is at risk with respect to at least 25 percent of the unadjusted basis of the property (determined without regard to any safe harbor rules). In addition, any nonrecourse financing for the property (other than financing by a qualified lender that is considered at risk) must be a level payment loan. A level payment loan is a loan repaid in substantially equal installments including both principal and interest.

If the taxpayer does not make adequate repayments of loan principal, some of the credit allowed will be recaptured, and additional interest added to the increase in tax, determined as if the increase in tax were for the taxable year in which the property was placed in service. The determination of whether the taxpayer has made the requisite repayments of loan principal is made at the end of the second taxable year following the year the property was placed in service and each succeeding year. Generally, credits are recaptured to the extent they are attributable to any principal payments that have not been made under the level payment loan standard. If the amount of principal payments not made under this standard is equal to or greater than the total principal payments under this standard for the most recent 5-taxable-year period, full recapture, attributable to both the deficiency of required principal payments and all future required principal payments will be triggered. If the property is disposed of before the loan is repaid, the credit is recaptured on the basis of the outstanding principal not paid in cash on the date of disposition.

This safe harbor only applies so long as the energy tax credit is in effect.

**Conference agreement.**—The conference agreement follows the Senate amendment.

## 21. Qualified progress and expenditures

**House bill.**—The investment credit is available for qualified progress expenditures made for property with a 2-year normal construction period and at least a 7-year useful life.

The House bill repeals the 7-year useful life requirement. Thus, the amount of credit allowed with respect to progress expenditures will be determined in accordance with the recovery period the taxpayer expects the property to have when the property is placed in service. For example, a full 10 percent credit will be allowed for



progress expenditure property that the taxpayer anticipates will be in the 10-year class when the property is placed in service.

The provision applies to progress expenditures made after December 31, 1980.

**Senate amendment.**—The Senate amendment is the same as the House bill.

**Conference agreement.**—The conference agreement follows the House bill and Senate amendment.

## 22. Leasing

**House bill.**—Under present IRS guidelines, a transaction is characterized as a lease if (1) the lessor's minimum at-risk investment in the property throughout the lease term is 20 percent of cost; (2) the lessor has a positive cash flow and a profit from the lease independent of tax benefits; (3) the lessee does not have a right to purchase the property at less than fair market value; (4) the lessee does not have an investment in the lease and does not lend any of the purchase costs of the owner, and (5) use of the property at the end of the lease term by a person other than the lessee must be commercially feasible.

The House bill creates a safe harbor that guarantees that a transaction will be characterized as a lease for purposes of allowing investment credits and cost recovery allowances to the nominal lessor. To come within the safe harbor, both the lessor and the lessee must affirmatively elect to treat the lessor as the owner of the property. The lessor must be a corporation, a partnership of corporations, or a grantor trust, the grantor and beneficiaries of which are all corporations. At all times during the term of the lease and at the time that the property is placed in service, the lessor must have a minimum "at-risk" investment of not less than 10 percent of the adjusted basis of the property. In addition, the term of the lease (including all extensions) cannot exceed the greater of (1) 90 percent of the useful life of the property under section 167 or (2) 150 percent of the present class life (ADR midpoint as of January 1, 1981).

Only property that is new section 38 property (or certain qualified mass commuting vehicles) may come within the safe harbor rules. The leased property must be leased within 3 months after its acquisition or, in the case of a sale-leaseback transaction, it must be purchased by the lessor within 3 months of the lessee's acquisition for a purchase price that does not exceed the adjusted basis of the property in the hands of the lessee at the time of the lessor's purchase. It is anticipated that the Secretary of the Treasury may prescribe regulations under which property which is part of a facility may not be deemed placed in service until the entire facility is placed in service in order to make the leasing rules available with respect to the entire facility.

If a transaction meets the above requirements, the transaction will be treated as a lease and the parties of the transaction will be treated as lessor and lessee as stipulated in their agreement. The following factors will therefore not be taken into account in determining whether a transaction is a lease:

- (1) whether the lessor or lessee must take the tax benefits into account in order to make a profit from the transaction;
- (2) the fact that the lessee is the nominal owner of the property for state or local law purposes (e.g., has title to the proper-

ty) and retains the burdens, benefits, and incidents of ownership (such as payment of taxes and maintenance charges with respect to the property);

(3) whether or not a person other than the lessee may be able to use the property after the lease term;

(4) the fact that the property may (or must) be bought or sold at the end of the lease term at a fixed or determinable price that is more or less than its fair market value at that time;

(5) the fact that the lessee or related party has provided financing or has guaranteed financing for the transaction (other than for the lessor's minimum 10-percent investment); and

(6) the obligation of any person is subject to any contingency or offset agreement.

Also, under the bill, if the obligation of the lessor under the lease agreement is contingent or offset, the basis of the lessor in the qualified lease property includes the amount of that obligation. In addition, in such cases, the gross income of the lessor includes the amount the lessor is to receive under the payment schedule in the agreement, whether or not received, and the lessor shall deduct interest due on such obligation, whether or not paid. The Secretary of the Treasury shall prescribe regulations to insure that such receipts and deduction are reflected in the lessor's income on a ratable basis (except that, with respect to interest deductions, calculations under a level payment mortgage assumption shall be permitted).

**Senate amendment.**—The Senate amendment is the same as the House bill.

**Conference agreement.**—In general, the conference agreement follows the House bill and Senate amendment. However, several clarifications are made. Under the conference agreement, property will qualify if it is leased within three months after the property was placed in service by the lessee. This is intended to prevent the lessee from also claiming cost recovery allowances or credits with respect to the qualified lease property. Also, under the conference agreement, the fact that the lessee used the property within the 3-month period prior to the lease will not deprive the property of its status as new section 38 property of the lessee. The conferees intend no change with respect to the factors that will not be considered in determining whether a transaction is a lease transaction under the safe harbor, even though the list of factors is not contained in the final language. For example, the fact that there is a fixed or determinable price in the agreement does not deprive the transaction of its lease status.

The conferees intend that the amount and timing of cost recovery allowances in the hands of the lessor will be the same as they would have been in the hands of the lessee.

### 23. Effective dates and phase-in provisions

**House bill.**—In general, the capital cost recovery provisions apply to property placed in service after December 31, 1980. Although there is no phase-in period, the most accelerated method of depreciation for personal property is not available until 1986. The rules for extension of the carryover period for operating losses apply for operating losses in taxable years ending after December 31, 1975. The effective dates for extension of the carryover periods for various credits is as follows:

(1) Investment credit and WIN credits.—Unused credit years ending after December 31, 1973.

(2) New employee credit.—Unused credit years ending after December 31, 1976.

(3) Alcohol fuels credit.—Unused credit years ending after September 30, 1980.

The at risk rule for the investment credit applies to property placed in service on or after February 19, 1981, except for property acquired by the taxpayer pursuant to a binding contract entered into on or before that date. A technical amendment to section 46(e) relating to investment credit for non-corporate lessors applies to leases entered into after June 25, 1981.

Special rules are provided to prevent the taxpayer from bringing its property used during 1980 (pre-1981 property) within the system by certain post-1980 transactions (i.e., “churning” transactions). Similar rules are provided to prevent the taxpayer from taking advantage of the increased recovery percentages available after 1984 for its property used before 1985 (pre-1985 property). Under these anti-churning rules ACRS will not apply to personal property in use during 1980 unless the property is transferred after 1980 in a transaction in which the owner and user (if different) change. Also, ACRS does not apply to personal property leased back to a person that owned or used the property during 1980 or to a person related to that person.

ACRS will not apply to real property if (a) the taxpayer or a person related to the taxpayer owned the property during 1980, (b) the property is leased back to a person that owned the property at any time during 1980 or to a person related to that person or (c) the property is acquired in certain like kind exchanges, “rollovers” of low-income housing, involuntary conversions, or repossessions, for property of the taxpayer or a related person owned during 1980.

Special rules apply in determining whether a person will be considered related to the prior owner-user. A subsidiary is not considered a related person if at least 80 percent of its stock was acquired by the taxpayer by purchase after December 31, 1980 in a transaction described in section 334(b)(2).

For real or personal property used in 1980 and transferred to a corporation or partnership in a transaction which the basis is determined by reference to the basis to the transferor (transaction described in sections 332, 351, 361, 371, 374, 721, or 731) ACRS will not apply. In that case, the Secretary shall provide rules similar to those that apply under section 381(c)(6).

**Senate amendment.**—The Senate amendment generally follows the House bill. However, in determining whether a person is related to the taxpayer under the anti-churning rules, the Senate amendment replaces the rule regarding liquidations described in section 334(b)(2) with a rule for any liquidation under section 331. Under the Senate amendment, a person is not related to the taxpayer if that person is a distributing corporation in a complete or partial liquidation to which section 331 applies and the stock of such corporation with respect to which the distribution described in section 331 is being made was acquired by purchase by the taxpayer or by a person related to the taxpayer after December 31, 1980.

**Conference agreement.**—The conference agreement follows the House bill and Senate amendment, with certain exceptions. To

make clear that property (1) owned by the taxpayer and under construction during 1980, and (2) placed in service by the taxpayer after December 31, 1980, is not subject to the anti-churning rules, the property is not treated as owned until it is placed in service. Also, new rules will apply for determining whether a corporation is a related person to the taxpayer. Under the new rules, a corporation is not a related person to the taxpayer if either (1) the person is a distributing corporation in a transaction described in section 334(b)(2)(B) and 80 percent of the stock is acquired by purchase after December 31, 1980, by the taxpayer or a person related to the taxpayer, or (2) if the person is a distributing corporation in a complete liquidation to which section 331(a)(1) applies and 80 percent of the stock of that corporation is acquired by purchase by one or more taxpayers or by persons related to the taxpayer after December 31, 1980.

The provision relating to leased railroad rolling stock applies to taxable years beginning after December 31, 1980. The conference agreement with respect to the effective date of the extension of the carryover period of certain losses and credits follows the House bill and Senate amendment, except the rule extending the NOL carryover period also applies to any NOL deduction taken by a former real estate investment trust (a "former REIT") in taxable years ending after October 8, 1976, with respect to NOLs incurred in taxable years ending after 1972 but only if the principal purpose of the change from a REIT to a former REIT was not to obtain the NOL.

## C. Rehabilitation Expenditures

### 24. Tax credit for rehabilitation expenditures

**House bill.**—Under present law, the 10-percent investment tax credit (and additional energy credit) is available for expenditures to rehabilitate a building that is at least 20 years old. The credit allowed does not reduce the basis of the property for purposes of depreciation. In lieu of the investment credit, the taxpayer may elect with respect to rehabilitation of a certified historic structure to amortize the expenditures over a 60-month period (sec. 191).

Under the House bill, the 10 percent regular investment credit (and the additional energy credit) and the 60-month amortization provision for certified historic rehabilitation expenditures is replaced by a 3-tier investment credit. The credit is 15 percent for structures at least 30 years old, 20 percent for structures at least 40 years old, and 25 percent for certified historic structures. No credit is allowed for rehabilitation of a building less than 30 years old.

The 15- and 20-percent credits are limited, as under present law, to nonresidential buildings. However, the 25-percent credit for certified historic rehabilitation is available for both nonresidential and residential buildings. These credits are available only if the taxpayer elects to use the straight-line method of cost recovery with respect to rehabilitation expenditures. In addition, there must be a substantial rehabilitation of the building to qualify for the credit. A building has been substantially rehabilitated if (1) the rehabilitation expenditures during the 24-month period ending on the last day of the taxable year exceed the greater of (a) the adjusted basis of the property as of the first day of the 24-month period or (b) \$5,000, or (2) if it meets the requirements under (1) by substituting 60 months for 22 months. The 60-month alternative is available only if there is a written set of architectural plans and specifications for all phases of the rehabilitation and a reasonable expectation that all phases of the rehabilitation will be completed.

For rehabilitation credits other than the credit for certified historic rehabilitations, the basis of the property must be reduced by the amount of the credit allowed. If subsequently there is a recapture of the credit, the resulting increase in tax (or adjustment in carrybacks and carryovers) will increase the basis of the building immediately before the recapture event.

No credit is available for a certified historic structure if approval of the rehabilitation is not obtained from the Secretary of Interior.

Also, no credit is available for a certified historic rehabilitation if the taxpayer or a member of the taxpayer's family uses the property for residential purposes.

The House bill treats a building in an historic district as a certified historic structure unless the taxpayer obtains a certification from the Secretary of Interior. This changes the present law rule under which a building in an historic district is not a certified historic district unless the Secretary of Interior takes action to designate the property as being of historic significance to the district.

The provisions generally apply to expenditures made after December 31, 1981. However, a special rule allows a credit under present law rules for buildings that are more than 20 but less than 30 years old, if the rehabilitation began before January 1, 1982.

**Senate amendment.**—The Senate amendment is the same as the House bill, except the restriction related to use by the taxpayer or a family member is deleted.

**Conference agreement.**—The conference agreement follows the Senate amendment, except the present law rule denying investment credit for property leased to tax-exempt organizations (sec. 48(a)(4)) or governmental units (sec. 48(a)(5)) does not apply to the portion of the basis of the building attributable to qualified rehabilitation expenditures. This corrects a clerical error in the enrollment of the Miscellaneous Revenue Act of 1980. Due to the error, this provision was omitted from that Act.

In connection with the investment tax credit for rehabilitation expenditures on a historic structure, Section 212(e) addresses the situation where qualified rehabilitation expenses are incurred before and after January 1, 1982. Where expenditures on a given qualified historic rehabilitation occur both before and after January 1, 1982, before January 1, 1982, expenditures can qualify for either the present ten percent investment tax credit for over-twenty-year-old buildings, or the five-year historic building amortization, while expenditures on or after January 1, 1982, can qualify for the new 25 percent investment tax credit. In other words, a combination of the old and new law is envisaged where the expenditures occur on both sides of January 1, 1982.

## 25. Demolition of historic structures

**House bill.**—Under present law, buildings constructed or reconstructed at the site of a demolished or substantially altered certified historic structure must be depreciated using the straight-line method over its useful life (sec. 167(n)). Demolition costs must be capitalized as part of the basis of land and, thus, may not be deducted as the loss or depreciated. (Sec. 280B.)

Under the House bill, section 167(n) is repealed, but section 280B is retained. The provision applies to expenditures made after December 31, 1981.

**Senate amendment.**—The Senate amendment is the same as the House bill.

**Conference agreement.**—The conference agreement follows the House bill and Senate amendment.

## D. Incentives for Research and Experimentation

### 26. Tax credit for research and experimentation

**House bill.**—Under present law, a taxpayer may elect to deduct currently the amount of research or experimental expenditures incurred in connection with the taxpayer's trade or business, or may elect to amortize certain research costs over a period of 60 months or more (sec. 174). These rules apply to the costs of research conducted by the taxpayer and, in general, to expenses paid for research conducted on behalf of the taxpayer by a research firm, university, etc. Treasury regulations define qualifying expenditures to mean "research and development costs in the experimental or laboratory sense," and provide illustrations of qualifying and nonqualifying expenditures.

The House bill provides a 25-percent tax credit for certain research and experimental expenditures paid in carrying on a trade or business of the taxpayer, but only to the extent that current-year expenditures exceed the average amount of research expenditures in a base period (generally, the preceding three taxable years). Subject to certain exclusions, the bill adopts the definition of research as used for purposes of the special deduction rules under section 174.

Under the House bill, research expenditures qualifying for the new incremental credit consist of (1) "in-house" expenditures for research wages and supplies, plus certain lease or other charges for research use of computers, laboratory equipment, etc.; (2) 65 percent of amounts paid (e.g., to a research firm or university) for contract research; and (3) 65 percent of corporate grants for basic research to be performed by universities or certain scientific research organizations (or of grants to certain funds organized to make basic research grants to universities).

The credit under the House bill applies to research expenditures made after June 30, 1981, and before 1986.

**Senate amendment.**—The tax credit for incremental research expenditures provided under the Senate amendment differs from the credit under the House bill, apart from minor language differences, in the following respects: (1) qualifying research costs, other than wages and supplies, consist of certain lease or other charges for research use of computers (but not for use of other equipment); (2) the amount of contract research expenditures qualifying for the credit is the amount reimbursed by the taxpayer for the costs of research wages, supplies, etc., paid by the person performing the research on the taxpayer's behalf; (3) there is not specific provision making corporate grants for basic research at universities, etc. eligible for the credit (although the credit is available for qualifying contract expenditures for such basic research); (4) the Senate bill does not have a "sunset" provision terminating the credit.

**Conference agreement.**—The conference agreement follows the House bill.

The conferees also agreed to certain interpretations of the rule under the bill that the new credit is available only with regard to qualified research expenditures paid by the taxpayer in carrying on a trade or business of the taxpayer. The "carrying on" test for purposes of the new credit generally is the same as for purposes of section 162. For example, it is intended that to be eligible for the credit, qualified research expenditures must be paid or incurred in

the particular business being carried on by the taxpayer. The conferees also intend that the Treasury will issue regulations, for credit purposes only, which will allow the credit in the case of research joint ventures by taxpayers who otherwise satisfy the "carrying on" test and who are entitled to the research results.

## **27. Charitable contributions of newly manufactured equipment to universities for research**

**House bill.**—Under present law, the amount of charitable deduction for a contribution of appreciated ordinary-income property generally is limited to the amount of the taxpayer's basis in the property. An exception is provided for corporate contributions of certain property for use in the care of the needy, the ill, or infants; in such case, the lesser of 50 percent of appreciation plus basis, or twice the basis, may be deducted.

The House bill allows a deduction equal to the taxpayer's basis plus 50 percent of appreciation (but not to exceed twice the basis) for qualified corporate contributions of newly manufactured ordinary-income property to a college or university for research or experimentation, including research training. This provision applies to qualified contributions made after the date of enactment of the bill.

**Senate amendment.**—The Senate amendment generally is the same as the House bill.<sup>1</sup>

**Conference agreement.**—The conference agreement follows the House bill.

## **28. Rule for allocating research and development expenditures to U.S. source income**

**House bill.**—Regardless of the source of the income generated by such expenditures, all research and experimentation expenditures which are paid or incurred for research conducted in the United States will be allocated and apportioned to income from sources within the United States.

**Senate amendment.**—Like the House bill, the Senate amendment provides that the allocation of all U.S. research and experimentation expenditures are to be allocated or apportioned to U.S. source income for all purposes under the Code. The rule applies only for one year—the taxpayer's first taxable year after the date of enactment.

Treasury is required to study the impact which Treasury regulation § 1.861-8 has on United States domestic research and experimentation activities and on the availability of the foreign tax credit. Treasury must report to the Ways and Means and Finance Committees within six months from the date of enactment.

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<sup>1</sup> The Senate amendment does not include certain requirements (contained in the House bill) for the increased charitable deduction, namely, that the donated property must be scientific equipment or apparatus, that the donee must use the contributed property in the United States, and that the donee's use of the property must be for research in the physical sciences (including physics, chemistry, astronomy, mathematics, and engineering) or biological sciences (including biology and medicine). Also, the Senate amendment provides that subchapter S corporations are ineligible for the new deduction rule, while the House bill also excludes personal holding companies and service organizations.



***Conference agreement.***—The conference agreement follows the Senate amendment except that the allocation or apportionment of U.S. research and experimentation expenditures to U.S. sources will be for the taxpayer's first two taxable years following the date of enactment.

## E. Small Business Provisions

### 29. Accumulated earnings credit

**House bill.**—Under present law, an accumulated earnings tax is imposed on earnings accumulated in a corporation to avoid income tax on the corporation's shareholders. In computing the tax base, a credit (of not less than \$150,000) is allowed for earnings retained for the reasonable needs of the business. The House bill increases the minimum accumulated earnings credit to \$250,000 except for service corporations in health, law, engineering, architecture, accounting, actuarial science, performing arts and consulting. The provision is effective for taxable years beginning after December 31, 1981.

**Senate amendment.**—Same as House bill.

**Conference agreement.**—The conference agreement follows the House bill and Senate amendment.

### 30. Subchapter S corporations

**House bill.**—Under present law, a Subchapter S corporation may not have more than 15 shareholders and generally trusts may not be shareholders. The House bill increases the number of permitted shareholders to 25 and allows "section 678" trusts to be shareholders. In addition certain trusts holding stock for a disabled beneficiary could be a shareholder. The provisions are effective for taxable year ending after December 31, 1981.

**Senate amendment.**—The Senate amendment also increases the shareholder limit to 25 and permits section "678 trusts." In addition, under the amendment, the sole income beneficiary of a trust which distributes all its income currently can elect to be treated as the owner, under section 678, of the stock of any subchapter S corporation held by the trust, and the trust will be eligible as a shareholder of that subchapter S corporation. The income beneficiary must be a U.S. citizen resident, and must be a beneficiary for his life unless the corpus of the trust is to be distributed to the income beneficiary upon termination of the trust. The election under this section may be made retroactive for up to 60 days.

**Conference agreement.**—The conference agreement follows the Senate amendment.

### 31. LIFO inventory and small business accounting

**House bill.**—Under the cash receipts and disbursements method of accounting, taxpayers may currently deduct all expenditures other than those for capital assets. However, if the production, purchase or sale of merchandise is an income producing factor, the taxpayer must use the accrual method of accounting and must keep inventories. Acceptable methods of accounting for inventories include specific identification, average cost, first-in first-out, and last-in first-out ("LIFO").

An approved method of computing LIFO inventories is the dollar-value method. Dollar-value LIFO is an advantageous method of computing LIFO inventories but because of its inherent complexity it is considered by some, especially small businessmen, as unworkable.

Under dollar-value LIFO the taxpayer accounts for his inventory on the basis of a pool of dollars rather than on an item-by-item basis. In general, the pool of dollars is actually measured in terms

of the equivalent dollar value of the inventory in the year the taxpayer first used the dollar-value LIFO method.

Under the House bill, businesses with average gross receipts of less than \$1 million for the 3 years (ending with the taxable year) may elect one inventory pool for purposes of dollar value LIFO inventory accounting. Also, taxpayers electing LIFO will have 3 years (beginning with the year of the election to LIFO) to take back into income inventory writedowns taken in years prior to the year of the LIFO election. The Secretary shall also prescribe regulations providing for the simplification of LIFO inventory accounting through the use of published government indexes.

Also under the House bill, the Secretary of the Treasury is directed to conduct a full and complete study of methods of tax accounting for inventory (including but not limited to the LIFO method and the cash receipts and disbursements method) with a view toward the development of simplified methods. The Secretary is also directed to submit to the Committee on Ways and Means of the House of Representatives and to the Committee on Finance of the Senate a report on this study, together with such recommendations as he deems appropriate, by December 31, 1982.

**Senate amendment.**—The Senate amendment provides that businesses with average gross receipts of less than \$3 million for the 3 years (ending with the taxable year) may elect one inventory pool for purposes of dollar value LIFO inventory accounting. Also taxpayers electing LIFO will have 3 years (beginning with the year of the election to LIFO) to take back into income inventory writedowns taken in years prior to the year of the LIFO election.

As in the House bill, the Secretary is directed to prescribe regulations providing for the simplification LIFO inventory accounting for businesses. However, the regulations will be based on 100 percent of the appropriate components of the Consumer Price Index or Producer's Price Index and will only apply to businesses with average gross receipts for the preceding three years of less than \$3 million. Additionally, taxpayers may elect to use the link-chain or the index method of accounting for dollar-value LIFO inventory without showing that any other method of computing dollar-value LIFO inventory is unsuitable or impractical. Finally, the Treasury Department is required to report to the Congress by June 30, 1982 on the results of a study on LIFO accounting and the use of cash accounting.

**Conference agreement.**—The conference agreement follows the House bill but increases the amount of average gross receipts that a business must have to use a single dollar-value LIFO pool from \$1 million to \$2 million. Also, the provisions regarding the three-year averaging of income relating to inventory writedowns taken in prior years and the use of single dollar-value LIFO pools are effective for the first taxable year beginning after December 31, 1981.

## F. Windfall Profit Tax and Other Energy Provisions

### 32. Windfall profit tax provisions

#### a. *Royalty owners credit and exemption*

**House bill.**—Qualified royalty owners were allowed a credit (or refund) of up to \$1,000 against the windfall profit tax imposed on their royalty oil during calendar year 1980.

The House bill makes the royalty owner credit available for calendar year 1981 and increases it from \$1,000 to \$2,500.

For 1982 and subsequent years, the House bill provides a limited exemption from the windfall profit tax for specified amounts of royalty production. For 1982 through 1984, the exemption is 2 barrels a day; starting in 1985 the exemption is 4 barrels a day.

The House bill also makes technical, administrative, and conforming amendments to the royalty owner provisions, including provisions providing for tax payment and withholding rules to allow royalty owners to receive the benefit of the provision prior to the close of the calendar year, as well as rules to prevent a proliferation of royalty interests.

**Senate amendment.**—The Senate amendment makes the royalty owner credit permanent and increases it to \$2,500. The amendment also provides for similar administrative rules.

**Conference agreement.**—The conference agreement follows the House bill except that in 1985 and subsequent years, the royalty exemption is 3 barrels per day.

#### b. *Producer exemption*

**House bill.**—Stripper oil is oil produced from a property from which the average daily per well production has been 10 barrels or less for any consecutive 12-month period after 1972. Stripper oil is in tier 2 of the windfall profit tax and generally is subject to a 60-percent rate of tax. However, independent producers are eligible for reduced windfall profit tax rates on up to 1,000 barrels a day of tier 1 and tier 2 oil. The reduced rate applicable to an independent producer's tier 2 oil is 30 percent rather than 60 percent.

The House bill exempts from the windfall profit tax, starting in 1983, stripper oil production of independent producers. The House bill also provides that stripper oil cannot qualify for this exemption if it is produced from a stripper well property which has been owned on or after July 23, 1981, by a producer other than an independent producer.

**Senate amendment.**—No provision.

**Conference agreement.**—The conference agreement generally follows the House bill. The conference agreement clarifies, however, that exempt stripper well oil does not include production attributable to an interest in any property which at any time after July 22, 1981, was owned by a person other than an independent producer (within the meaning of Code section 4992(b)(1)).

Because both the exemption and existing law's lower rates for up to 1,000 barrels a day of oil produced by independent producers apply, in part, to tier 2 oil (which includes stripper oil), the conference agreement clarifies that any person's independent producer amount eligible for lower rates is not reduced by the amount to which the exemption applies.

**c. Reduced rate on newly discovered oil**

**House bill.**—Newly discovered oil is taxed at a 30-percent rate on the difference between its removal price and a severance tax adjustment plus a base price of \$16.55 adjusted for grade, quality, location and inflation plus 2 percent.

The House bill reduces the newly discovered oil tax rate from 30 percent to the following rates:

[In percent]

1982.....	27.5
1983.....	25.0
1984.....	22.5
1985.....	20.0
1986 and after.....	15.0

**Senate amendment.**—The Senate amendment is the same as the House bill.

**Conference agreement.**—The conference agreement follows the House bill and the Senate amendment.

**d. Exemption for qualified charities**

**House bill.**—Under present law, oil production attributable to certain qualifying charitable interests is exempt from the windfall profit tax. A charitable organization for the residential placement, care, or treatment of delinquent, dependent, orphaned, neglected, or handicapped children is not within this exemption.

The House bill extends the existing windfall profit tax exemption for specified charitable educational organizations and medical facilities to oil production attributable to economic interests held by charitable organizations, described in Code section 170(c)(2), which are organized and operated primarily for the residential placement, care, or treatment of delinquent, dependent, orphaned, neglected, or handicapped children. To qualify for this exemption, the oil interest must have been held by the organization on January 21, 1980, and at all times thereafter before the last day of the calendar quarter.

If the interest is *not* held by the organization, the exemption may apply if the interest was held by a church for the benefit of the organization and if all the proceeds from the interest were dedicated on January 21, 1980, and at all times thereafter before the close of the calendar quarter, to the qualifying child care organization. These rules are the same as the present rules for qualifying charitable interests.

**Senate amendment.**—Same as the House bill.

**Conference agreement.**—The conference agreement follows the House bill and the Senate amendment.

**33. Percentage depletion on oil and gas**

**House bill.**—Under present law, percentage depletion, which is available only to independent producers and royalty owners, is calculated as a percentage of gross income from each oil and gas property. Under a 1975 amendment, the applicable percentage, which was 22 percent in 1980 and earlier years, is to be reduced to 20 percent in 1981, 18 percent in 1982, 16 percent in 1983, and to 15 percent for 1984 and subsequent years.

The House bill provides that the rate of percentage depletion will remain at 22 percent for 1981 and subsequent years.

**Senate amendment.**—No provision.

**Conference agreement.**—The conference agreement follows the Senate amendment.

#### 34. Tax credit for woodburning stoves

**House bill.**—Under present law, a 15-percent tax credit is available for the first \$2,000 of qualifying expenditures for insulation and other specified energy-conserving items. The credit is available for the installation of specified energy property after April 19, 1977, and before January 1, 1986, with respect to a taxpayer's principal residence, if the residence was substantially completed before April 20, 1977.

The House bill adds to the list of energy conserving items eligible for the credit certain woodburning stoves and furnaces.

**Senate amendment.**—No provision.

**Conference agreement.**—The conference agreement follows the Senate amendment.

#### 35. Production credit for certain gases

**House bill.**—No provision.

**Senate amendment.**—Present law allows a credit for the production of specified alternative fuels, including several types of natural gas which are eligible for incentive prices under the Natural Gas Policy Act of 1978 (NGPA). The credit phases out as the price of uncontrolled domestic oil rises from \$23.50 to \$29.50 a barrel, adjusted for inflation. Because of the phase out based on the price of oil, the credit generally was not available during 1980.

Section 107(d) of the NGPA provides that gas production is not eligible for an incentive price if any special tax provision applies and if the producer does not file a price election with the Federal Energy Regulatory Commission within 30 days of enactment of the special tax provision.

The amendment provides that no production credit is available unless the taxpayer elects it on the appropriate tax return. This has the effect of allowing the producer to elect the incentive price under the NGPA after the 30-day period has elapsed.

The Senate amendment does not change any provision of the NGPA or deal with the FERC's administration of that Act. It is intended, however, that the amendment be administered by Treasury and, to the extent appropriate, by FERC so as to prevent any producer from obtaining the benefits of the production credit and the incentive price.

**Conference agreement.**—The conference agreement follows the Senate amendment.

## G. Corporate Rate Reduction and Other Business Provisions

### 36. Corporate tax rate reductions

**House bill.**—Under present law, the corporate income tax is imposed at the following rates:

Taxable income—	Rate (percent)
Less than \$25,000.....	17
25,000–50,000.....	20
50,000–75,000.....	30
75,000–100,000.....	40
Over \$100,000.....	46

The House bill decreases the tax rates on the two lowest brackets, i.e., those imposing tax on taxable income below \$50,000. The change will go into effect in 1982 and 1983.

The brackets below \$50,000 will be adjusted as follows:

Taxable income—	Rate (percent)
<i>In 1982—</i>	
Less than 25,000.....	16
\$25,000–50,000.....	19
<i>1983 and later years—</i>	
Less than \$25,000.....	15
\$25,000–\$50,000.....	18

**Senate amendment.**—The provision is the same as in the House bill.

**Conference agreement.**—The conference agreement follows the House bill and the Senate amendment.

### 37. Incentive stock options

**House bill.**—Under present law, the taxation of stock options granted by an employer to an employee as compensation is governed by section 83. The value of the option constitutes ordinary income to the employee when granted only if the option itself has a readily ascertainable fair market value at that time. If the option does not have a readily ascertainable value when granted, it does not constitute ordinary income at that time. Instead, when the option is exercised, the difference between the value of the stock at exercise and the option price constitutes ordinary income to the employee. Ordinary income on grant or on exercise of a stock option is treated as personal service income and, hence, generally is taxed at a maximum rate of 50 percent.

An employer who grants a stock option generally is allowed a business expense deduction equal to the amount includible in the employee's income in its corresponding taxable year (sec. 83(h)).

The bill reinstates "restricted stock options," under which there is no tax consequences when a restricted stock option is granted or when the option is exercised, and the employee is generally taxed at capital gains rates when the stock received on exercise of the option is sold. Similarly, no business expense deduction will be allowed to the employer with respect to a restricted stock option.

To receive restricted stock option treatment, the bill provides that the employee must not dispose of the stock within two years after the option is granted, and must hold the stock itself for at least one year. If all requirements other than these holding period rules are met, the tax will be imposed on sale of the stock, but gain

will be treated as ordinary income rather than capital gain, and the employer will be allowed a deduction at that time.

In addition, at the time the option is exercised, the option holder must be an employee either of the company granting the option, a parent or subsidiary of that corporation, or a corporation (or parent or subsidiary of that corporation) which has assumed the option of another corporation as a result of a corporate reorganization, liquidation, etc., or must have been such an employee within three months of the date of exercise (twelve months if the employee is disabled (within the meaning of section 105(d))). This requirement and the holding period requirements are waived in the case of the death of the employee.

For an option to qualify as a "restricted stock option," terms of the option itself must meet the following conditions:

1. The option must by its terms be exercisable within ten years of the date it is granted.

2. The option price must equal or exceed 85 percent of the fair market value of the stock at the time the option is granted.

3. The option by its terms must be nontransferable other than at death and must be exercisable during the employee's lifetime only by the employee.

4. The employee must not, immediately before the option is granted, own stock representing more than ten percent of the voting power or value of all classes of stock of the employer corporation or its parent or subsidiary. However, the stock ownership limitation will be waived if the option price is at least 110 percent of the fair market value (at the time the option is granted) of the stock subject to the option and the option by its terms is not exercisable more than five years from the date it is granted.

5. In the case of a corporation whose stock is tradable on a stock exchange or any over-the-counter market, under the terms of the plan, the aggregate fair market value of the stock (determined at the time of grant of the option) for which any employee may be granted restricted stock options in any calendar year may not exceed \$75,000. Only \$150,000 of prior options can be exercised.

6. The option by its terms is not exercisable while there is outstanding any restricted stock option which was granted to the employee at an earlier time. For this purpose, an option which has not been exercised in full is outstanding for the period which under its initial terms it could have been exercised. Thus, the cancellation of an earlier option will not enable a subsequent option to be exercised any sooner. Also, for this purpose an option is considered to retain its original date of grant even if the terms of the option or the plan are later amended to qualify the option as a restricted stock option.

The bill provides that stock acquired on exercise of the option may be paid for with stock of the corporation (or its parent or subsidiary) granting the option.

The difference between the option price and the fair market value of the stock at the exercise of the option will not be an item of tax preference.

The bill will apply to options granted after May 21, 1976, and exercised after December 31, 1980. However, in the case of an option which was granted on or before January 1, 1981, and which was not a qualified option, the corporation granting the option may



elect (within six months after enactment of the bill) to have the option not be treated as a restricted stock option.

In the case of an option granted after May 21, 1976, and outstanding on the date of enactment, the option terms (or the terms of the plan under which the option was granted) may be changed, to conform to the restricted stock option rules, within one year of the date of enactment of the bill, without the change giving rise to a new option requiring the setting of an option price based on a later valuation rate.

All such changes relate back to the time of granting the original option. For example, if the option price of a ten-year option granted in 1978 is increased during the one year after date of enactment to 85 percent (110 percent, if applicable) of the fair market value of the stock on the date the option was granted in 1978, the price requirement will be met. Likewise, if the term of an option held by a 10-percent shareholder is shortened to five years from the date the option was granted, the 10-percent stock ownership limitation will not apply.

Any restricted stock option must meet the requirements of new section 424(b)(5), limiting the amount of options which may be granted to an employee to \$75,000 per year (determined at time of grant). In the case of options outstanding on date of enactment granted under a plan (or plans) providing for the granting of more than \$75,000 of options per year, the employer may amend the plan to specify that only certain options under the plan (up to \$75,000 granted per year) will be treated as restricted stock options.

**Senate amendment.**—The amendment provides for “incentive stock options,” which will be taxed in a manner similar to the tax treatment previously applied to restricted and qualified stock options. That is, there will be no tax consequences when an incentive stock option is granted or when the option is exercised, and the employee will be taxed at capital gains rates when the stock received on exercise of the option is sold. Similarly, no business expense deduction will be allowed to the employer with respect to an incentive stock option.

The term “incentive stock option” means an option granted to an individual, for any reason connected with his or her employment, by the employer corporation or by a parent or subsidiary corporation of the employer corporation, to purchase stock of any of such corporations.

To receive incentive stock option treatment, the amendment provides that the employee must not dispose of the stock within two years after the option is granted, and must hold the stock itself for at least one year. If all requirements other than these holding period rules are met, the tax will be imposed on sale of the stock, but gain will be treated as ordinary income rather than capital gain, and the employer will be allowed a deduction at that time.

In addition, for the entire time from the date of granting the option until three months before the date of exercise, the option holder must be an employee either of the company granting the option, a parent or subsidiary of that corporation, or a corporation (or parent or subsidiary of that corporation) which has assumed the option of another corporation as a result of a corporate reorganization, liquidation, etc. This requirement and the holding period requirements are waived in the case of the death of the employee.

For an option to qualify as an "incentive stock option," terms of the option itself must meet the following conditions:

1. The option must be granted under a plan specifying the number of shares of stock to be issued and the employees or class of employees to receive the options. This plan must be approved by the stockholders of the corporation within 12 months before or after the plan is adopted.

2. The option must be granted within ten years of the date the plan is adopted or the date the plan is approved by the stockholders, which ever is earlier.

3. The option must by its terms be exercisable only within 20 years of the date it is granted.

4. The option price must equal or exceed the fair market value of the stock at the time the option is granted. This requirement will be deemed satisfied if there has been a good faith attempt to value the stock accurately, even if the option price is less than the stock value.

5. The option by its terms must be nontransferable other than at death and must be exercisable during the employee's lifetime only by the employee.

6. The employee must not, immediately before the option is granted, own stock representing more than ten percent of the voting power or value of all classes of stock of the employer corporation or its parent or subsidiary. However, the stock ownership limitation will be waived if the option price is at least 110 percent of the fair market value (at the time the option is granted) of the stock subject to the option and the option by its terms is not exercisable more than five years from the date it is granted.

7. The option by its terms is not to be exercisable while there is outstanding any incentive stock option which was granted to the employee at an earlier time. For this purpose, an option which has not been exercised in full is outstanding for the period which under its initial terms it could have been exercised. Thus, the cancellation of an earlier option will not enable a subsequent option to be exercised any sooner. Also, for this purpose an option is considered to retain its original date of grant even if the terms of the option or the plan are later amended to qualify the option as an incentive stock option.

The amendment provides that stock acquired on exercise of the option may be paid for with stock of the corporation granting the option.

The difference between the option price and the fair market value of the stock at the exercise of the option will not be an item of tax preference.

Also, under the amendment, any option which was a qualified stock option or restricted stock option under prior law will become an incentive stock option, if it was not exercised before January 1, 1981, and if it otherwise satisfies requirements for incentive stock options. Such an option will not be subject to the minimum tax.

An option will not be disqualified because of the inclusion of any condition not inconsistent with the qualification requirements, nor because the corporation may make a cash payment to the employee at the time of exercise.

The amendment generally applies to options exercised or granted after December 31, 1980, or outstanding on such date. However, in the case of an option which was granted on or before December 31,

1980, the corporation granting the option must elect to have the option treated as an incentive stock option. Only \$50,000 of stock may be purchased with restricted options granted in any year prior to 1981, and only \$250,000 of stock from such options could be purchased in the aggregate.

In the case of an option granted before 1982, the modification or deletion of any stock appreciation right or right to receive cash payments to permit the option to qualify as an incentive stock option can be made within one year of the enactment of the bill without the modification being treated as the grant of a new option.

In addition, the terms of a stock option plan or an option issued before 1982 can be modified to conform to the incentive stock option rules within one year of the date of enactment of the bill, without the modification being considered as giving rise to a new option requiring a new option price.

**Conference agreement.**—The agreement generally follows the Senate amendment except—

(1) the term of the option may not exceed 10 years from the date of grant,

(2) a disabled employee has 12 months after leaving employment to exercise the option,

(3) the amendment clarifies that additional cash or other property may be transferred to the employee at the time the option is exercised, so long as such property is subject to inclusion in income under the provisions of section 83,

(4) the managers wish to clarify that alternative rights may be granted, so long as no alternative options to purchase stock are granted which cause the option to violate the terms of section 422A(b), and

(5) in the case of options granted after 1980, the terms of the plan must limit the amount of aggregate fair market value of the stock (determined at the time of the grant of the option) for which any employee may be granted incentive stock options in any calendar year to not more than \$100,000 plus the carryover amount. The carryover amount from any year is one-half of the amount by which \$100,000 exceeds the value (at time of grant) of the stock for which incentive stock options were granted in such prior year. Amounts may be carried over 3 years. Options granted in any year use up the \$100,000 current year limitation first and then the carryover from earliest year.

The agreement will apply to options granted after January 1, 1976, and exercised after December 31, 1980, or outstanding on such later date.

However, in the case of options granted before January 1, 1981, an option is an incentive stock option only if the employer elects such treatment for an option. The aggregate value (determined at time of grant) of stock for which any employee may be granted incentive stock options prior to 1981 shall not exceed \$50,000 per calendar year and \$200,000 in the aggregate.

In the case of an option granted after January 1, 1976, and outstanding on the date of enactment, the option terms (or the terms of the plan under which the option was granted or shareholder approval) may be changed, to conform to the incentive stock option rules, within one year of the date of enactment, without the change

giving rise to a new option requiring the setting of an option price based on a later valuation date.

All such changes relate back to the time of granting the original option. For example, if the option price of a ten-year option granted in 1978 is increased during the one year after date of enactment to 100 percent (110 percent, if applicable) of the fair market value of the stock on the date the option was granted in 1978, the price requirement will be met. Likewise, if the term of an option held by a 10-percent shareholder is shortened to five years from the date the option was granted, the 10-percent stock ownership limitation will not apply.

### 38. Extension and modification of targeted jobs tax credit

*House bill.*—Under present law, the targeted jobs tax credit, which applies to eligible trade or business wages paid before January 1, 1982, is available on an elective basis for hiring individuals from one or more of seven target groups. In general, the credit is equal to 50 percent of the first \$6,000 of first-year wages and 25 percent of the first \$6,000 of second-year wages. Qualified first-year wages are limited to 30 percent of FUTA wages (the first \$6,000 per calendar year) for all employees.

In the case of trade or business employment, taxpayers are allowed a WIN tax credit equal to 50 percent of qualified first-year wages and 25 percent of qualified second-year wages paid to WIN registrants and AFDC recipients. For employment other than in a trade or business, the credit is 35 percent of qualified first-year wages.

The House bill extends and modifies the targeted jobs credit as follows:

*Extension and eligible wages.*—The bill provides that credit is available for wages paid or incurred before January 1, 1984. The provision limiting qualified first-year wages to 30 percent of FUTA wages is repealed.

*Targeted groups.*—AFDC recipients and WIN registrants are added as a targeted group, and the WIN credit is terminated. Eligible cooperative education students are limited to those who are economically disadvantaged, effective for wages paid after December 31, 1981. The age limitation for Vietnam veterans (under age 35) is eliminated, and employees laid off from public service employment funded by CETA are made eligible for the credit.

*Changes in certification requirements.*—Certifications issued or requested after the individual begins work are invalid, effective for individuals who begin work after the date of enactment; certifications that individuals are members of economically disadvantaged families are valid for a minimum of 45 days; and certification and marketing are to be performed by State employment security agencies.

*Hiring of relatives.*—The credit is denied for hiring relatives of the employer.

*Authorization for administrative expenses.*—No provision.

*Senate amendment.*—The Senate amendment has the following provisions:

*Extension and eligible wages.*—The Senate amendment provides that full credit is available for targeted employees who begin work before January 1, 1983. For cooperative education students, qualified first-year wages are limited to \$3,000, and qualified second-

year wages are limited to \$1,500. Qualified first-year wages may be at least \$25,000, regardless of the 30-percent FUTA wage cap.

*Targeted groups.*—Same as House bill, except cooperative education students are not limited to those who are economically disadvantaged, and general assistance and Supplemental Security Income recipients are not removed as targeted group.

*Changes in certification requirements.*—Same as House bill, except (1) requirement for certification before the employee begins work applies to individuals who begin work after July 23, 1981, or with respect to whom the employer has not received a certification by this date, (2) the credit is not allowed for rehires, and (3) certifications based on false information provided by the employee are revoked prospectively.

*Hiring of relatives.*—Same as the House bill.

*Authorization for administrative expenses.*—For fiscal year 1982, \$30 million of appropriations is authorized for program administration, of which \$5 million is to be used for a quality program.

*Conference agreement.*—The conference agreement is as follows:

*Extension and eligible wages.*—The conference agreement provides that full credit is available for targeted employees who begin work before January 1, 1983. The provision limiting qualified first-year wages to 30 percent of FUTA wages is repealed.

*Targeted groups.*—Same as House bill.

*Changes in certification requirements.*—Same as Senate amendment, with one exception. The requirements that certification is to be received or requested before the individual begins work and that certifications based on false information are revoked prospectively generally apply to all individuals, regardless of the date they begin work for their employer. However, for an individual, other than a cooperative education student, who began work earlier than 45 days before the date of enactment, the certification has to have been requested or received before July 23, 1981, and for an individual who begins work for the employer during the 90-day period beginning with the date 45 days before the date of enactment or a cooperative education student who begins work before the end of this period, the certification must be requested or received before the last day of this 90-day period.

*Hiring of relatives.*—Same as House bill and Senate amendment.

*Authorization for administrative expenses.*—Same as Senate amendment.

### 39. Motor carrier operating rights

*House bill.*—Under present law, taxpayers are not allowed a loss deduction under section 165 for the diminution in the value of a license or permit (caused, for example, by an expansion in the number of licenses or permits that could be issued) if the license or permit continues to have value as a right to carry on a business.

Under the House bill, an ordinary deduction is allowed ratably over a 60-month period for the adjusted bases of motor carrier operating authorities held by the taxpayer on July 1, 1980 (the date of enactment of the Motor Carrier Act of 1980). The House bill provides a special stock acquisition rule for cases in which a corporation acquired the stock of another corporation that directly or indirectly held an operating authority. Under regulations, the taxpayer holding the authority on July 1, 1980, may elect to allocate to the basis of the authority a portion of the acquiring corporation's basis

in the stock of the acquired corporation. The allocable portion is the amount of basis the acquiring corporation would have had in the authority under section 334(b)(2) if such corporation had received the authority in a liquidation of the acquired corporation (and any other corporations necessary for the acquiring corporation to receive the authority) immediately after acquisition of the acquired corporation. Under regulations, adjustments shall be made to the acquiring corporation's basis in the stock of the acquired corporation and any other property, to the extent deemed necessary by the Secretary. The provision applies to taxable years ending after June 30, 1980.

**Senate amendment.**—The provision in the Senate amendment is generally the same as the provision in the House bill, except for certain technical details relating to the stock acquisition rule.

**Conference agreement.**—The Conference agreement generally follows the House bill and Senate amendment, except that certain technical modifications are made to the stock acquisition rule.

## H. Savings Incentives Provisions

### 40. Self-employed retirement savings (Keogh plans)

**House bill.**—The deduction limit for employer contributions to a defined contribution Keogh plan, to a defined contribution plan maintained by a subchapter S corporation, or to a simplified employee pension (SEP) is increased from \$7,500 to \$15,000. The 15-percent limit on contributions is not changed. To provide a similar increase in the level of benefits permitted under a defined benefit Keogh or subchapter S corporation plan, the compensation taken into account in determining permitted annual benefit accruals is increased from \$50,000 to \$100,000.

The bill also increases the amount of compensation which may be taken into account to determine contributions to a Keogh plan, to a subchapter S plan, or to a SEP. Under the bill, the includible compensation limit is increased from \$100,000 to \$200,000. However, if annual compensation in excess of \$100,000 is taken into account, the rate of employer contributions for a plan participant who is a common-law employee cannot be less than the equivalent of 7½ percent of that participant's compensation.

The House bill also extends to all partners the present-law rule under which a loan from a Keogh plan to an owner-employee or his use of an interest in the plan as security for a loan is treated as a distribution.

In addition, the House bill permits (1) the penalty-free correction of an excess contribution to a Keogh plan if the excess is withdrawn before the return filing due date and (2) early withdrawals from a terminated Keogh plan by an owner-employee without regard to the 5-year ban on Keogh plan contributions for the owner-employee.

**Senate amendment.**—The Senate amendment generally follows the House bill except that it contains no provision relating to excess contributions to Keogh plans or distributions made on account of the termination of a Keogh plan.

**Conference agreement.**—The conference agreement follows the House bill.

### 41. Individual retirement accounts

**House bill.**—In the case of an individual who is not an active participant in an employer-sponsored plan, the annual contribution limit is raised from the lesser of \$1,500 or 15 percent of compensation to the lesser of \$2,000 or 100 percent of compensation. The limit for a spousal IRA is increased from \$1,750 to \$2,250, and the present-law requirement that contributions under a spousal IRA be equally divided between the spouses is deleted.

In the case of an employee who is an active participant in a plan, a deduction is allowed for contributions to an IRA or for voluntary contributions to the plan. The voluntary contributions and earnings thereon under a plan are subject to IRA-type rules, except that (1) distributions starting at age 70½ are not mandated and (2) rollovers may be made to an IRA with regard to the present law rule limiting rollovers to one per year.

Under the House bill, benefits under a qualified plan (including deductible employee contributions and earnings thereon) are taxed only when paid to the employee or a beneficiary and are not taxed if merely made available. Of course, as under present law, if bene-

fits are paid with respect to an employee to a creditor of the employee, a child of the employee, etc., the benefits paid would be treated as if paid to the employee.

Under present law, individuals generally may self-direct IRA investments or investments under an account in a qualified plan. Under the House bill, amounts invested in collectibles (antiques, art, gems, stamps, etc.) under an IRA or a self-directed account in a qualified plan are treated as distributions for income tax purposes.

Under the House bill, the proceeds of a redeemed U.S. retirement bond which is distributed under a qualified bond purchase plan may be rolled over, tax-free, to an IRA. U.S. retirement bonds purchased for an employee may be redeemed only after the employee attains age 59½, dies or becomes disabled. Also, the bill clarifies the treatment of IRA retirement bonds acquired in a tax-free rollover.

**Senate amendment.**—The Senate amendment is generally the same as the House bill, except that (1) active plan participants are allowed a deduction for contributions to an IRA or for qualified voluntary contributions to a plan limited annually to the lesser of \$1,500 (\$1,625 for a spousal IRA) or 100 percent of compensation for the year, and (2) a surviving or divorced spouse may deduct at least \$1,125 annually for life for contributions to a spousal IRA established by the individual's former spouse at least 5 years before the death or divorce.

In addition, the Senate amendment does not include provisions relating to investments in collectibles under IRAs or self-directed accounts in qualified plans or to rollovers of the redemption proceeds of U.S. retirement bonds. Also, voluntary contributions and earnings thereon are taxed only if paid, but other plan benefits are taxed if paid or made available.

The Senate amendment requires that Treasury provide the Congress (before June 30, 1982) a study of the tax incentives for individual retirement savings.

**Conference agreement.**—The conference agreement follows the House bill, except that a divorced spouse is allowed a deduction for contributions to a spousal IRA established by the individual's former spouse at least 5 years before the divorce if the former spouse contributed to the IRA under the spousal IRA rules for at least three of the five years preceding the divorce. If these requirements are met, the limit on the divorced spouse's IRA contributions for a year is not less than the lesser of (1) \$1,125, or (2) the sum of the divorced spouse's compensation and alimony includible in gross income.

#### 42. Partial dividend and interest exclusion

**House bill.**—Under present law, individuals may exclude from income up to \$200 (\$400 on a joint return) of dividends and interest earned from most domestic sources in 1981 and 1982. After 1982, only the dividend exclusion, which applied before 1981, will be available. This exclusion was limited to \$100 of dividends per taxpayer.

The House bill repeals the \$200/\$400 interest and dividend exclusion after 1981 and reinstates the \$100 per taxpayer dividend exclusion of prior law for 1982 and subsequent years. Effective in 1985, the bill provides for a 15-percent net interest exclusion on up to \$3,000 of net interest (\$6,000 on a joint return). Interest described



in section 116(c) of present law is eligible for the percentage exclusion but only to the extent it exceeds the taxpayer's qualified interest expenses. Qualified interest expense is interest paid for which a deduction is allowed other than interest paid on debt related to a taxpayer's dwelling or his conduct of a trade or business.

**Senate amendment.**—The Senate amendment generally follows the House bill except that (1) the net interest exclusion is effective in 1984 and (2) the \$100 per taxpayer limit on the reinstated dividend exclusion is replaced with a limit of \$100 for a single return and \$200 for a joint return.

**Conference agreement.**—The conference agreement generally follows the House bill, except that the Senate amendment on the \$200 maximum dividend exclusion for joint returns is adopted. In addition, two technical and clarifying changes are made. First, real estate investment trusts, regulated investment companies, and insurance companies are added to the list of eligible payors of excludable interest. Second, the conferees intend that only qualified interest expenses that give rise to a tax benefit are to reduce the amount of excludable interest. Thus, for example, individuals who do not itemize their deductions are not to reduce excludable interest. The Secretary is to provide regulations to implement this rule.

#### 43. Exclusion of interest on qualified saving certificates

**House bill.**—Present law no provision that provides specifically for the exclusion of interest earned on saving certificates. Under section 116, and for calendar years 1981 and 1982 only, up to \$200 (\$400 on a joint return) of dividends and interest from a variety of domestic sources may be excluded from gross income.

House bill provides for a lifetime exclusion from gross income of \$1,000 (\$2,000 in the case of a joint return) of interest earned on qualified tax-exempt savings certificates.

Qualified tax-exempt savings certificates are one-year certificates issued after September 30, 1981, and before January 1, 1983, by a qualified depository institution with a yield equal to 70 percent of the yield on 52-week Treasury bills. A qualified depository institution is a bank defined in section 581, a mutual savings bank, cooperative bank, domestic building and loan association, industrial loan association or bank, credit union, or any other savings or thrift institution chartered and supervised under Federal or State law, if the deposits or accounts of the institution (other than an industrial loan association) are insured under Federal or State law or protected or guaranteed by State law.

For interest to qualify for the exclusion, a certificate issued by a qualified institution must meet several requirements. First, such certificates may be issued only during the period beginning on October 1, 1981, and ending on December 31, 1982. Interest paid after December 31, 1982, with respect to certificates properly issued before that date will be entitled to the exemption. Second, the certificates must have a maturity period of one year. Thus, all of the interest excludable by virtue of the new provision will be earned before January 1, 1984. Third, the certificate must have a yield equal to 70 percent of the yield on 52-week Treasury bills. Whether a certificate meets this 70-percent requirement is determined by comparing the yield to maturity on the certificates (including the effect of any compounding of interest) to the yield to maturity on 52-week Treasury bills sold at the last Treasury auction to have oc-

curred in a calendar week preceding the week the certificate is issued. Fourth, the issuing institution must provide that certificates are available for any deposit of \$500 or more, subject to any limit on maximum deposits.

The provision does not authorize the issuance of qualified tax-exempt savings certificates; however, the House anticipates that the cognizant regulatory authorities will consider such authorization as expeditiously as practicable.

Generally, the provision requires that at least 75 percent of the proceeds of qualified certificates issued during a calendar quarter by an institution other than a credit union be used to provide residential financing by the end of the subsequent calendar quarter. In the case of an institution with net new savings less than the amount of net new savings. For this purpose, qualified net savings is the amount by which deposits into passbook savings accounts, 6-month money market certificates, 30-month small saver certificates, time deposits of less than \$100,000, and qualified certificates exceeds the amount withdrawn or redeemed from such accounts measured at the beginning and end of each calendar quarter. A special rule limits the amount of certificates issued by a credit union that may be outstanding at the close of any calendar quarter to 100 percent of the credit union's savings deposits as of September 30, 1981, plus 10 percent of any new net savings as of the end of the quarter over the credit union's savings deposits as of September 30, 1981.

Qualified residential financing of an institution is any of the following held by the institution:

- (a) any loan secured by a lien on a single-family or multifamily residence;
- (b) any secured or unsecured qualified home improvement loan;
- (c) any mortgage on a single-family or multi-family residence which is insured or guaranteed by the Federal, State or local government or any instrumentality thereof;
- (d) any loan to acquire a mobile home;
- (e) any loan for the construction or rehabilitation of a single-family or multifamily residence;
- (f) any mortgage secured by single-family or multifamily residences purchased on the secondary market, but only to the extent purchases exceed sales of such assets;
- (g) any security issued or guaranteed by the Federal National Mortgage Association, the Government National Mortgage Association, or the Federal Home Loan Mortgage Corporation, or security issued by any other person if such security is secured by mortgages, but only to the extent purchases exceed sales of such assets; or
- (h) any agriculture loan.

The term single-family residence includes stock in a cooperative housing corporation as defined in section 216, and 2, 3, and 4 family residences.

If an institution fails to meet the proceeds investment test at the end of any calendar quarter, it may not issue additional certificates until the requirement is satisfied.

The amount that any individual may exclude from income under the new provision is limited to \$1,000. This limitation applies to the aggregate of all interest paid on all certificates. In the case of mar-

ried individuals filing joint returns, the limit is increased to \$2,000. This is true even if all of the \$2,000 is earned by only one of the individuals filing the joint return.

Interest paid on qualified certificates is excludable only when earned by individuals or by estates that receive such certificates by reason of the decedent's death. In the case of a partnership, the individual partners may exclude their distributive shares of interest paid on qualified certificates held by the partnership subject to each partner's \$1,000 lifetime limitation on the exclusion. In applying the dollar limitation to estates, the estate is treated as having claimed as having claimed any exclusion taken by the decedent or by a surviving spouse who files a joint return claiming an exclusion.

If a taxpayer earns interest in excess of the excludable amount, the first interest earned is the interest eligible for exclusion. The receipt of interest earned on the certificate prior to maturity is not a premature redemption. However, if any portion of a certificate is redeemed or disposed of before maturity, the exclusion from income is not available for any interest earned on the certificate for the year in which the certificate is redeemed or disposed of or in any subsequent year. If interest paid on a certificate is excluded from income in one year and the certificate is prematurely redeemed or disposed of in a subsequent year, then the amount of excluded interest in the prior year must be included in income for the year of the redemption or disposition. Previously excluded amounts that are recaptured under this rule are not taken into account for purposes of the \$1,000 limitation. Thus, if a holder redeems a certificate and reinvests a portion in a new certificate, interest on the new certificate can be excluded.

The provision also provides that using a certificate or any portion of a certificate as collateral or security for a loan will be treated as a redemption of the entire certificate.

There is a denial of the deduction for interest paid on indebtedness incurred to purchase or carry investment in qualified tax-exempt savings certificates. These rules are the same as those that apply under present law with respect to debt incurred or continued to purchase or carry tax-exempt obligations (sec. 265(2)).

The House bill requires the Secretary of the Treasury to report to the Congress before June 1, 1982, on the results of a study to be conducted by the Treasury on the effectiveness of the new saving certificates provision in generating additional savings.

Since some interest earned in 1981 may otherwise be eligible for exclusion under both the new provision and the section 116 interest and dividend exclusion the bill provides a special transition rule. This rule provides that any amount earned on a depository institution tax-exempt savings certificate may be excluded only under new section 128 and may not be excluded under the general interest and dividend exclusion in section 116 of present law, even if the interest on the certificate is not tax-exempt because of a premature redemption or disposition.

**Senate amendment.**—The Senate amendment is the same as the House bill with some exceptions. Savings certificates must be available in denominations of \$500. The term single-family residence does not include stock in a cooperative housing corporation. No restrictions are placed on the amount of certificates issued by credit unions or on investment by credit unions.

**Conference agreement.**—The conference agreement follows the House bill. In addition, the conferees agreed to three technical amendments. First, if a consolidated return is filed for any part of a calendar quarter in which savings certificates may be issued, the amount of qualified certificates, residential financing, and net new savings are to be determined on a net aggregate basis for all affiliated corporations.

Foreign branches and international banking facilities of U.S. banks may not issue tax-exempt savings certificates, and their deposits will not be taken into account in determining the required level of residential financing and agricultural loans needed.

Loans secured by cooperative housing stock will be treated as residential financing.

#### 44. Employee stock ownership plans (ESOPs)

**House bill.**—No provision.

**Senate amendment.**—The Senate amendment accelerates the termination of the present law investment-based tax credit for ESOP contributions by one year, so that it expires at the end of 1982, and replaces it with a payroll-based tax credit. The payroll-based credit (which is not available if contributions allocated to officers, shareholders (more than 10 percent), and employees whose compensation exceeds \$83,000 (adjusted for inflation) exceed specified limits) is limited to one-half of one percent of aggregate employee compensation in calendar year 1983, three-quarters of one-percent in 1984, and one percent in 1985 and subsequent years.

The amendment generally increases from 15 percent of aggregate employee compensation to 25 percent of such compensation the deduction allowed the employer for contributions to an ESOP where the contributions are applied by the plan to make principal payments on a loan incurred to purchase employer stock. An unlimited deduction is allowed the employer for contributions applied to pay interest on the loan.

The Senate amendment also provides that (1) contribution applied to pay loan interest, and (2) forfeitures of fully leveraged ESOP stock are disregarded for purposes of the present law limit on contributions to any participant's account (generally, for 1981, the lesser of \$41,500 or 25 percent of compensation). This rule applies only if contributions allocated to officers, shareholders (more than 10 percent) and employees whose compensation exceeds \$83,000, do not exceed specified limits.

Distributions from a tax credit ESOP which are made on account of the sale of corporate assets or the disposition of a subsidiary are permitted without regard to the present law rule which generally precludes distributions of employer securities for at least 84 months. The Senate amendment also changes the cash distribution and put-option rules to reflect certain State laws and corporate charter restrictions which prevent compliance with present law rules. In addition, the Senate amendment repeals (for all but tax credit ESOPs) the present law rule requiring that employees be entitled to direct voting of employer securities allocated under a defined contribution plan of a closely held corporation.

The non-tax rules of ERISA are also amended to supersede State securities laws to permit Continental Airlines to establish and maintain an ESOP, to issue previously authorized stock to an ESOP, to permit the company to guarantee a loan to the ESOP,

and to permit the ESOP to distribute company stock to employees and beneficiaries.

**Conference agreement.**—The conference agreement generally follows the Senate amendment except that the new payroll-based tax credit for contributions to a tax credit ESOP is allowed only for wages paid in calendar years 1983 through 1987. The credit is limited for 1983 and 1984 to one-half of one percent of compensation paid to employees under the plan and to three-quarters of one percent of such compensation for 1985, 1986, and 1987. The tax credit expires on December 31, 1987.

In addition, the present-law rule requiring that an employee must be entitled to vote stock allocated to his account under a defined contribution plan is deleted with respect to profit-sharing plans for securities acquired after 1979, but is still applicable to all other defined contribution plans.

The conference agreement does not include the Senate provision which supersedes State securities laws with respect to Continental Airlines.

#### 45. Dividend reinvestment plans

**House bill.**—Under present law (sec. 305(a)), a pro rata stock distribution is not taxable to a shareholder at the time he or she receives it, but it is taxable only when the taxpayer sells or otherwise disposes of the shares received as a distribution. Any gain on the sale generally is treated as a long-term capital gain if the underlying shares (on which the distribution was declared) were held for more than one year. Stock distributions which are not pro rata, including stock distributions received pursuant to a shareholder's option to receive either stock or cash, are taxable at fair market value when the shares are initially received.

Under the House bill, a domestic public utility corporation may establish a plan under which shareholders who choose to receive a dividend in the form of common stock rather than cash or other property may elect to exclude up to \$1,500 per year (\$3,000 in the case of a joint return) of the stock dividends from income.

To qualify, the stock must be newly issued common stock, designated by the board of directors of the corporation to qualify for this purpose. The number of shares to be distributed to any shareholder must be determined by reference to a value which is not less than 95 percent (and not more than 105 percent) of the stock's value during the period immediately before the distribution date.

Generally, stock will not qualify where the corporation has repurchased any of its stock within one year before or after the distribution date (or any member of the same affiliated group of corporations has purchased common stock of any other member of such group). However, if the corporation establishes a business purpose for the purchase not inconsistent with the purpose of the dividend reinvestment provision to aid in the raising of new capital, the purchase will not disqualify any dividend otherwise eligible for exclusion.

Stock received as a qualified dividend will have a zero basis, so that when the stock is later sold the full amount of the sales proceeds will be taxable. In general, proceeds from the sale of such stock will be taxed as capital gains. However, where the stock is sold within one year after distribution, any gain will be treated as ordinary income. In addition, if shares of stock of the distributing

corporation are sold by the taxpayer any time after the record date for the dividend and before a date one year after the dividend distribution date, the sale will be treated as a sale of the qualified dividend stock. These rules are designed to prevent the immediate resale of stock without the recognition of ordinary income which would have resulted in the case of a taxable dividend.

Under the House bill, the earnings and profits of the distributing corporation will not be reduced by reason of the distribution of qualified stock, whether or not the shareholder elects to exclude the dividend from income.

Only individual shareholders are eligible for the exclusion. Corporations, trusts, estates, non-resident aliens, and persons holding at least 5 percent of the voting power or value of stock in the corporation (using the attribution rules of section 318) are not eligible to exclude any dividends under this provision.

A public utility is qualified if during the 10 years prior to its taxable year in which the dividend is paid, at least 60 percent of the cost of the depreciable property the corporation acquired for the members of an affiliated group (in which the public utility is a member) was public utility recovery property (within the meaning of new sec. 168A). For periods before 1981, the determination of whether property would have been public utility recovery property shall be made as if section 168A had been in effect.

*Senate amendment.*—No provision.

*Conference agreement.*—The conference agreement generally follows the House bill. The exclusion from income applies to dividends up to \$750 a year (\$1,500 on a joint return), and the exclusion will be allowed for dividends distributed in calendar years 1982 through 1985.

#### 46. Qualified group legal services plans

*House bill.*—No provision.

*Senate amendment.*—Employer contributions to, and benefits provided under, a qualified group legal services plan are excluded from an employee's income. This income exclusion expires December 31, 1981.

Under the Senate amendment, the income exclusion for qualified group legal services plans is extended through December 31, 1984.

*Conference agreement.*—The conference agreement follows the Senate amendment.

## I. Estate and Gift Tax Provisions

### 47. Unified credit

**House bill.**—The unified credit against estate and gift taxes is gradually increased from \$47,000 to \$192,800 over six years. The amount of the credit is \$62,800 for gifts made, and decedents dying, in 1982, \$79,300 in 1983, \$96,300 in 1984, \$121,800 in 1985, \$155,800 in 1986, and \$192,800 in 1987 and subsequent years. Thus, cumulative transfers exempt from gift and estate taxes increase from \$175,625 under present law to \$225,000 in 1982, \$275,000 in 1983, \$325,000 in 1984, \$400,000 in 1985, \$500,000 in 1986, and \$600,000 in 1987 and subsequent years.

**Senate amendment.**—The Senate amendment also increases the unified credit to \$192,800, but provides a five-year phase-in. For 1982 and 1983, the amount of the credit and the amount of cumulative transfers exempt from estate and gift taxes follows the House bill. However, the amount of the credit is \$104,800 for gifts made and decedents dying in 1984 (exempting cumulative transfers of \$350,000), \$138,800 in 1985 (exempting cumulative transfers of \$450,000), and reaches \$192,800 exempting cumulative transfers of \$600,000) for 1986 and subsequent years.

**Conference agreement.**—The conference agreement follows the House bill.

### 48. Rate reduction

**House bill.**—The maximum gift and estate tax rates are reduced over a 4 year period in five percent increments from 70 percent to 50 percent. The maximum rate is 65 percent for gifts made, and decedents dying, in 1982, 60 percent in 1983, 55 percent in 1984, and 50 percent in 1985 and subsequent years. When fully phased in, in 1985, the 50-percent tax rate will apply to taxable gifts and bequests in excess of \$2.5 million.

**Senate amendment.**—No provision.

**Conference agreement.**—The conference agreement follows the House bill.

### 49. Marital deduction

**House bill.**—Present law permits a gift tax marital deduction for the first \$100,000 of gifts to a spouse and for 50 percent of gifts to a spouse in excess of \$200,000. An estate tax marital deduction is allowed for transfer to a surviving spouse up to the greater of \$250,000 or one-half the adjusted gross estate. Transfers of terminable interests generally do not qualify for the gift or estate tax marital deduction.

The House bill removes the quantitative limits on both the gift and estate tax marital deductions and provides that certain terminable interests also qualify for those deductions.

**Senate amendment.**—The Senate amendment is the same as the House bill.

**Conference agreement.**—The conference agreement follows the House bill and Senate amendment.

### 50. Current use valuation

#### a. Increase in maximum reduction in fair market value

**House bill.**—Under present law, the fair market value of qualified real property cannot be reduced by more than \$500,000 as a

result of current use valuation. The House bill increases the maximum amount by which the fair market value of qualified real property may be reduced as a result of current use valuation to \$750,000 for estates of decedents dying in 1981, \$875,000 in 1982, and \$1,000,000 in 1983 and thereafter.

**Senate amendment.**—Under the Senate amendment, the maximum amount by which the fair market value of qualified real property may be reduced as a result of current use valuation is increased to \$600,000 for estates of decedents dying in 1982 and thereafter.

**Conference agreement.**—Under the conference agreement, the maximum amount by which the fair market value of qualified real property may be reduced as a result of current use valuation is increased to \$600,000 for estates of decedents dying in 1981, \$700,000 in 1982, and \$750,000 in 1983 and thereafter.

### ***b. Predeath qualified use requirement***

**House bill.**—Under present law, to be specially valued, real property must be used or held for use as a farm or closely held business (“a qualified use”) for five of the last eight years before the decedent’s death and on the date of death.

The House bill provides that the qualified use requirement of present law, applicable to periods on and before the date of the decedent’s death (sec. 2032A(b)(1)), may be satisfied if either the decedent or a member of the decedent’s family uses real property otherwise eligible for current use valuation in the qualified use. This change is retroactive to estates of certain decedents dying after December 31, 1976.

The House bill also clarifies the types of operations that are to be considered “qualified uses.” The bill divides these operations into three categories: (1) farming (including timber operations other than those that are incidental to other farming operations), (2) timber operations which are not incidental to other farming operations, and (3) other trades or businesses. The requirement of present law that each of these uses be an active trade or business use, as opposed to a passive, or investment, use is not changed.

**Senate amendment.**—The Senate amendment permits the qualified use requirement of present law, applicable to periods on or before the date of the decedent’s death (sec. 2032A(b)(1)), to be satisfied if either the decedent or a member of the decedent’s family uses real property otherwise eligible for current use valuation in the qualified use.

The Senate amendment contains no provision redefining what types of business uses constitute qualified uses.

**Conference agreement.**—The conference agreement follows the Senate amendment.

### ***c. Pre-death material participation requirement***

**House bill.**—Under present law, the decedent or a member of his family must materially participate in the farm (or other business operation) for periods aggregating five years of the eight years before the decedent’s death. On the other hand, if the decedent materially participates in the farm operation, any income derived from the farm is treated as earned income for social security purposes and, therefore, may reduce social security benefits.



Under the House bill, the material participation requirement has to be satisfied during periods aggregating five years or more of the eight-year period ending before the earlier of (1) the date of death, (2) the date on which the decedent became disabled (which condition lasted until the date of the decedent's death), or (3) the date on which the individual began receiving social security retirement benefits (which status continued until the date of the decedent's death).

An individual is considered to be disabled if the individual is mentally or physically unable to materially participate in the operation of the farm or other business.

The House bill provides an alternative to the material participation requirement for qualification of real property for current use valuation in the estates of surviving spouses who receive the property from a decedent spouse in whose estate it was eligible to be valued based on its current use. The bill provides that the spouse will be treated as having materially participated during periods when the spouse (but not a family member) engaged in active management of the farm or other business operation. Active management of the making of business decisions other than the daily operating decisions of a farm or other trade or business.

*Senate amendment.*—The Senate amendment is the same as the House bill.

*Conference agreement.*—The conference agreement follows the House bill and the Senate amendment.

*d. Tacking to satisfy certain requirements in cases of certain pre-death involuntary conversions and like-kind exchanges*

*House bill.*—The House bill changes present law to permit tacking of the ownership, qualified use, and material participation requirements in the case of replacement property acquired pursuant to like-kind exchanges under section 1031 and involuntary conversions under section 1033. This tacking is available only for that portion of the replacement property or exchange property which does not exceed the value of the property disposed of in the exchange or conversion, and is permitted only when the replacement property or exchange property is used in the same qualified use as the property which was disposed of.

*Senate amendment.*—No provision.

*Conference agreement.*—The conference agreement follows the House bill.

*e. Election requirements*

*House bill.*—Under present law, an election to specially value qualified real property must be made on a timely filed estate tax return. An agreement to the election which is binding under local law must be signed by all parties having an interest in the property. State law normally requires that a guardian be appointed to sign the agreement for minor heirs.

Under the House bill, elections to specially value property must be made on the decedent's estate tax return rather than by the due date of the return as under present law. Therefore, the election is permitted to be made on a late return, if that return is the first estate tax return filed by the estate. As under present law the election is irrevocable once made.

House bill also permits a custodial parent to sign the required agreement to the current use valuation election on behalf of minor heirs, who otherwise have no guardian empowered to sign on their behalf. The consent by the custodial parent is binding on the minor heir for all purposes under the current use valuation provision, the special lien under section 6324B, and income tax basis rules for specially valued property.

**Senate amendment.**—No provision.

**Conference agreement.**—The conference agreement follows the portion of the House bill that provides that an election to specially value property must be made on the decedent's estate tax return rather than by the due date of that return as under present law. The conference agreement deletes the portion of the House bill permitting a custodial parent to sign the required agreement on behalf of a minor heir.

#### ***f. Use of share rentals in the formula valuation method***

**House bill.**—Under present law, farm real property may be specially valued using a formula valuation method. Under the formula method, the value of qualified real property is determined by (1) subtracting the average annual State and local real estate taxes for tracts of comparable land used for farming from the average annual gross cash rental for the tracts of the comparable land, and (2) dividing that amount by the average annual effective interest rate for all new Federal land bank loans. Each average annual computation is made on the basis of the five most recent calendar years ending before the decedent's death.

The House bill permits substitution of net share rentals for cash rentals in the formula valuation method for farm real property if the executor cannot identify actual tracts of comparable farm real property in the same locality as the decedent's farm property that are rented solely for cash. As under present law, if there is no comparable land from which a cash or share rental can be determined, the real property subject to the election is to be valued using the multiple factor valuation method.

**Senate amendment.**—The Senate amendment is the same as the House bill.

**Conference agreement.**—The conference agreement follows the House bill and the Senate amendment.

#### ***g. Reduction in post-death recapture period***

**House bill.**—Under present law, if, within 15 years after the death of the decedent (and before the death of the qualified heir), specially valued property is disposed of to nonfamily members or ceases to be used for the farming or other closely held business purpose based upon which it was valued in the decedent's estate, all or a portion of the Federal estate tax benefits obtained by virtue of the reduced valuation are recaptured by means of a special "additional estate tax" or "recapture tax" imposed on the qualified heir. Failure by the heir or a member of the heir's family to materially participate in the business operation for periods aggregating three years or more during any eight-year period ending within 15 years after the decedent's death is treated as a cessation of qualified use.

The House bill reduces the present 15-year recapture period to 10 years; the five-year phase-out period of present law is repealed.

**Senate amendment.**—The Senate amendment is the same as the House bill.

**Conference agreement.**—The conference agreement follows the House bill and the Senate amendment.

***h. Increase in basis of property on which a recapture tax is paid***

**House bill.**—Under present law, if an election is made to value property based on its current use, the qualified heir's income tax basis in the property is the current use value. No adjustment is made to this basis if the recapture tax is imposed.

The House bill permits a qualified heir to make an irrevocable election to have the income tax basis of qualified real property increased to the fair market value of the property as of the date of the decedent's death (or the alternate valuation date under section 2032, if the estate elected that provision) where the recapture tax is paid. If the heir elects this basis adjustment, the heir must pay interest on the amount of the recapture tax from the date which in nine months after the decedent's death until the due date of the recapture tax. The interest is computed at the rate (or rates) charged on deficiencies of tax for the period involved. If the heir does not make the election and pay the interest, no adjustment is made to the basis of the property.

**Senate amendment.**—Under the Senate amendment, the increase in income tax basis is automatic if a recapture tax is paid, and no interest is imposed on the recapture tax.

**Conference agreement.**—The conference agreement follows the House bill.

***i. Miscellaneous technical changes to post-death recapture period rules***

**House bill.**—The House bill retains the present requirement that the qualified heir owning the real property after the decedent's death use it in the qualified use throughout the recapture period. However, the bill creates a special two-year grace period immediately following the date of the decedent's death during which failure by the qualified heir to commence use of the property in the qualified use will not result in imposition of a recapture tax. The 10-year recapture period (15 years for estates of decedents dying before December 31, 1981) is extended by a period equal to any part of the two-year grace period which expires before the qualified heir commences using the property in the qualified use. This provision is retroactive to estates of certain decedents dying after December 31, 1976.

In the case of an eligible qualified heir, the House bill provides that "active management" by the eligible qualified heir is treated as material participation for purposes of meeting the material participation requirement during the post-death recapture periods. Eligible qualified heirs include the spouse of the decedent, a qualified heir who has not attained the age of 21, a qualified heir who is a full-time student (within the meaning of sec. 151(e)(4)), and a qualified heir who is disabled (within the meaning of sec. 2032A(b)(4)(B), as added by the bill). Active management means the making of business decisions other than the daily operating decisions of the trade or business.

The House bill provides that an exchange pursuant to section 1031 of qualified real property solely for qualified replacement

property to be used for the same qualified use as the original qualified real property does not result in imposition of the recapture tax.

The House bill also repeals the requirement that a qualified heir make an election to secure the benefits of the special nonrecognition rules for the recapture tax for involuntary conversions.

**Senate amendment.**—The Senate amendment is the same as the House bill, except the grace period immediately following the decedent's death during which the qualified use requirement need not be met is one year, and the provision applies only to estates of decedents dying after December 31, 1981.

**Conference agreement.**—The conference agreement follows the House bill.

#### ***j. Qualification of property purchased from a decedent's estate***

**House bill.**—Under present law, only that property which is acquired from a decedent is eligible for current use valuation. The House bill expands the circumstances in which property is considered to be so acquired to include property that is purchased from a decedent's estate by a qualified heir as well as property that is received by bequest, devise, inheritance, or in satisfaction of a right to pecuniary bequest. This change reverse present law in cases where the decedent gives a qualified heir an option to purchase property otherwise qualified for current use valuation as well as in cases where the executor sells the property to an heir in the absence of such a direction in the will. If purchased property is specially valued, the qualified heir who purchases the property is limited to the current use value of the property as his income tax basis. This change is retroactive to estates of certain decedents dying after December 31, 1976.

**Senate amendment.**—No provision.

**Conference agreement.**—The conference agreement follows the House bill.

#### ***k. Property transferred to discretionary trusts***

**House bill.**—Under present law, property owned indirectly through ownership of an interest in a partnership, a corporation, or a trust qualifies for current use valuation to the extent that it would qualify if it were owned directly. However, trust property qualifies for current use valuation only to the extent that an heir receives a "present interest" in the trust property. Treasury regulations define the term "present interest" by reference to the gift tax law (sec. 2503). This definition precludes current use valuation of any property passing from the decedent to a trust in which the interest of the life tenant (or any other beneficiary whose interest becomes a present interest before expiration of the recapture period) is subject to discretion on the part of the trustee. This result is the same even if all potential beneficiaries of the trust are qualified heirs. (Treas. Reg. § 20.203A-3(b)(1)).

The House bill provides that property meeting the other requirements for current use valuation can be specially valued if it passes to a discretionary trust in which no beneficiary has a present interest (under sec. 2503) because of the discretion in the trustee to determine the amount to be received by any individual beneficiary so long as all potential beneficiaries of the trust are qualified heirs.

This provision applies retroactively to certain estates of decedents dying after December 31, 1976.

**Senate amendment.**—No provision.

**Conference agreement.**—The conference agreement follows the House bill.

#### *l. Definition of family member*

**House bill.**—Under present law, only real property that passes to qualified heirs is eligible for current use valuation. The term “qualified heir” means a member of the decedent’s family, including his spouse, lineal descendants, parents, grandparents, and aunts or uncles of the decedent and their descendants. The term does not include members of a spouse’s family.

Additionally, the pre-death qualified use and material participation requirement may be satisfied by the decedent or a member of the decedent’s family. Likewise, the post-death material participation requirement may be satisfied by participation of the qualified heir or a member of the heir’s family. Property can only be disposed of during the recapture period without imposition of a recapture tax if the transfer is to a member of the qualified heir’s family.

The House bill changes the definition of family member. The new definition includes an individual’s spouse, parents, brothers and sisters, children, stepchildren, and spouses and lineal descendants of those individuals.

**Senate amendment.**—No provision.

**Conference agreement.**—The conference agreement follows the House bill.

#### *m. Judicial review of fair market value of specially valued property*

**House bill.**—Under present law, the fair market value or specially valued property, as well as the property’s use value, must be determined for several purposes. The House bill provides for a declaratory judgment proceeding in the Tax Court review of Treasury Department determinations of the fair market value of specially valued property.

**Senate amendment.**—No provision.

**Conference agreement.**—The conference agreement follows the Senate amendment.

#### *n. Credit for State recapture tax*

**House bill.**—Many States have enacted current use valuation provisions similar to the Federal provision. Some of these States impose a recapture tax like the Federal recapture tax. Those State recapture taxes are not eligible for the State death tax credit of present law.

The House bill permits a qualified heir to claim part or all of any recapture tax imposed by a State which has a current use valuation provision like the Federal provision as a credit against the Federal recapture tax.

**Senate amendment.**—No provision.

**Conference agreement.**—The conference agreement follows the Senate amendment.

***o. Special rules for woodlands***

***House bill.***—Under present law, only real property used as a farm for farming purposes or in other closely held business operations (“a qualified use”) is eligible for current use valuation. Timber operations are included in the definition of farming purposes. Standing timber, like other growing crops, is not treated as part of the qualified real property.

The House bill permits an executor to elect to treat timber operations as a separate qualified use. Qualified timber operations are operations where growing and harvesting trees (other than milling) are not incidental to other types of farming operations. If the election is made, standing timber can be specially valued as part of the real property on which it is located, and active management is treated as material participation for purposes of qualifying for current use valuation and of avoiding imposition of the recapture tax.

If standing timber is specially valued, disposition or severance of the timber results in imposition of the recapture tax. This recapture tax is determined by treating the timber as an interest in the real property on which the timber stands or stood.

***Senate amendment.***—The Senate amendment continues treatment of timber operations as a farming use, but permits executors to elect to specially value the standing timber. If standing timber is specially valued, the recapture tax is imposed when the timber is disposed of or severed.

***Conference agreement.***—The conference agreement follows the Senate amendment on current use valuation of standing timber.

***p. Effective dates***

***House bill.***—The changes to the current use valuation provision apply generally to estates of decedents dying after December 31, 1981.

The increase in the limitation on the amount by which the fair market value of specially valued property can be reduced applies to estates of decedents dying after December 31, 1980.

The changes to the recapture period rules on involuntary conversions (under sec. 1033) and like-kind exchanges (under sec. 1031) apply to such exchanges occurring after December 31, 1981, even if the decedent in whose estate the property was specially valued died before that date.

As noted in the discussion of individual items, four provisions apply to all estates for which estate tax returns are due to be filed after July 28, 1980, and to all estates for which a timely use valuation election was made between January 1, 1977, and July 28, 1980. These four provisions are the change in the pre-death qualified use requirement, the provision on property passing to discretionary trusts, the provision on property purchased from a decedent’s estate, and the two-year grace period during which the post-death qualified use requirement need not be met.

***Senate amendment.***—The changes to the current use valuation provision apply to estates of decedents dying after December 31, 1981.

***Conference agreement.***—The conference agreement follows the House bill.

### 51. Transfers within 3 years of death

**House bill.**—Present law generally requires that gifts made by a decedent within 3 years of death be included in the decedent's gross estate at their value as of the date of death or alternate valuation date (sec. 2035(a)). In general, the House bill provides that this rule does not apply to decedents dying after December 31, 1981. However, the House bill continues to apply present law to gifts of certain types of property covered by sections 2036, 2037, 2038, 2041, and 2042. In addition, all gifts made within 3 years of death are included for purposes of qualifying for current use valuation (sec. 2032A), deferred payment of estate tax (sec. 6166), qualified redemptions to pay estate tax (sec. 303), and estate tax liens (subchapter C of chapter 64).

**Senate amendment.**—Gifts made within 3 years of death are included in a decedent's estate at their value as of the date of the gift.

**Conference agreement.**—The conference agreement follows the House bill.

### 52. Time for payment of estate tax attributable to closely held businesses

**House bill.**—The most liberal provisions of present law sections 6166 and 6166A, relating to the deferred payment of estate taxes attributable to interests in closely held businesses, are combined into one provision. The new provision permits deferred payment if interests in closely held businesses exceed 35 percent of the adjusted gross estate. Conforming changes are made to section 303, which permits redemption of stock in a closely held business to pay certain estate taxes, funeral expenses, and administration expenses.

The House bill also provides that the remaining unpaid tax balance will not be accelerated upon the death of the decedent's heir or a subsequent transferee provided the interest in closely held businesses passes to a family member of the heir or subsequent transferee.

In addition, the House bill provides a declaratory judgment procedure to determine eligibility for deferral and whether acceleration is proper.

**Senate amendment.**—The Senate amendment also combines sections 6166 and 6166A into one provision, but provides that qualifying interests in closely held businesses must exceed 35 percent of the gross estate or 50 percent of the taxable estate.

No acceleration of the unpaid tax balance occurs upon the death of decedent's heir or subsequent transferee, whether or not the interest in closely held businesses passes to a family member of the heir or subsequent transferee.

The Senate amendment contains no provision permitting judicial review of controversies involving deferred payment of estate taxes.

**Conference agreement.**—In general, the conference agreement follows the House bill, except that it deletes the provision of the House bill which provides a declaratory judgment procedure for controversies involving deferred payment of estate taxes.

### 53. Disclaimers

**House bill.**—The House bill provides that a timely transfer of property to the person who would have received it had an effective

disclaimer been made under the applicable local law is considered an effective disclaimer for purposes of Federal estate and gift taxes where the other Federal requirements of qualified disclaimers are met.

**Senate amendment.**—The Senate amendment follows the House bill except for technical language differences.

**Conference agreement.**—The conference agreement follows the House bill.

#### 54. Basis rule for property received within 3 years of death

**House bill.**—The House bill provides that the basis of appreciated property acquired by gift within 3 years of death is not adjusted to its fair market value at date of death if it is returned to the donor (or donor's spouse).

**Senate amendment.**—No provision.

**Conference agreement.**—In general, the conference agreement follows the House bill, except that it reduces the 3-year period to one year.

#### 55. Certain charitable contributions

**House bill.**—Where a charitable transfer is an interest which is less than the donor's entire interest in property, present law provides that no charitable deduction is allowable unless the split-interest gift is made in certain specified forms. Because an original work of art and a related copyright are considered interests in the same property, no deduction is allowed for the transfer of an original work of art to charity if the copyright is retained or transferred to a noncharity.

The House bill provides that where a donor or decedent makes a qualified contribution of a copyrightable work of art, the work of art and its copyright will be treated as separate properties for purposes of the estate and gift tax charitable deduction. Thus, a charitable deduction will be allowed for a transfer of a work of art to a qualified charitable organization, whether or not the copyright itself is simultaneously transferred to the charitable organization.

**Senate amendment.**—The Senate amendment contains no provision relating to split-interest transfers of copyrightable works of art. However, it provides a special credit against the estate taxes imposed on the estate of D. M. Kunhardt. The amount of the credit is equal to the smallest of (1) the total estate tax imposed, (2) the fair market value of the Matthew Brady glass plate negatives transferred to the Smithsonian, or (3) \$700,000.

**Conference agreement.**—The conference agreement follows the portion of the House bill relating to the gift or bequest of a copyrightable work of art and the portion of the Senate amendment relating to the special credit to the estate of D. M. Kunhardt.

#### 56. Certain bequests, etc., to minor children

**House bill.**—The House bill repeals the provision of present law which permits a limited deduction for certain property passing to certain orphaned minor children.

**Senate amendment.**—No provision.

**Conference agreement.**—The conference agreement follows the House bill.



### 57. Generation-skipping transfer tax

**House bill.**—No provision.

**Senate amendment.**—The Tax Reform Act of 1976 imposed a tax on generation-skipping transfers. A transitional rule exempts from the tax generation-skipping trusts created by wills or revocable trusts in existence on June 11, 1976, if (1) such wills and trusts were not amended after that date to create or increase the amount of the generation-skipping transfer, and (2) the testator or trust grantor dies before January 1, 1982.

Under the Senate amendment, the January 1, 1982, date contained in the present transitional rule is extended one additional year to January 1, 1983.

**Conference agreement.**—The conference agreement follows the Senate amendment.

### 58. Annual gift tax exclusion

**House bill.**—The House bill increases the amount of the annual gift tax exclusion from \$3,000 to \$10,000 per donee and provides an unlimited exclusion for amounts paid for the benefit of a donee for certain medical expenses and school tuition.

**Senate amendment.**—The Senate amendment follows the House bill in increasing the annual exclusion from \$3,000 to \$10,000 per donee, but does not provide an unlimited exclusion for tuition and medical expenses.

**Conference agreement.**—The conference agreement follows the House bill.

### 59. Annual payment of gift tax

**House bill.**—Present law requires that gift tax returns must be filed, and any gift tax paid, on a quarterly basis if the sum of (1) the taxable gifts made during the quarter, plus (2) all other taxable gifts made during the taxable year (for which a return has not yet been required to be filed) exceeds \$25,000. If annual gifts are less than \$25,000, a return must be filed for the fourth quarter.

The House bill provides that all gift tax returns are to be filed, and any gift tax paid, on an annual basis.

**Senate amendment.**—No provision.

**Conference agreement.**—The conference agreement follows the House bill.

## J. Tax Straddles

### 60. Gains or losses on straddles

**House bill.**—Under present law, gain or loss on property generally is recognized at the time of its disposition. In Revenue Ruling 77-185, the Internal Revenue Service denied deductions for losses on certain partial dispositions of straddles on the grounds that the transactions were incomplete, tax-motivated and not reflective of true economic position. The theory of this ruling is currently in litigation.

The House bill allows taxpayers to deduct straddle losses to the extent of straddle gains and net non-straddle commodity gains. Disallowed straddle losses are carried forward as straddle losses. The bill applies to commodity-related property which includes futures contracts, forward contracts, actual commodities (including metals), Treasury bills, other debt instruments, currency, and any interests in the foregoing. The bill does not apply to real estate, stock (except commodity substitute stock), interest income and short-term stock options. Positions in commodity-related property are attributed to and from related persons and flow-through entities in order to determine whether taxpayers hold offsetting positions. Related persons are a taxpayer, the taxpayer's spouse and minor children; a taxpayer and a person under common control within section 414(b) or (c); and persons whose relationship is subject to the loss disallowance rules in sections 267 and 707(b). Hedging transactions are excepted from this provision. The bill applies to property acquired and positions established by the taxpayer after January 27, 1981, in taxable years ending after that date.

**Senate amendment.**—The Senate amendment marks all commodity futures contracts to market at year end and treats them as if 60 percent of the capital gains and losses on them were long-term and 40 percent were short-term. Net losses under the market-to-market rule may be carried back three years against market-to-market gains. Taxpayers may elect to mark their futures to market for the entire 1981 year as if 1982 rates were in effect. Tax due on gains rolled forward from prior years into 1981 may be paid in five annual installments with interest. The first installment payment is due with the taxpayer's 1981 taxes.

In the case of straddles involving property other than futures which are market-to-market, the Senate amendment allows straddle losses only to the extent such losses exceed the unrealized gains on offsetting positions. Disallowed losses are deferred. The wash sale and short sale principles of present law are extended to straddles by regulation. The loss deferral rule applies to actively-traded personal property (other than stock). This rule does not apply to such property as real estate, stock and short-term stock options. Attribution of positions runs to and from related persons, but only from a flow-through entity to a taxpayer. Related persons are a taxpayer and the taxpayer's spouse, or a taxpayer and any person with whom the taxpayer files a consolidated return under section 1501. Hedging transactions are excepted from this provision.

The Senate amendment applies to property acquired and positions established by the taxpayer after June 23, 1981, in taxable years ending after that date.

**Conference agreement.**—The conference agreement follows the Senate amendment.

## 61. Interest and carrying charges

**House bill.**—Present law allows a current deduction for interest and carrying charges for purchasing or carrying commodity investments. The House bill requires that such charges be added to the basis of the commodity if it is part of a straddle. However, futures traders may continue to deduct these charges currently from commodity-related gains. Hedging transactions are excepted from the capitalization rule.

**Senate amendment.**—The Senate amendment follows the House bill except it omits the special rule for futures traders.

**Conference agreement.**—The conference agreement follows the Senate amendment.

## 62. Hedging exception

**House bill.**—The House bill excepts hedging transactions from the capitalization rule and the rule limiting straddle losses. Syndicates are not entitled to the hedging exemption. A syndicate is defined as a flow-through entity (1) more than 35 percent of whose losses go to limited partners or limited entrepreneurs; or (2) whose interests must at any time be registered under State or Federal law.

**Senate amendment.**—The Senate amendment generally follows the House bill, except that the hedging exception applies to the mark-to-market and loss deferral rules, as well as the capitalization rule. Under the Senate amendment, a syndicate is defined as a flow-through entity with more than 35 percent of its losses allocable to limited partners or limited entrepreneurs. Certain interests held by family members of an active participant in an entity, retired active participants, and estates of active participants are treated as if held by active participants. The Senate amendment gives the Secretary discretion to treat any interest held by an individual as if it were held by an active participant, provided the Secretary determines that tax-avoidance is unlikely.

**Conference agreement.**—The Conference agreement follows the Senate amendment.

The Senate amendment's provisions on syndicates provide the Secretary with flexibility to treat certain limited interests in partnerships and other flow-through entities as interests held by active participants when the facts and circumstances warrant such treatment. It is intended that authority granted the Secretary to treat an interest in an entity as if it were held by an active participant be used to insure that for legitimate and demonstrated business reasons, an entity may take advantage of this exemption. However, in allowing a taxpayer to claim the hedging exemption, the Secretary must determine that the facts and circumstances in the specific case indicate that the hedging exemption is not sought, nor could it be exploited, for tax avoidance purposes.

Further, it is intended that in determining eligibility for the exemption, the Secretary need not require requests for rulings and information from every interest or participant, in the entity nor to examine every interest and participant, in order to make such a determination. The Secretary must determine that the entity itself has the required percentage of interests held by active participants and by others treated as active participants and that the entity and such participants lack tax-avoidance purpose.

### 63. Characterization of Treasury bills

**House bill.**—Under present law, gain and loss on certain governmental obligations (including Treasury bills) issued at discount and payable at a fixed maturity date less than one year from issue date are treated as ordinary income and loss. The House bill treats such obligations as capital assets and the discount on these obligations as ordinary income if they were property acquired after or positions established after January 27, 1981.

**Senate amendment.**—The Senate amendment follows the House bill, but applies to property acquired after and positions established after June 23, 1981.

**Conference agreement.**—The Conference agreement follows the Senate amendment.

### 64. Dealer identification of securities held for investment

**House bill.**—Present law requires dealers to identify securities held as investments within 30 days of the date of acquisition. The House bill requires identification of securities acquired after the date of enactment by the close of business on the date of acquisition.

**Senate amendment.**—The Senate amendment follows the House bill, except that securities acquired after the date of enactment and before January 1, 1982, must be identified by the close of business on the first day after the date of acquisition. Floor specialists are allowed seven business days to designate stock for which they are registered specialists.

**Conference agreement.**—The conference agreement follows the Senate amendment.

### 65. Sale or exchange of capital assets

**House bill.**—Under present law, for gain or loss to be capital gain or loss, it must result from the sale or exchange of a capital asset. The House bill provides that taxable dispositions of capital assets which are commodity-related property are treated as sales or exchanges. This change applies to property acquired after January 27, 1981.

**Senate amendment.**—The Senate amendment follows the House bill, except that it applies to actively traded personal property acquired after June 23, 1981.

**Conference agreement.**—The conference agreement follows the House bill and Senate amendment.

### 66. Treasury study

**House bill.**—The House bill requires the Treasury Department to study the effects of straddles provisions and provide two reports to the Committee on Ways and Means of the House of Representatives and the Committee on Finance of the Senate. The first report is due on or before July 1, 1983, and must analyze 1981 tax returns; the second is due on or before July 1, 1984, and must analyze 1982 returns.

**Senate amendment.**—No provision.

**Conference agreement.**—The conference agreement follows the Senate amendment.

## K. Administrative Provisions

### 67. Interest on deficiencies and overpayments

**House bill.**—Under present law, the interest rate applicable to deficiencies and overpayments is set by Treasury regulations at 90 percent of the adjusted prime rate for September, and is effective on February 1 of the immediately succeeding year. The interest rate, however, cannot be changed more frequently than once every 23 months.

The House bill provides that the interest rate is to be set annually at the prime rate. Starting in 1983, changes in the interest rate are to be effective on January 1, rather than on February 1, of the year immediately succeeding that in which the rate is established.

**Senate amendment.**—No provision.

**Conference agreement.**—The conference agreement follows the House bill.

### 68. Penalties for false withholding allowance certificate

**House bill.**—Under present law, a civil penalty of \$50 may apply for claiming withholding allowances based on false information (Code sec. 6682). The criminal penalty for willfully failing to supply information, or for willfully supplying false or fraudulent information, in connection with wage withholding is a fine of up to \$500 and/or up to one year imprisonment. The bill increases to \$500 the civil penalty for filing false information with respect to wage withholding. The bill also increases the criminal penalty for willfully failing to supply information, or for willfully supplying falsified information in connection with wage withholding to \$1,000.

These provisions are effective for acts and failures to act after December 31, 1981.

**Senate amendment.**—No provision.

**Conference agreement.**—The conference agreement follows the House bill.

### 69. Penalty for failure to file information returns

**House bill.**—Present law requires taxpayers to file a variety of information returns with the Secretary. Generally, such returns relate to payments to, and transactions with, other persons. The penalty for failure to file most information returns is \$1 per return, subject to a maximum of \$1,000 for any calendar year (Code sec. 6652(b)). Present law generally does not require a taxpayer who must file an information return to furnish a copy to the person to whom the payment relates. However, such a requirement is imposed as to some information returns (Code sec. 6678).

The bill generally requires that information returns be furnished to the person to whom the payments on the return relate.

The bill also increases the penalty for failure to file most information returns with the Secretary. The increased penalty is \$10 for each return, subject to a maximum penalty of \$25,000 for any calendar year. Because the obligation to furnish a statement and the requirement to file an information return are different obligations, a taxpayer could be subject to both the information and statement penalties.

The bill retains the \$1 penalty of present law for failure to file information returns with respect to certain payments aggregating less than \$10.

The provision is effective as to returns and statements required to be furnished after December 31, 1981.

**Senate amendment.**—No provision.

**Conference agreement.**—The conference agreement follows the House bill.

## 70. Penalty for overstated tax deposits

**House bill.**—Present law requires periodic deposits of various taxes prior to the close of the taxable year (see, e.g., Code sec. 6302, relating to tax deposits). Taxpayers who fail to comply with these depository requirements may be subject to a penalty of 5 percent of any underdeposit not deposited on or before the prescribed date, unless it is shown that the failure is due to reasonable cause and not due to willful neglect (Code sec. 6656(a)). In addition, criminal penalties may apply with respect to taxpayers who make a false return claiming to have made deposits of tax (Code sec. 7206), or who fail to collect, account for or pay over collected taxes (Code sec. 7215, 7512).

The bill contains a specific penalty applicable to persons who make an overstated deposit claim. The penalty is 25 percent of the overstated deposit claim, and applies in addition to any other applicable penalty. However, the overstated deposit claim penalty does not apply if the overstated deposit claim is due to reasonable cause and not due to willful neglect.

**Senate amendment.**—No provision.

**Conference agreement.**—The conference agreement follows the House bill.

## 71. Penalty for valuation overstatements

**House bill.**—Present law imposes an addition to tax, or penalty, with respect to certain tax underpayments due to negligence or civil fraud (Code sec. 6653). The penalty for negligence is 5-percent of any underpayment that is due to negligent or intentional disregard for rules and regulations but not with intent to defraud. The alternative civil fraud penalty is 50 percent of any underpayment.

The bill provides a graduated addition to tax applicable to certain income tax “valuation overstatements.” The addition to tax applies only to the extent of any income tax underpayment which is attributable to such an overstatement, and only if the taxpayer is an individual, a closely held corporation, or a personal service corporation.

Under the bill, there is a valuation overstatement if the value of any property, or the adjusted basis of any property, claimed on any return exceeds 150 percent of the amount determined to be the correct amount of the valuation, or adjusted basis. If there is a valuation overstatement, the following percentages are used to determine the applicable addition to tax:

	<i>The applicable percentage</i>
If the valuation claimed is the following percent of the correct valuation:	<i>is—</i>
150 percent or more but not more than 200 percent .....	10
More than 200 percent but not more than 250 percent .....	20
More than 250 percent .....	30

The penalty is effective for returns filed after December 31, 1981.

**Senate amendment.**—Same as the House bill.

**Conference agreement.**—The conference agreement follows the House bill and the Senate amendment.

## 72. Addition to negligence penalty

**House bill.**—Present law imposes an addition to tax, or penalty, with respect to certain tax underpayments due to negligence or civil fraud (Code sec. 6653). The penalty for negligence is 5 percent of any underpayment that is due to negligent or intentional disregard for rules and regulations but not with intent to defraud. The alternative civil penalty is 50 percent of any underpayment.

The bill imposes an addition to tax equal to 50 percent of the interest (determined under Code sec. 6601) attributable to that portion of an underpayment which is attributable to negligent or intentional disregard of rules or regulations. The addition to tax is 50 percent of the interest for the period beginning on the last day for payment of the underpayment and ending on the date of the assessment.

As an addition to tax, amounts imposed under this new penalty are nondeductible.

**Senate amendment.**—No provision.

**Conference agreement.**—The conference agreement follows the House bill. For deficiency notice purposes (sec. 6212), the addition to tax imposed under this provision is considered to be an amount stated even though the addition is dependent upon the interest due on the underpayment.

## 73. Disclosure of returns and return information for purposes not relating to tax administration

**House bill.**—No provision.

**Senate amendment.**—Under present law, Federal agencies may, in certain circumstances, receive tax returns, taxpayer return information (i.e., books and records supplied by the taxpayer), and return information from the Internal Revenue Service for their use in nontax criminal investigations. Returns and taxpayer return information are available only pursuant to an ex parte order granted by a Federal district court judge. Return information, other than taxpayer return information, may be received by written request. The IRS may refuse to disclose tax returns, taxpayer return information, or return information if it determines that disclosure would identify a confidential informant or seriously impair a civil or criminal tax investigation. Present law also permits the IRS to disclose return information, other than taxpayer return information, which may constitute evidence of a violation of Federal criminal laws, to the extent necessary to apprise the head of the appropriate Federal agency charged with enforcing such laws.

Under present law, the unauthorized disclosure of tax returns or return information is a felony punishable upon conviction by a fine of not more than \$5,000 or imprisonment of not more than 5 years, or both.

Under present law, a taxpayer may bring a civil action for damages against a person who knowingly or negligently discloses returns or return information in violation of the disclosure provisions.

The Senate amendment relaxes the standards for obtaining an ex parte court order for the disclosure of returns and books and records of individuals. In addition, the books and records of any

business entity consisting of more than two owners would be available upon written request. Return information that has been disclosed to the Justice Department may be disclosed, further, to other Federal agencies; and may, pursuant to court order, be disclosed to State law enforcement officials.

The IRS would be required to disclose any nonreturn information that may constitute evidence of a violation of Federal criminal law to the appropriate Federal agency. Moreover, in certain emergency situations, the IRS would be required to disclose returns on its own initiative.

In certain circumstances, the bill would permit disclosure of returns and return information to foreign law enforcement officials.

The bill provides that a Federal employee will not be criminally liable for a wrongful disclosure that results from a good faith but erroneous interpretation of the law while the employee was acting within the scope of his employment. Moreover, any civil action for wrongful disclosure would be brought against the appropriate Federal agency, rather than a Federal employee.

**Conference agreement.**—The conference agreement follows the House bill. However, the conferees intend that this matter should be thoroughly examined in Congressional hearings in the very near future and that appropriate legislative action should be taken.

#### 74. Confidentiality of certain IRS information

**House bill.**—Present law restricts the disclosure of tax returns and return information. However, information that cannot identify any particular taxpayer is not protected under the disclosure restrictions. Because of this, questions have been raised concerning whether the IRS can legally refuse to disclose information which is used to develop standards for auditing tax returns.

The House bill provides that nothing in the tax law, or in any other Federal law, will be construed to require the disclosure of standards used, or to be used, for the selection of returns for examination (or data used, or to be used, for determining such standards), if the Secretary determines that such disclosure will seriously impair assessment, collection, or enforcement under the internal revenue laws. However, it is intended that nothing in this provision be construed to limit disclosure of statistical data or other information (other than of the type that could be used by the IRS to determine criteria for selecting returns for examination) to the extent permitted under present law. Thus, any information that is currently made available will continue to be available.

**Senate amendment.**—No provision.

**Conference agreement.**—The conference agreement follows the House bill.

#### 75. Tax Court filing fee

**House bill.**—No provision.

**Senate amendment.**—Under present law, the tax Court is authorized to impose a fee of up to \$10 for the filing of any petition. The House bill authorizes the Tax Court to impose a filing fee of up to \$60. This provision applies to petitions filed after December 31, 1981.

**Conference agreement.**—The conference agreement follows the Senate amendment.



## 76. Cash management: Corporate estimated tax payments

**House bill.**—Under present law, corporations whose taxable income exceeded \$1 million in any of the three preceding taxable years must pay estimated tax of at least 60 percent of current year's tax liability regardless of their prior year's tax liability. The House bill provides that corporations whose taxable income exceeded \$1 million in any of three preceding taxable years will be required to pay estimated tax of at least 80 percent of current year's tax liability regardless of their prior year's tax liability. The provision is effective for taxable years beginning after December 31, 1981.

**Senate amendment.**—The Senate amendment is similar to the House bill, except that the 80 percent requirement is phased in over a three-year period. In 1982, large corporations will have to be at least 65 percent current with estimated tax payments. This will increase to 75 percent in 1983, and to 80 percent for 1984 and subsequent years. The provision is effective for taxable years beginning after December 31, 1981.

**Conference agreement.**—The conference agreement follows the Senate amendment.

## 77. Declaration and payment of estimated taxes by individuals

**House bill.**—In general, present law provides that individuals whose tax liability, over amounts withheld during the year, is less than \$100 are not required to file declarations of estimated taxes. The House bill increases the tax liability threshold for the payment of estimated taxes from \$100 to \$500 over a four year period, as follows:

Taxable years beginning in:	Threshold amount
1982 .....	\$200
1983 .....	300
1984 .....	400
1985 and thereafter .....	500

Individuals whose tax liability, in excess of withholding does not exceed the threshold amount would not be required to declare or pay estimated tax, nor would they be penalized for underpayment of estimated tax.

The increase in the tax liability threshold begins in taxable years beginning after December 31, 1981.

**Senate amendment.**—No provision.

**Conference agreement.**—The conference agreement follows the House bill.

## 78. Railroad retirement taxes

**House bill.**—The House bill has the following provisions:

**Tier II taxes.**—Under present law (code section 3221), there is imposed on railroad employers a tax of 9.5 percent of compensation paid in a calendar month, subject to a maximum limitation. Currently, the annual taxable compensation base is \$22,200; however, in no case does the tax apply to any amount paid in a month in excess of one-twelfth of the annual limitation (\$1,850 in 1991). The annual (and monthly) limitation on taxable compensation for the purposes of section 3221 is indexed pursuant to section 230 (c) and (d) of the Social Security Act. The rate of tax under section 3221 applies to employers only.

The House bill will, pursuant to a negotiated agreement between railway management and labor, provide for adjustments in the financing of the tier-II pension component. The tax on employers under section 3221 will be increased from 9.5 to 11.75 percent, an increase of 2.25 points. In addition, the provision will provide for a new tax of 2 percent on the compensation of employees (as defined in section 3221).

*Advance transfers to the railroad retirement account.*—Generally, under the railroad retirement and social security interchange, for a given fiscal year there is computed the amount of social security taxes that would have been collected if railroad employment had been covered directly by social security. This amount is netted against the amount of benefits social security would have paid to railroad beneficiaries based on railroad and nonrailroad earnings during that period. Where social security benefits that would have been paid exceed social security taxes that would have been due, the excess, plus an allowance for interest and administrative expenses, is transferred from the social security trust funds to the Railroad Retirement Account. The financial interchange amount for a given fiscal year is determined and transferred no later than June of the year following the close of the preceding fiscal year.

The House bill provides advanced, limited transfers to the Railroad Retirement Account from the general fund in amounts necessary to make monthly benefit payments. In no case will the amounts outstanding at any time for any fiscal year under this authority exceed the estimated interchange transfer for that fiscal year. The Board will pay the prevailing rate of interest currently being paid on short-term instruments of the Department of the Treasury on amounts transferred under this authority. The borrowing authority will be effective upon enactment.

*Payments of employee taxes by railroad employers.*—Under present law (code section 3221(e)(1)(iii)), payments made by railroad employers of railroad employee taxes under section 3211 without deduction from the remuneration of the employee are excluded from the definition of compensation for the purposes of the Railroad Retirement Tax Act (RRTA). Until 1981, a similar provision was included in the Federal Insurance Contributions Act (code section 3121(a)(6) and section 209(f) of the Social Security Act). The exclusion of such payment from the definition of wages for FICA tax and social security benefit computation purposes was eliminated by section 1141(a)(1) of Public Law 96-499, the Omnibus Reconciliation Act of 1980.

The House bill provides that payments by an employer of employee railroad payroll taxes, without deduction from the employee's remuneration, will be included in taxable compensation for RRTA purposes. This change will conform the provisions of the Railroad Retirement Tax Act to the corresponding provisions of the recently amended Federal Insurance Contributions Act. The changes made by this provision will be effective with respect to compensation paid for services rendered after September 30, 1981.

*Definition of compensation.*—Under present law, there is imposed on employers a tax on so much of compensation paid in any calendar month by such employer for services rendered by an employee. It is unclear whether the intent of the law is to tax compensation when paid or when earned.

The House bill provides that compensation that is paid in one calendar month but that would be payable in a prior or subsequent taxable month but for the fact that the prescribed date of payment would fall on a Saturday, Sunday, or legal holiday will be deemed to have been paid in such prior or subsequent taxable month. The bill thus makes clear the treatment for RRTA purposes of compensation "bunched" in any month for services rendered in the preceding month.

The House bill also provides that, in the absence of evidence to the contrary (e.g., the statutory presumption curing "bunching" of compensation problems in certain months, as clarified by the immediately preceding provision), payments by railroad employers shall be presumed to be compensation for services rendered as an employee in the period for which the payment is made, an employee receiving retroactive wage payments (such as lump sum retroactive wage payments and crew consists payments) will be deemed under the provision to be compensation paid in the period for which the payment is made unless the employee requests in writing (pursuant to existing provisions in sec. 3231(e)(2)) that such compensation was earned in a period other than the period in which it was paid.

This provision generally applies to taxable years ending on or after the date of enactment. It also applies in taxable years ending before enactment for which the period for assessment, collection, or claim for credit or refund of taxes has not expired.

*Senate amendment.*—No provision.

*Conference agreement.*—The conference agreement follows the House bill with several modifications. The conference agreement does not include the House bill provision dealing with advance transfers to the railroad retirement account. Under the conference agreement, the provision that clarifies the definition of compensation is effective for taxable years beginning after December 31, 1981. It is the specific intent of the conferees that no inference be drawn from this clarification for taxable years beginning after 1981 as to Congressional intent with respect to prior legislation concerning the definition of compensation for the purposes of administrative or judicial proceedings.

## L. Miscellaneous Provisions

### 79. State legislators business expenses

**House bill.**—For taxable years before 1981, State legislators were allowed an election to treat their residences within the district represented as their tax home for purposes of computing business deductions for expenses while away from home. If such an election is made, the allowable deduction is equal to the sum of the legislator's legislative days multiplied by the Federal per diem for the State capital.

The House bill extends, and modifies, the State legislator provision for taxable years beginning on or after January 1, 1973. Under the provision, an electing State legislator is deemed to have expended for business purposes an amount equal to the individual's legislative days multiplied by the greater of the Federal per diem or the State per diem (put not over 110 percent of the Federal per diem). This amount is deductible, except for legislators living within 50 miles of the capitol building, without regard to the away-from-home rule.

**Senate amendment.**—The amendment generally is the same as the House bill, except that the Senate provision does not apply to taxable years before 1981, and the 50-mile rule is applied with respect to distances from the capital city.

**Conference agreement.**—The conference agreement generally follows the House bill and the Senate amendment. The 50-mile rule adopted is that contained in the House bill, and the provision is effective for taxable years beginning on or after January 1, 1976.

### 80. Fringe benefit regulations

**House bill.**—Prior to June 1, 1981, the Treasury was prohibited from issuing final regulations, under Code section 61, relating to the income tax treatment of fringe benefits. The House bill extends this prohibition until May 31, 1983.

**Senate amendment.**—The Senate amendment is the same as the House bill except that the prohibition is extended until December 31, 1983.

**Conference agreement.**—The conference agreement follows the House bill and the Senate amendment, and extends the prohibition until December 31, 1983.

### 81. Commuting expense regulations

**House bill.**—Prior to June 1, 1981, the Treasury was required to apply the income tax, FICA, FUTA, and withholding provisions relating to the treatment of certain transportation expenses as they were applied before the issuance of Rev. Rul. 76-453, 1976-2 C.B. 86. The House bill extends the requirement until May 31, 1981.

**Senate amendment.**—No provision.

**Conference agreement.**—The conference agreement follows the Senate amendment.

### 82. Campaign funds

**House bill.**—No provision.

**Senate amendment.**—Under present law, candidates for election to Congress must designate *one* "principal campaign committee" to receive contributions and make expenditures on the candidate's behalf (2 USC 432(e)). A campaign committee may be designated as

a "principal campaign committee" by only one candidate, and such a designated committee may not support any other candidate. A statement of designation must be filed with the Federal Election Commission (FEC) and, as appropriate, with the Clerk of the House or the Secretary of the Senate. A congressional candidate's principal campaign committee must coordinate the submission of FEC reports of affiliated campaign committees.

Under Code section 527, a candidate's campaign organization generally is exempt from taxation. However, political organization taxable income, e.g., interest on account balances, etc., is subject to the highest rate, rather than the graduated rates, of the corporate income tax. Currently, this rate is 46 percent for amounts over \$100,000.

The Senate amendment applies the generally applicable corporate income tax rates to political organization taxable income of a Congressional candidate's "principal campaign committee," as defined under present law (2 USC 432(e)). Under regulations prescribed by the Secretary, candidates have to furnish the Secretary with the principal campaign committee's designation. No change is made to the present law rules applicable to other campaign or political organizations.

Under the amendment, political organization taxable income of a candidate's "principal campaign committee" is taxed at the generally applicable corporate income tax rates. Thus, after 1982, the lowest rate would be 15 percent as to amounts of \$25,000 or less, and the highest rate would be 46 percent on amounts over \$100,000.

The Senate amendment is effective for taxable years beginning after December 31, 1981.

**Conference agreement.**—The conference agreement follows the Senate amendment.

### 83. Tax-exempt bonds for the purchase of mass transit equipment

**House bill.**—Under section 103, interest on State and local government obligations is generally exempt from Federal income tax. However, tax exemption is denied to State and local government issues of industrial development bonds with certain exceptions. A State or local government bond is an industrial development bond (IDB) if (1) all or a major portion of the proceeds of the issue are to be used in any trade or business not carried on by a State or local government or tax-exempt organization, and (2) payment of principal or interest is secured, in whole or in major part, by an interest in, or derived from payments with respect to, property used in a trade or business.

Certain industrial development bonds qualify for tax exemption where the proceeds of the bonds are used to provide exempt activity facilities. Such facilities include mass commuting facilities. These facilities do not include the equipment used for commuting purposes, such as buses, subway cars, or railroad passenger cars used in a commuting system.

The House bill provides that interest on obligations of a State or local government are exempt from Federal income tax, if substantially all of the proceeds of the obligations are used to provide qualified mass commuting vehicles. Qualified mass commuting vehicles is defined in the committee bill to mean any bus, subway car, rail car, or similar equipment which is leased to a mass transit

system that is wholly owned by one or more governmental units and which is principally used by the mass transit system in providing mass commuting services to the general public.

*Senate amendment.*—No provision.

*Conference agreement.*—The conference agreement follows the House bill.

#### 84. Tax-exempt bonds for volunteer fire departments

*House bill.*—In general, obligations issued by States or their political subdivisions are exempt from Federal income tax. Volunteer fire departments are not considered to be political subdivisions and, thus, cannot issue tax-exempt bonds on their own behalf.

The House bill treats an obligation of a volunteer fire department as an obligation of a political subdivision of a State if the following conditions are met: (1) the volunteer fire department is the sole organization providing firefighting services in a particular area; (2) the volunteer fire department is required by the political subdivision, by agreement or otherwise, to provide firefighting services; (3) the volunteer fire department receives more than half of its funds from political subdivisions; and (4) the volunteer fire department makes no charge for its firefighting services.

Tax-exempt obligations may be used only to finance (1) depreciable property that is used in training for, or the performance of, firefighting or ambulance services, or (2) depreciable property used to house such property.

The provision is effective for obligations issued after December 31, 1980.

*Senate amendment.*—The Senate amendment treats an obligation of a volunteer fire department as an obligation of a political subdivision of a State if the following conditions are met: (1) the volunteer fire department is organized and operated to provide firefighting or emergency medical services in an area that is not provided with firefighting services, and (2) the volunteer fire department is required by written agreement to provide firefighting services.

Tax-exempt obligations may be used only to finance (1) depreciable property that is used in training for, or the performance of, firefighting or ambulance services, or (2) depreciable property used exclusively to house such property.

The provision applies to obligations issued after December 31, 1968.

*Conference agreement.*—The conference agreement generally follows the Senate amendment, with several modifications. Under the conference agreement, obligations must be issued as part of an issue substantially all of the proceeds of which are to be used for the acquisition, construction, reconstruction, or improvement of a firehouse or fire truck used or to be used by a volunteer fire department.

The provision generally applies to obligations issued after December 31, 1980. However, the provision has retroactive effect with respect to certain obligations held by the First Bank and Trust Company of Indianapolis, Indiana, which were issued after December 31, 1969, and before January 1, 1981.

#### 85. Modification of foreign investment company provisions

*House bill.*—No provision.

**Senate amendment.**—Gain on the sale or exchange of stock in a foreign investment company is taxed as ordinary income to the extent attributable to earnings and profits derived after 1962. Once a foreign corporation becomes a foreign investment company, the ordinary income treatment applies to even earnings and profits derived before the foreign corporation became a foreign investment company.

Under section 1248 of the Code, certain gain attributable to post-1962 earnings and profits derived by a controlled foreign corporation are treated as a dividend. Under section 1248, gain attributable to earnings and profits of a foreign corporation which were accumulated during any taxable year beginning before January 1, 1976, while the corporation was a less developed country corporation under section 902(b) as in effect before the enactment of the Tax Reduction Act of 1976, would be taxed as capital gain, rather than a dividend, under section 1248(d)(3).

The Senate amendment provides that gain on the disposition of stock in a foreign investment company attributable to earnings and profits derived before the foreign corporation became a foreign investment company will not be subject to tax under section 1246 of the Code. Instead, that gain not covered by section 1246 because of the amendment is covered by section 1248 where that section is otherwise applicable. The amendment only applies to companies that became foreign investment companies because they met the requirements of section 1246(b)(2) of the Code.

**Conference agreement.**—The conference agreement follows the Senate amendment.

## 86. Charitable contributions by corporations

**House bill.**—No provision.

**Senate amendment.**—Under present law, a corporation's deduction for charitable contributions may not exceed 5 percent of its taxable income. The Senate amendment increases the limitation on a corporation's charitable contributions deduction to 10 percent of taxable income. The provision is effective for taxable years beginning after December 31, 1981.

**Conference agreement.**—The conference agreement follows the House bill.

## 87. Unemployment tax status for certain fishing boat services

**House bill.**—No provision.

**Senate amendment.**—Under present law, certain crew members of fishing boats are treated as self-employed individuals rather than as employees for purposes of the Federal Insurance Contributions Act (FICA) and income tax withholding. However, services which are not subject to FICA taxes are not exempt for purposes of the Federal Unemployment Tax act (FUTA) if the services are related to catching halibut or salmon for commercial purposes or if the services are performed on a vessel of more than ten net tons. In general, a claim for credit or refund of any tax imposed by the Internal Revenue Code must be made either within 3 years from the time the return was filed or 2 years from the time the tax was paid (whichever is later). If no return was filed, the claim for refund must be made within 2 years from the time the tax was paid.

The Senate amendment exempts for purposes of FUTA, the services of fishing boat crew members which currently are exempt for purposes of FICA and income tax withholding. Thus, services by members of the crew on boats engaged in catching fish or other forms of aquatic animal life are exempt for purposes of FUTA if the remuneration for those services is a share of the boat's catch, or of the proceeds of the catch, and if the crew of such boat normally is made up of fewer than ten individuals. In the case of a fishing operation involving more than one boat, services are exempt for purposes of FUTA if the remuneration for services is a share of the entire fleet's catch or its proceeds, and if the operating crew of each boat in the fleet normally is made up of fewer than ten individuals.

On addition, the provision allows employers who paid FICA taxes prior to the enactment of the Tax Reform Act of 1976 for services exempted from FICA by that Act to claim a refund of these taxes within one year of the date of enactment of this Act.

The FUTA tax exemption applies to wages paid after December 31, 1980, for services performed after that date. The provision allowing a refund of FICA taxes previously paid is effective on the date of enactment.

*Conference agreement.*—The conference agreement follows the Senate bill with modifications. Under the conference agreement, the FUTA tax exemption is effective for one year. In addition, employers will not be permitted to seek a refund for FICA taxes previously paid.

#### 88. Tax credit for planting certain pecan trees

*House bill.*—No provision.

*Senate amendment.*—Under present law, there is no provision that allows taxpayers to take tax credits for planting pecan trees. The Senate amendment allows taxpayers to claim a nonrefundable credit for planting pecan trees to replace pecan trees that were destroyed, in September 1979, by Hurricane Frederick. The amount of the credit is \$10 per tree. Excess credits may be carried forward to succeeding taxable years.

The credit generally is available to taxpayers in taxable years beginning after December 31, 1980, and before January 1, 1986. However, in the case of a taxpayer's first taxable year beginning after December 31, 1980, the credit is available with respect to trees planted after August 31, 1979.

*Conference agreement.*—The conference agreement follows the House bill.

#### 89. General obligation veterans mortgage subsidy bonds for State of Oregon

*House bill.*—No provision.

*Senate amendment.*—Under section 103A, limitations have been imposed on the issue of tax-exempt mortgage subsidy bonds for the purchase of owner-occupied homes, effective January 1, 1981. Transition rules apply to certain issues. Qualified veterans mortgage bonds are exempt from the limitation, if they are general obligation bonds, are in registered form, and the home-owner meets the principal residence requirements.

The amendment permits the issuance of \$66.5 million of State of Oregon general obligation bonds that will be used to finance resi-



dential mortgages for veterans to whom commitments were delayed beyond the effective date of the Act.

**Conference agreement.**—The conference agreement follows the House bill.

#### 90. 2-year extension of telephone excise tax at 1 percent

**House bill.**—No provision.

**Senate amendment.**—The present excise tax on communications services (local telephone, toll telephone, and teletypewriter services) is 2 percent for 1981 and 1 percent for 1982, with no tax as of January 1, 1983. The Senate amendment extends the 1-percent rate for two years, and thus delays the termination of the telephone tax until January 1, 1985.

**Conference agreement.**—The conference agreement follows the Senate amendment.

#### 91. Exemption from firearms excise tax for small producers

**House bill.**—No provision.

**Senate bill.**—Present law (sec. 4181) imposes an excise tax on firearms generally and on shells and cartridges at a rate of 11 percent of the manufacturer's sales price. Also, a tax of 10 percent is imposed on pistols and revolvers. There are no exemptions except for sales to the Department of Defense.

The Senate amendment provides an exemption from the excise taxes on firearms, pistols, and revolvers for small producers who produce or assemble 50 or fewer complete firearm units per year. The amendment also exempts from the tax on ammunition hand-loaded shells or cartridges for individuals who load it for themselves or for others on a nonprofit basis. The small producer exemption is effective for sales made after December 31, 1975, and the exemption for hand-loaded shells or cartridges is effective upon enactment.

**Conference agreement.**—The conference agreement follows the House bill.

#### 92. Amortization of construction period taxes and interest

**House bill.**—Under present law, taxpayers other than most corporations, in general, are required to capitalize and amortize construction period interest and taxes (sec. 189). This rule is not applicable to low-income housing until after December 31, 1981.

The House bill delays application of section 189 to low-income housing until 1983.

**Senate amendment.**—The Senate amendment excludes application of section 189 to low-income housing, phases out application to other residential housing for post-1986 years, and repeals section 189 for post-1990 years.

In general, the provision applies to amounts paid or accrued in taxable years beginning after December 31, 1981.

**Conference agreement.**—The conference agreement follows the House bill, but extends permanently the exemption of low-income housing from section 189.

#### 93. Amortization of low-income housing rehabilitation expenditures

**House bill.**—The House bill has no provision.

**Senate amendment.**—Under present law, the taxpayer may elect to amortize qualified low-income housing rehabilitation expenditures over a 60-month period. The amount of expenditures is limited to \$20,000 per dwelling unit (sec. 167 (k)).

The Senate amendment increases the amount of expenditures eligible for amortization under section 189 to \$40,000 per unit if the rehabilitation is conducted pursuant to a program under which tenants who demonstrate home ownership responsibilities may purchase their units at a price that limits the profit to the seller. The program must be certified by the Secretary of Housing and Urban Development or by a State or local governmental unit and the tenants must occupy the units as their principal residence. The program must provide that the sum of the taxable income and the amount realized on sale must not exceed the excess of (1) the taxpayer's basis in the property (without adjustment for deductions under section 167) over (2) the new tax benefits from the section 167 deduction less tax on the taxable income from leasing.

The provision applies to amounts paid or incurred after December 31, 1980.

**Conference agreement.**—The conference agreement follows the Senate amendment.

#### 94. Investment credit for theatrical productions and TV shows

**House bill.**—No provision.

**Senate amendment.**—The present law investment credit is allowed neither for live theatrical productions nor for television game shows. The Senate amendment provides an investment credit for live theatrical productions and extends the investment credit for movie and television films to television game shows.

**Conference agreement.**—The conference agreement follows the House bill.

#### 95. Foreign investment in U.S. real property

**House bill.**—No provision.

**Senate amendment.**—On November 26, 1980, Congress passed the Omnibus Reconciliation Act of 1980 which contained a provision that requires, in general, that foreign persons selling U.S. real estate after June 18, 1980, will be subject to United States taxation on that sale. Also, foreign persons selling stock in a U.S. corporation having 50 percent or more of its gross asset value comprised of U.S. real property interests will be subject to U.S. taxation. Finally, the distributions (liquidating or non-liquidating) of U.S. real property interests by a foreign corporation shall be subject to tax.

While the provision was effective for dispositions after June 18, 1980, special rules applied to transactions covered by a treaty of the United States. In general, the Code provision overrides treaties, but not until January 1, 1985. If treaties are negotiated and signed before 1985, the old treaty is to take precedence over the Code provision for a maximum period of two years after the new treaty is signed.

**Withholding.**—The Senate amendment provides that the foreign investment in United States real property provisions are to be enforced by a system of withholding.

The provision requires withholding by a purchaser, purchaser's agents, or any settlement officer or seller's agent where U.S. real estate is acquired from a foreign person.

The amount to be withheld is the smallest of: first, 20 percent of the amounts realized; second, the seller's maximum tax liability, discussed below; or third, the fair market value of that portion of the sale proceeds which is within the withholder's control. The seller's maximum tax liability is the maximum amount which the Treasury determines that the seller could owe on his gain on the sale plus any unsatisfied prior withholding tax liabilities of prior foreign owners with respect to that property that, under the provisions of the amendment, the seller was required to withhold when he bought the property but failed to do so.

The withholding requirement would apply only if the purchaser knows or has received a notice that the seller is a foreign person. The seller is required to notify the purchaser, the purchaser's agent, and settlement officer that the seller is a foreign person. The seller's agent is also required to notify the purchaser that the seller is a foreign person if the agent has reason to believe that the seller may be a foreign person.

The withholding is thus required only if the purchaser has actual knowledge that the seller is foreign or has received notice that the seller is foreign. However, the seller's agent is relieved of any responsibility to give notice to a purchaser if he relies in good faith on a written statement of the seller—or, in the case of a seller's agent retained by another agent of the seller a written statement by that other seller's agent—that the seller is a U.S. person.

No withholding is required if the purchaser is to use the real property as his principal residence and the purchase price is \$200,000 or less. Also, withholding is not required if the seller obtains a qualifying statement from the Treasury that he is exempt from tax or has provided adequate security for payment of the tax, or has otherwise made arrangements with Treasury for the payment of the tax. Furthermore, withholding is not required if the property being sold is stock of a corporation and the sale takes place on an established U.S. securities market.

The provision provides that a seller agent who does not carry out his obligation to provide notice will be required to withhold any of the purchaser's consideration he has within his control, including any compensation received by him in connection with the transaction.

Provision is made for the Treasury, upon request of the seller or any withholding agent, to reduce the amount of withholding otherwise required. Any request, as well as a request for a qualifying statement, must be acted upon within 30 days of receipt of the request.

The provision sets forth special rules for withholding by a domestic partnership, a trustee of a domestic trust, or an executor of a domestic estate. These persons will be required to withhold from amounts which such entities have in their custody and which are attributable to the disposition of a U.S. real property interest, but only if the amounts are income of a nonresident alien individual or foreign corporation, partnership, trust, or estate.

Special rules are also provided requiring withholding where a U.S. real property interest is distributed by a foreign corporation or is disposed of in a transaction which, under the general rules in the Code, would be a nonrecognition transaction. For example, it is intended that, where a foreign corporation distributes U.S. real property interest to its shareholders, it would be required to with-

hold a tax equal to 20 percent of the fair market value of the property reduced by the adjusted basis of the property.

*Technical Amendments.*—The Senate amendment makes a number of clarifying and technical amendments to the foreign investment in U.S. real property provisions. These provisions are intended to make clear the Congress' intention to tax dispositions of U.S. real property interests by foreign investors.

*Virgin Islands Corporations.*—Under present law, gains realized by foreign investors on the sale of U.S. real property are subject to U.S. tax unless the property is held by a Virgin Islands corporation. This arises because section 28(a) of the Revised Organic Act of the Virgin Islands provides that Virgin Islands corporations satisfy their U.S. income tax obligations by paying their tax on worldwide income to the Virgin Islands under the so-called mirror system. The mirror system means that the name "Virgin Islands" is substituted for the name "United States," and vice versa, wherever such names appear in the U.S. income tax laws.

For purposes of the Virgin Islands mirror tax, a Virgin Islands corporation is a domestic corporation and arguably may avoid tax on its capital gains if it sells its U.S. real estate and liquidates under the rules prescribed by section 337. It has been argued that gains realized by the foreign shareholders will also escape Virgin Islands tax, since section 897, as mirrored, can be read to impose a Virgin Islands tax on gain from a disposition of a Virgin Islands real property interest, but there is no Virgin Islands tax on the sale of a U.S. real property interest. It has also been argued that various other transactions involving foreign corporations interacting with the mirror system avoid the effect of the real estate legislation.

This problem does not exist for the other possessions of the United States.

The Senate amendment provides that a U.S. real property interest includes an interest in real property located in the United States or the Virgin Islands. Under this definition, a foreign shareholder of a Virgin Islands corporation 50 percent or more of the gross asset value of which consists of a Virgin Islands or U.S. real property interests is subject to tax on gain from disposition of an interest in a Virgin Islands real property holding corporation.

Thus, for example, this provision makes clear that if a Virgin Islands corporation purchases U.S. real estate, adopts a plan of complete liquidation, and then sells the real estate, the shareholder will be subject to Virgin Islands taxation on the gain under mirror section 987. For a further example, the provision also makes clear that a foreign corporation cannot avoid the provisions of section 897 by establishing a permanent establishment in the Virgin Islands for investment in U.S. real property.

To prevent double taxation, the amendment provides that a person subject to tax because of section 897 shall pay such tax and file the necessary returns with the United States with respect to real property interests where the underlying interest in real property is in the United States, and with the Virgin Islands with respect to a real property interest where the underlying interest in real property is located in the Virgin Islands. Sale of an interest, other than solely as a creditor, in a U.S. real property holding corporation shall be subject to tax in the United States while the tax on

the sale of an interest in a Virgin Islands real property holding corporation will be paid to the Virgin Islands.

The source rules are amended to provide that gain on the disposition of an interest in real property located in the Virgin Islands is foreign source income to United States taxpayers. This insures that the gain will be taxed as income that is effectively connected with the conduct of a trade or business in the United States or the Virgin Islands, as the case may be. Further, this amendment will insure that a U.S. person subject to Virgin Islands tax on the disposition of Virgin Islands property can take a foreign tax credit against his U.S. liability for such tax.

*Partnership Assets.*—Current taxation applies to the disposition of an interest in a U.S. real property holding corporation, which is a U.S. corporation 50 percent or more of the fair market value of the assets of which consists of U.S. real property. If a corporation is a partner, only the U.S. real property of the partnership is taken into account for purposes of determining whether a corporation is a U.S. real property holding corporation.

The amendment provides that for purposes of determining whether a corporation is a U.S. real property holding corporation, the corporate partner takes into account its proportionate share of all assets of the partnership. Thus, for example, the corporate partner would count its proportionate share of the foreign real estate of the partnership. The same rules apply to trusts and estates in which a corporation has an interest. The amendment also makes clear that the same rules apply to a chain of successive partnerships, trusts or estates.

*Taxation in Carryover Basis Cases.*—Under present law, the Treasury has the authority to override the nonrecognition provisions of the Code in the case of certain transfers of a U.S. real property interest. The Senate amendment makes clear the Treasury's authority to provide for recognition of gain where a carryover basis transaction is entered into for the purpose of avoiding Federal income tax on the transaction. Taxation is specifically provided for if, at the time of receipt of the property, the distribution would not be subject to tax on a later disposition of the property by the recipient.

However, after the issuance of regulations by the Secretary, the Treasury may waive taxation in appropriate cases where tax avoidance is not present.

For example, assume that, A, a nonresident alien individual owns real estate through corporation B organized in country X. A contributes the stock of B to corporation C which is located in country Y. Y has a treaty with the U.S. B liquidates under section 332 of the Code. Since the present treaty between Y and the United States enables C to dispose of the property free of U.S. tax, B is taxed on the distribution to the extent the fair market value of the property at the time of the distribution exceeds B's adjusted basis in the property.

*Nondiscrimination.*—U.S. income tax treaties generally contain a provision that provides for nondiscriminatory tax treatment by the treaty partners of U.S. residents and residents of the treaty partner. A similar provision is contained in some friendship, commerce and navigation treaties. Present law avoids any possible claim that a foreign corporation is discriminated against by allowing a foreign corporation that has a permanent establishment in the United

States to elect to be treated as a domestic corporation, but only if, under a treaty, the permanent establishment may not be treated less favorably than domestic corporations carrying on the same activities. The treaties are overridden by the legislation, but not until 1985.

Despite this provision and the intent of Congress, it is understood that some taxpayers may be taking the position that because of technical problems under old treaties, they cannot make the election and therefore are being discriminated against. This enables taxpayers to plan around the provision.

The amendment makes clear that under section 897(i), any foreign corporation may make an election to be treated as a domestic corporation for purposes of section 897 of the Code and the related reporting requirements if the corporation owns a U.S. real property interest, and, under any treaty obligation of the United States, the foreign corporation is entitled to nondiscriminatory treatment with respect to that interest.

The election may be revoked only with the consent of the Secretary. The election can be made only if all shareholders of the corporation at the time of the election consent to the election and specifically agree that any gain from the disposition of the interest after June 18, 1980, the effective date of the original legislation, which would be taken into account under the legislation will be taxable even if such taxation would not be allowed under a treaty to which the United States is a party. If a class of interest is traded on an established securities market, then the consent need only be made by a person who held more than 5 percent of that class of interest.

For example, foreign person A owns all of the stock of X, a corporation organized in the Netherlands Antilles which owns U.S. real estate. A contributes the stock of X to Y, a Netherlands corporation. X, with the consent of its sole shareholder Y makes an election under section 897(i) to be treated as a U.S. corporation. Under the Netherlands—U.S. treaty, the sale of X's shares by Y would be exempt from tax. To prevent taxpayers from rearranging their United States real property interest holdings so as to avoid U.S. taxation on gains derived from the disposition of a U.S. real property interest, the amendment confirms that X cannot make the section 897(i) election unless Y agrees that on the ultimate sale of X's shares, Y would be subject to U.S. tax under section 897.

The amendment also makes clear that the election provided by this provision is the exclusive remedy for any person claiming discriminatory treatment because of sections 897 or 6039(C) or both of them.

*Indirect Holdings.*—The amendment makes clear that for purposes of determining whether a foreign corporation has substantial U.S. real property investors, and therefore must report, the foreign corporation must look through to the assets of any U.S. corporations in which the foreign corporation has an interest.

*Contributions to Capital.*—Under present law, an argument has been made that a foreign investor can avoid paying U.S. tax on his gain from the disposition of a U.S. real property interest through the device of contributing that interest to the capital of a foreign corporation in which he is a shareholder. The amendment clarifies present law by specifically providing that gain will be recognized by a nonresident alien individual or foreign corporation on the

transfer of a U.S. real property interest to a foreign corporation if the transfer is made as paid in surplus or as a contribution to capital to the extent of the fair market value to the property transferred over the adjusted basis and any other gain recognized by the transferor.

*Liquidation of Foreign Corporations.*—Under present law, a foreign corporation is taxed when it sells or exchanges a U.S. real property interest. Taxation applies even if the sale would otherwise be tax-free under the nonrecognition liquidation provisions of the Code. Under the legislation as reported by the Senate Finance Committee on December 15, 1979, and the House Ways and Means Committee on June 18, 1980, a foreign corporation could have taken advantage of the tax-free liquidation provisions, but the foreign shareholders would have been taxed on the exchange of their stock, which was a real property interest, for the property distributed.

In the case of a U.S. person acquiring the stock of a foreign corporation from a foreign person between December 15, 1979, and November 26, 1980, it would have been reasonable to assume that the tax, if any, due with respect to the unrealized appreciation of the U.S. real estate would have been borne by the foreign seller of the corporation's stock. The conference action shifted that burden to the liquidating corporation—effectively the acquiring shareholders. Thus, in the case of an acquiring U.S. corporation, it now owns the stock of a foreign corporation that has a substantial tax liability due on its U.S. real estate. In contrast, if the U.S. corporation had acquired the stock of a U.S. corporation, it could have liquidated the corporation without a tax liability and received a step-up in basis of the U.S. real estate to its fair market value.

The amendment permits foreign corporations that were acquired during the period that began after December 31, 1979, and before November 26, 1980, to elect to be treated as a U.S. corporation for purposes of liquidating under section 334(b)(2) of the Code. This will enable those corporations to liquidate tax-free with a corresponding step-in basis of the U.S. real estate in the hands of the U.S. purchaser corporation.

For all other purposes, the foreign corporation will be treated as a foreign corporation. Thus, the selling foreign shareholders will be treated as having sold the stock of a foreign corporation and, accordingly, will generally not be taxable by the U.S.

A separate problem arises in situations where a U.S. individual has held stock of a foreign corporation which holds U.S. real estate. Under present law, upon a 12-month liquidation of the foreign corporation, there would be a tax at the corporate level on the U.S. real property interest, as well as a tax at the shareholder level. If the acquired corporation had been a U.S. corporation, the liquidation could have been accomplished tax-free at the corporate level with a tax remaining at the shareholder level. The double tax in the case of U.S. shareholders of foreign corporations was not intended.

The amendment relieves the double tax burden by giving U.S. shareholders who acquired their interests prior to the effective date of this legislation a credit against any tax imposed on them on the surrender of their stock in the liquidating foreign corporation. The credit is equal to the tax imposed on the liquidating foreign corporation on the sale of the U.S. real property. This rule would

apply only if the U.S. persons continuously held the stock since June 18, 1980, the effective date of the legislation.

The statute provides for the override of certain nonrecognition provisions of the Code, and for the continued application of treaties until 1985. However, it was never intended that these provisions be manipulated so as to make the provisions of the legislation in effect elective until 1985. Accordingly, the conferees agree with the Senate that the statute should be clarified to reiterate Congress' original intent to collect at least one tax on the transfer of U.S. real property interests by foreign investors. Congress provided a grace period until January 1, 1985, to certain foreign investors who were residents on the enactment of section 897 of a treaty country which provides an exemption from tax on the gain from such sale. However, it was not Congress' intent to grant such an exemption to a foreign investor, who after the enactment of section 897 rearranged their investments so as to come under a treaty which would exempt the gain from U.S. tax. While most, if not all, of the transactions are already covered by the present statute because of the great latitude given to the Secretary of the Treasury to prescribe regulations to prevent tax avoidance, clarification will help avoid any misunderstandings.

*Application of Treaties.*—Public Law 96-499 provided that existing treaties will take precedence over the real estate legislation until January 1, 1985. However, if a new treaty is negotiated to resolve conflicts with this legislation, the provisions of the old treaty will apply for a maximum period of 2 years after the new treaty is signed. However, if the new treaty is ratified earlier, the period may be shorter. The effect of this effective date provision on treaties with countries with which we already signed a treaty is unclear.

The amendment would make clear that, in order for a new treaty to begin the 2-year period, it must have been signed on or after January 1, 1981, and before January 1, 1985. It also makes clear that the old treaty with that country will take precedence over the legislation for 2 years after the new treaty is signed, even if that 2-year period ends after December 31, 1984. If a new treaty was signed before January 1, 1981, the old treaty will continue to apply until December 31, 1984, or, if earlier, until the new treaty is ratified.

*Effective Date.*—These provisions apply to dispositions after June 18, 1980.

*Conference agreement.*—The Senate recedes with respect to withholding. The conference agreement follows the Senate amendment with respect to the technical amendments.

The statute provides for the override of certain nonrecognition provisions of the Code, and for the continued application of treaties until 1985. However, it was never intended that these provisions be manipulated so as to make the provisions of the legislation, in effect, elective until 1985. Accordingly, the conferees agree with the Senate that the statute should be clarified to reiterate Congress' original intent to collect at least one tax on the transfer of U.S. real property interests by foreign investors. Congress provided a grace period of tax exemption until January 1, 1985, to certain foreign investors who were residents of a treaty country on the date section 897 became effective. However, it was not Congress' intent to grant such an exemption to a foreign investor, who after the en-



actment of section 897 rearranged his investment so as to come under a treaty which would exempt the gain from U.S. tax while these transactions are already covered by the present statute because of the great latitude given to the Secretary of the Treasury to prescribe regulations to prevent tax avoidance. The conferees agreed that clarification of these provisions will help avoid any misunderstandings.

#### 96. Payout requirement of private foundations

*House bill.*—No provision.

*Senate amendment.*—Under present law, private foundations (other than operating foundations) are required to distribute annually the greater of their minimum investment return or their adjusted net income, less certain taxes (sec. 4942). The minimum investment return basically is 5 percent of the foundation's net investment assets. Under the definition of an operating foundation, the foundation is required (among other requirements) to spend for charitable purposes substantially all of its adjusted net income (sec. 4942(j)).

The Senate amendment reduces the required payout for private foundations so that they must distribute only their minimum investment return. The Senate amendment also provides a comparable amendment to the definition of an operating foundation. The Senate amendment is effective for taxable years beginning after December 31, 1980.

*Conference agreement.*—The conference agreement follows the Senate amendment, but delays the effective date of the amendment one year until taxable years beginning after December 31, 1981, and clarifies the comparable amendment to the definition of an operating foundation.

#### 97. Imputed interest rates on installment sales

*House bill.*—No provision.

*Senate amendment.*—Section 483 requires that a minimum portion of payments under an installment sales contract be treated as interest. The current rate used for this purpose is 10 percent in the case of contracts that do not provide for at least 9 percent interest.

The Senate amendment provides a special 7-percent maximum rate of imputed interest for sales of non-depreciable property for less than \$2 million.

*Conference agreement.*—The conference agreement adopts a modified form of the Senate amendment. Under the provision, the maximum rate of imputed interest on qualified sales of land is 7 percent. An installment sale of land qualifies for this lower rate if the installment sale takes place between members of the same family (within the meaning of sections 453(f) and 318(a)(1)) and if the sales price of property sold or exchange between the same family members during the calendar year does not exceed \$500,000. If the \$500,000 limit is exceeded, the lower rate is available only as to the first sales or exchanges up to the limit.

#### 98. Bad debt deduction of commercial banks

*House bill.*—No provision.

*Senate amendment.*—Under present law, commercial banks compute their bad debt deductions under either the experience method or the percentage of outstanding loans method (sec. 585).

Under the Tax Reform Act of 1969, the percentage of outstanding loans method is phased out over an 18-year period. Under the phase-out of the method, bad debt deductions generally are permitted to the extent necessary to increase the bad debt reserve to the following percentages of eligible outstanding loans: 1969 to 1975, 1.8 percent; 1976-1981, 1.2 percent; and 1982-1987, 0.6 percent. After 1987, the bad debt deduction of commercial banks is to be computed under the experience method.

The Senate amendment provides that the applicable percentage under the percentage of eligible loans is to be 1.0 percent for taxable years beginning in 1982 instead of the 0.6 percent provided by present law. For years after 1982 and before 1988, the applicable percentage will be 0.6 percent.

*Conference agreement.*—The conference agreement follows the Senate amendment.

#### 99. House heating oil credit

*House bill.*—No provision.

*Senate amendment.*—A credit is allowed in 1981 for home heating costs. The credit is calculated by multiplying heating costs by 40 percent of the increase in the Consumer Price Index. The maximum allowable credit is \$200 and phases out as the taxpayer's adjusted gross income increases from \$15,000 to \$25,000. Special rules are provided for households with more than one person and for tenants who do not pay separately for heating.

*Conference agreement.*—The conference agreement follows the House bill.

#### 100. Deduction for gifts and awards

*House bill.*—No provision.

*Senate amendment.*—Present law generally disallows deductions for business gifts to the extent that the cost of all gifts to the same individual during the taxable year exceeds \$25. This general rule does not apply, however, to items costing \$100 or less which are awarded to an employee by reason of length of service or for safety achievement.

The Senate amendment increases the ceiling on the deductibility of employee awards, and expands the purposes for which they may be given. The amendment allows employee awards for length of service, productivity, or safety achievement, and increases the ceiling from \$100 to \$400 per item. The amendment also allows a deduction for such awards to the extent that the item is awarded as part of a permanent, written plan or program that does not discriminate in favor of officers, shareholders, or highly compensated employees as to eligibility or benefits. A deduction is allowed for such plan awards only if the average cost of all awards under the plan during the taxable year does not exceed \$400. However, no deduction may be claimed under such an award plan or program to the extent the cost of an item exceeds \$1,600. The amendment is effective for taxable years ending after the date of enactment.

*Conference agreement.*—The conference agreement follows the Senate amendment.

### 101. Reorganizations involving financially troubled thrift institutions

*House bill.*—Under present law, there is a nonstatutory requirement applicable to tax-free mergers and other reorganizations (commonly called the “continuity of interest” requirement) that the shareholders of the acquired corporation receive stock in the acquiring corporation. Present law is unclear as to how this continuity of interest requirement applies to reorganizations involving a mutual thrift institution. Present law also imposes limitations on the use of pre-reorganization net operating loss carryovers where shareholders of the acquired corporation are not shareholders of the surviving corporation in a merger or other reorganizations (sec. 382). Further, under present law, distributions out of excess bad debt reserves of buildings and loan associations are recaptured as ordinary income (sec. 593(e)). Finally, under present law, contributions to capital by nonshareholder are excluded from the income of a recipient corporation (see 118), but the basis of property is reduced by such contributions (sec. 362(c)).

The House bill allows tax-free reorganizations of thrift institutions undertaken in connection with a case under jurisdiction of the Federal Home Loan Bank Board or Federal Savings and Loan Insurance Corporation (or where neither has supervisory authority, an equivalent state authority) without regard to the “continuity of interest” requirement.

Institutions to which this rule applies are building and loan associations, cooperative banks, and mutual savings banks (i.e., thrift institutions to which sec. 593 applies). The amendment covers all possible combinations of stock and mutual thrift institutions, i.e., stock acquiring mutual, stock acquiring stock, mutual acquiring mutual, and mutual acquiring stock. The amendment applies to these combinations where the appropriate agency certifies that one of the grounds in section 1464(d)(6)(A) (i) (ii) or (iii) of title 12 of the U.S. Code exists. The amendment requires that substantially all the assets of the transferor be acquired by the transferee and that substantially all of the liabilities of the transferor, including deposits, immediately before the transfer become liabilities of the transferee. The amendment removes the requirement that stock or securities in the transferee corporation be received or distributed in the transaction. No inference is intended by the amendment concerning the proper tax treatment of supervisory mergers under existing law or concerning the extent to which the continuity of interest requirement will be considered satisfied in acquisitions outside the scope of the amendment.

The bill provides that, in applying section 382(b) to operating loss carryovers to the surviving corporation after a reorganization of a thrift institution which has been certified by the appropriate agency as described above, deposits in the acquired corporation which become deposits in the transferee are treated as stock of both corporations. Deposits in the transferee are also treated as stock for this purpose.

Under the bill, the recapture rule for distributions out of excess bad debt reserves does not apply to distributions to the Federal Savings and Loan Insurance Corporation with respect to an interest in a thrift institution received in exchange for financial assistance. The exclusion from recapture applies whether or not the in-

terest may be treated as an equity interest under applicable tax law rules.

The bill excludes from income of a building and loan association all money or property contributed to the thrift institution by the Federal Savings and Loan Insurance Corporation under its financial assistance program without reduction in basis of property. The amendment applies to assistance payments whether or not the association issues either a debt or equity instrument in exchange therefore. No inference is intended as to the proper treatment of Federal Savings and Loan Insurance Corporation assistance payments under prior law with respect to whether they are excluded from income or require a basis reduction.

The amendments apply with respect to transfers in reorganization, distributions by building and loan associations, and payments by the Federal Savings and Loan Insurance Corporation on or after January 1, 1981.

**Senate amendment.**—The Senate amendment is the same as the House bill, except that the exclusion from the recapture rule applied to all distributions with respect to interests originally received by the Federal Savings and Loan Corporation.

**Conference agreement.**—The conference agreement follows the House bill and adds the requirement that only distributions in redemption will escape section 593(e) recapture. Thus, the exclusion will not apply to payments of interest to the Federal Savings and Loan Insurance Corporation by the building and loan association. The conferees intend that section 269 will apply as under current law to reorganizations covered by the amendment. The conferees understand that, in applying section 269 to such acquisitions, depositors in a thrift institution to which section 593 applies will be treated as shareholders and deposits in the institution will be treated as stock. The conferees understand that no certification will be made by the appropriate agency on the grounds set forth in 12 USC section 1464(d)(6)(A) (ii) or (iii) unless it is determined that the transferor is unable to meet its obligations as they become due or will be unable to do so in the immediate future.<sup>1</sup> The conferees understand that no certification will be made by the appropriate agency where it is determined that the association has intentionally placed itself in the position where one of the grounds for certification would otherwise apply.

## 102. Tax treatment of mutual savings banks that convert to stock associations

**House bill.**—No provision.

**Senate amendment.**—Under present law, building and loan associations, cooperative banks, and nonstock mutual savings banks compute their bad debt deduction under a special set of rules (sec. 593). Under one of these rules, called the percent of taxable income method, these institutions are allowed a bad debt deduction equal to 40 percent of the institution's taxable income (computed without regard to the bad debt deduction). However, in order to qualify for the full amount of this deduction, at least 82 percent of its assets in the case of a building and loan association or cooperative bank, or

<sup>1</sup> Notwithstanding the fact that the appropriate agency can make a certification required by this amendment only on the grounds that the institution can or will not be able to meet its obligations, the appropriate agency may nevertheless appoint a receiver on any of the grounds set forth in 12 USC sections 1464(d)(6)(A) (ii) or (iii).

72 percent of its assets in the case of mutual savings banks, must be invested in certain assets (hereafter called "qualified assets"). The 40 percent is reduced under a formula to the extent that the percentage of qualified assets is less than the 82- or 72-percent levels. The reduction in the case of building and loan associations and cooperative banks is three-fourths of one percent for each percentage point that the percent of qualified assets is less than 82 percent of all assets. The reduction in the case of mutual savings banks is 1½ percent for each percentage point that the percent of qualified assets is less than 72 percent of all assets.

Present law also provides rules which recapture excess bad debt deductions to building and loan associations when there are dividends in excess of post-1951 earnings and profits or when there are liquidations or redemptions of stock (sec. 593(e)). Finally, present law permits mutual savings banks to compute the tax on their life insurance business as if the life insurance business was in a separate corporation subject to the special rules applicable to life insurance companies (sec. 594).

The Senate amendment makes two changes which are designed to facilitate the conversion of mutual savings banks into stock associations. These amendments apply to both mutual savings banks which convert into stock associations and to newly formed stock associations so long as the institution is operated as a savings institution and is subject to the same Federal or State regulatory scheme as a mutual savings bank chartered under Federal or State law, as the case may be. First, the Senate amendment provides that a stock association which is subject to the same regulation as a mutual savings bank is to be treated as a mutual savings bank and, thus, is eligible to compute its bad debt deduction under section 593. However, consistent with the treatment of building and loan associations which may be organized as stock associations, such stock associations would compute their bad debt deduction under the percentage of eligible loan method under the same rules applicable to building and loan associations (i.e., 82 percent of their assets would have to be invested in qualified assets in order to receive the full 40-percent deduction and the reduction would be at three-fourths of one percent rate). Similarly, the Senate amendment requires recapture of excess bad debt deductions by such stock associations in the same manner as building and loan associations (sec. 593(e)).

Second, the Senate amendment extends the special rule under which mutual savings banks can compute their tax on life insurance business as if it were a separate corporation to stock associations which are regulated as mutual savings banks. The Senate amendment also clarifies that amounts paid to depositors of such stock associations are deductible to the same extent as mutual savings banks (sec. 591).

**Conference agreement.**—The conference agreement follows the Senate amendment.

### 103. Restricted property

**House bill.**—Under present law, property transferred to an employee as compensation for services is taxable at the time the property is not subject to a substantial risk of forfeiture or is transferable. The Tax Court has ruled that the provisions of section 16(b) of the Securities and Exchange Act of 1934 do not restrict transferabi-

lity for this purpose. Under the House bill, the provisions of section 16(b) are taken into account to postpone taxation until the provisions no longer may apply. A similar rule applies to certain restrictions under the SEC accounting rules. The House bill is effective for taxable years ending after December 31, 1981.

*Senate amendment.*—No provision.

*Conference agreement.*—The conference agreement follows the House bill.

#### 104. Deduction for certain adoption expenses

*House bill.*—No provision.

*Senate amendment.*—Under present law, expenses that are paid or incurred in connection with the adoption of a child are nondeductible, personal expenses. The Senate amendment permits taxpayers to deduct from gross income (that is, the deduction is available whether or not taxpayers itemize deductions) up to \$1,500 of the expenses that are paid or incurred in connection with the adoption of a qualified child (generally a hard to place child).

Adoption expenses that are eligible for the deduction are reasonable and necessary adoption fees, court costs, attorney fees, and other expenses that are directly related to the legal adoption of a qualified child. The Senate amendment applies to taxable years beginning after December 31, 1980.

*Conference agreement.*—The conference agreement follows the Senate amendment with modifications that limit the deduction to taxpayers who itemize deductions and define eligible expenses in terms of the Social Security Act adoption assistance program. Under the agreement, adoption expenses are allowable in the case of children who have been found by the State to be eligible for adoption assistance on the basis that they are children with special needs, i.e., that there is a specific factor which leads the State to conclude that they cannot be placed without adoption assistance. (Adoption assistance under the Social Security Act provides an ongoing maintenance payment but does not reimburse adoption expenses.)

#### 105. Separate report on social security trust funds

*House bill.*—No provision.

*Senate amendment.*—Reports on the receipts, outlays, surplus or deficit, and reserve balance of each of the 3 social security trust funds are included in the President's annual budget submission in January in a separate section of the budget. The information is brought up to date in sections within the context of the (July 15) mid-session budget review. In addition, the Board of Trustees publishes an annual report on the financial status of the trust funds and includes in the report its current estimates of the short-run and long-run actuarial balances of each trust fund.

The amendment requires the President, in the annual budget message and mid-session review, to include a separate statement which contains a summary of his requests for new budget authority, and estimates of outlays, revenues, and surplus or deficit of the Federal Old-Age and Survivors Insurance, Federal Disability Insurance, and Federal Hospital Insurance trust funds. The separate statement will show the revenues, outlays, and surplus or deficit estimates for the trust funds, will describe the economic assumptions that were used in making the estimates for the trust funds

and the relationship to economic assumptions made for other parts of the budget, will indicate the financial prospects of the trust funds, and will present a comparative summary of the 3 trust funds with all the other portions of the unified budget. This report will be in addition to the usual budget submission which includes the budget estimates for the trust funds within the unified budget estimates.

*Conference agreement.*—The conference agreement follows the House bill.

#### 106. Congressional Budget Office reports on state of the economy

*House bill.*—No provision.

*Senate amendment.*—The Congressional Budget Office reports to the House and Senate Budget Committees, by April 1 of each year, on the economic outlook and related fiscal policy and Budget matters. The report covers the President's budget submission and relevant alternative considerations. In addition, CBO submits additional reports relating to the economy and fiscal and budget policy, as may be necessary during the year.

In the Senate amendment, the CBO is to report to Congress quarterly on the extent that the purposes and goals of the Economic Recovery Tax Act of 1981 and the Omnibus Reconciliation Act of 1981 are being accomplished. If expectations of economic performance are not realized, CBO is instructed to recommend available options and actions that may be taken to improve economic performance. The first report is due by January 31, 1982. In the event of negative real growth in two successive quarters, CBO is to submit monthly reports.

*Conference agreement.*—The conference agreement follows the House bill.

#### 107. Level of interest rates

*House bill.*—No provision.

*Senate amendment.*—Since persistent high interest rates have meant reduced credit for small commercial, financial, industrial and construction enterprises and the recent increase in merger activity in all areas is being financed with massive lines of credit, the Senate amendment declares that it is the Sense of the Senate that the President should adopt policies to ensure the independence, credit availability, and financial health of small enterprises, the Federal Reserve Board should exercise its regulatory power to require that loans be used for productive purposes rather than business mergers, and the President, Federal Reserve Board, and Congressional Budget Office should report annually on the actions taken to implement these policies and the degree of success or failure, beginning on January 1, 1982, and by January 1 of each subsequent year.

*Conference agreement.*—The conference agreement follows the House bill.

#### 108. Limitation on revenue losses

*House bill.*—No provision.

*Senate amendment.*—The Senate amendment, in a Sense of the Senate resolution, provides that the revenue loss in the bill should not be greater than—

Fiscal year:	<i>Revenue loss (billions)</i>
1981 .....	-\$1.5
1982 .....	-38.3
1983 .....	-91.8
1984 .....	-150.0

As passed by the Senate, revenue losses under the bill were estimated as—

Fiscal year:	<i>Revenue loss (billions)</i>
1981 .....	-\$1.5
1982 .....	-37.7
1983 .....	-91.0
1984 .....	-148.6

**Conference agreement.**—The conference agreement follows the House bill.

### 109. Interfund borrowing among social security trust funds

**House bill.**—No provision.

**Senate amendment.**—The Senate amendment includes a resolution that it is the Sense of the Senate that the Senate Finance Committee report a bill to the Senate by November 15, 1981, which would authorize interfund borrowing among the social security trust funds, or other such measures as may be required.

**Conference agreement.**—The conference agreement follows the House bill.



## II. ESTIMATED REVENUE EFFECTS OF THE CONFERENCE AGREEMENT

Table 1.—SUMMARY OF ESTIMATED REVENUE EFFECTS OF THE PROVISIONS OF H.R. 4242 AS APPROVED BY THE CONFERENCE COMMITTEE, FISCAL YEARS 1981-86

(In millions of dollars)

Provision	1981	1982	1983	1984	1985	1986
Individual income tax provisions .....	-39	-26,929	-71,098	-114,684	-148,237	-196,143
Business tax cut provisions .....	-1,562	-10,657	-18,599	-28,275	-39,269	-54,468
Energy tax provisions .....		-1,320	-1,742	-2,242	-2,837	-3,619
Savings incentive provisions .....		-263	-1,821	-4,215	-5,740	-8,375
Estate and gift tax provisions .....		-204	-2,114	-3,218	-4,248	-5,568
Tax straddles provisions <sup>1</sup> .....	37	623	327	273	249	229
Administrative provisions .....		1,182	2,048	1,856	718	592
Miscellaneous provisions .....	-1	-88	267	561	61	-275
<b>Total Revenue Effect .....</b>	<b>-1,565</b>	<b>-37,656</b>	<b>-92,732</b>	<b>-149,944</b>	<b>-199,303</b>	<b>-267,627</b>

<sup>1</sup> See footnote 9 for table 2

Table 2.—ESTIMATED REVENUE EFFECTS OF THE PROVISIONS OF H.R. 4242 AS APPROVED BY THE CONFERENCE COMMITTEE, FISCAL YEARS 1981-86

(In millions of dollars)

Provision	1981	1982	1983	1984	1985	1986
<b>Individual income tax provisions:</b>						
Rate cuts <sup>1</sup> .....		-25,793	-65,703	-104,512	-122,652	-143,832
20 percent rate on capital gains for portion of 1981 .....	-39	-355				
Deduction for two-earner married couples .....		-419	-4,418	-9,090	-10,973	-12,624
Indexing .....					-12,941	-35,848
Child and dependent care credit .....		-19	-191	-237	-296	-356
Charitable contributions deduction for nonitemizers .....		-26	-189	-219	-681	-2,696
Rollover period for sale of residence .....	( <sup>3</sup> )	( <sup>4</sup> )	( <sup>4</sup> )	( <sup>4</sup> )	( <sup>4</sup> )	( <sup>4</sup> )
Increased exclusion on sale of residence .....	( <sup>3</sup> )	-18	-53	-63	-76	-91
Changes in taxation of foreign earned income .....		-299	-544	-563	-618	-696
<b>Total, individual tax reductions .....</b>	<b>-39</b>	<b>-26,929</b>	<b>-71,098</b>	<b>-114,684</b>	<b>-148,237</b>	<b>-196,143</b>
<b>Business tax cut provisions:</b>						
Capital cost recovery provisions .....	-1,503	-9,569	-16,796	-26,250	-37,285	-52,797
Corporate rate reductions .....		-116	-365	-521	-565	-610
Credit for rehabilitation expenditures .....	-9	-129	-208	-239	-302	-409
Credit for used property .....	-24	-61	-74	-85	-137	-198
Credit for increasing research activities .....		-448	-708	-858	-847	-485
Permit complete allocation to domestic deductions of all domestically performed R&D .....		-57	-120	-62	( <sup>2</sup> )	
Charitable contributions of scientific property used for research .....	( <sup>2</sup> )	( <sup>2</sup> )	( <sup>2</sup> )	( <sup>2</sup> )	( <sup>2</sup> )	( <sup>2</sup> )
Increase in accumulated earnings credit .....		( <sup>2</sup> )	-33	-36	-40	-44
Subchapter S shareholders .....		( <sup>2</sup> )	( <sup>2</sup> )	( <sup>2</sup> )	( <sup>2</sup> )	( <sup>2</sup> )
LIFO inventories and small business accounting .....		-68	-184	192	-145	-64
Reorganizations of certain savings and loan associations <sup>5</sup> .....	( <sup>2</sup> )	( <sup>2</sup> )	( <sup>2</sup> )	( <sup>2</sup> )	( <sup>2</sup> )	( <sup>2</sup> )
Commercial bank bad debt deduction .....		-15	-15			
Conversion of mutual savings banks .....	-5	-10	-12	-18	-22	-25
Extension and modification of targeted jobs tax credit .....		-63	-13	57	117	161
Incentive stock options .....	( <sup>2</sup> )	( <sup>2</sup> )	( <sup>2</sup> )	( <sup>2</sup> )	11	21
Motor carrier operating rights <sup>6</sup> .....	-21	-121	-71	-71	-54	-18
<b>Total, business tax cut provisions .....</b>	<b>-1,562</b>	<b>-10,657</b>	<b>-18,599</b>	<b>-28,275</b>	<b>-39,269</b>	<b>-54,468</b>
<b>Energy provisions</b>						
\$2,500 royalty credit for 1981, exemption for 1982 and thereafter .....		-1,220	-947	-986	-1,193	-1,279
Reduction in tax of newly discovered oil .....		-75	-255	-520	-867	-1,528
Exempt independent producer stripper well oil .....			-525	-721	-762	-797
Exemption from windfall profit tax for child care agencies .....		-25	-15	15	15	15
<b>Total, energy provisions .....</b>		<b>-1,320</b>	<b>-1,742</b>	<b>-2,242</b>	<b>-2,837</b>	<b>-3,619</b>
<b>Savings incentives provisions <sup>7</sup></b>						
Individual retirement savings .....		-229	-1,339	1,849	-2,325	-2,582
Self-employed plans .....		-56	-157	-173	-183	-201
Exclusion of interest on certain savings certificates .....		-398	-1,791	-1,142		
15 percent net interest exclusion .....					-1,124	-3,126
Repeal of \$200 exclusion of interest and return to prior law \$100 dividend exclusion .....		566	1,916			

Table 2.—ESTIMATED REVENUE EFFECTS OF THE PROVISIONS OF H.R. 4242 AS APPROVED BY THE CONFERENCE COMMITTEE, FISCAL YEARS 1981-86—Continued

(In millions of dollars)

Provision	1981	1982	1983	1984	1985	1986
Reinvestment of dividends in public utility stock .....		-130	-365	-416	-449	-278
Employee stock ownership plans.....		( <sup>2</sup> )	-61	-628	-1,659	-2,188
Group legal service plans.....		-16	-24	-7		
Total, savings incentives provisions.....		-263	-1,821	-4,215	-5,740	-8,375
Estate and gift tax provisions:						
Increase in unified credit.....		( <sup>2</sup> )	-1,077	-1,981	-2,811	-3,834
Reduction in maximum rates of tax.....		( <sup>2</sup> )	-172	-371	-556	-890
Unlimited marital deduction.....		( <sup>2</sup> )	303	-304	-311	-300
Current use of certain farm etc., real property.....		-18	-280	-295	-326	-319
Extensions of time for payment of estate tax.....		( <sup>2</sup> )	-20	-16	-15	-12
Tax treatment of contributions of works of art, etc.....		( <sup>2</sup> )	( <sup>2</sup> )	( <sup>2</sup> )	( <sup>2</sup> )	( <sup>2</sup> )
Transfers of gifts with 3 years of death.....		( <sup>2</sup> )	-58	-50	-42	-38
Repeal of deduction for bequests to minor children.....		( <sup>8</sup> )	( <sup>8</sup> )	( <sup>8</sup> )	( <sup>8</sup> )	( <sup>8</sup> )
Increase in annual gift tax exclusion.....		-123	-204	-201	-187	-175
Annual filing and payment of gifts taxes.....		-63	( <sup>2</sup> )	( <sup>2</sup> )	( <sup>2</sup> )	( <sup>2</sup> )
Total, estate and gift tax provisions.....		-204	-2,114	-3,218	-4,248	-5,568
Tax straddles <sup>9</sup> .....	37	623	327	273	249	229
Administrative provisions:						
Changes in interest rate for overpayments and underpayments.....		100	( <sup>2</sup> )	100	-100	60
Changes in certain penalties.....	( <sup>8</sup> )	( <sup>8</sup> )	( <sup>8</sup> )	( <sup>8</sup> )	( <sup>8</sup> )	( <sup>8</sup> )
Cash management—changes in estimated tax payment requirements for large corporations.....		614	1,522	1,190	201	-142
Individual threshold for filing estimated payments increased to \$500.....		-44	-29	-38	-40	-38
Financing of railroad retirement system.....		512	555	604	657	712
Total, administrative provisions.....		1,182	2,048	1,856	718	592
Miscellaneous provisions:						
State legislators travel expenses.....		-9	-5	-6	-6	-7
Taxation of investment income of campaign funds.....	( <sup>2</sup> )	( <sup>2</sup> )	( <sup>2</sup> )	( <sup>2</sup> )	( <sup>2</sup> )	( <sup>2</sup> )
Tax-exempt bonds for volunteer fire departments.....		( <sup>10</sup> )	( <sup>10</sup> )	( <sup>10</sup> )	( <sup>10</sup> )	( <sup>10</sup> )
Charitable contributions by corporations.....		-44	-93	-102	-112	-123
Unemployment tax status of fishing boat services.....		( <sup>10</sup> )				
Excise tax on telephone service.....			435	766	309	
Amortization of construction period interest and taxes.....		-14	-33	-27	-23	-21
Amortization of low-income housing rehabilitation expenditures.....	-1	-8	-16	-25	-35	-39
Foreign investment in U.S real property.....	( <sup>2</sup> )	( <sup>2</sup> )	( <sup>2</sup> )	( <sup>2</sup> )	( <sup>2</sup> )	( <sup>2</sup> )
Payout requirements of private foundations.....	( <sup>2</sup> )	( <sup>2</sup> )	( <sup>2</sup> )	( <sup>2</sup> )	( <sup>2</sup> )	( <sup>2</sup> )
Imputed interest rates on installment sales.....	( <sup>2</sup> )	( <sup>2</sup> )	( <sup>2</sup> )	( <sup>2</sup> )	( <sup>2</sup> )	( <sup>2</sup> )
Deduction for gifts and awards.....		-4	-5	-6	-7	-9
Industrial development bonds for mass transit.....		( <sup>10</sup> )	-7	-29	-54	-64
Deduction for certain adoption expenses.....		-9	-9	-10	-11	-12

Table 2.—ESTIMATED REVENUE EFFECTS OF THE PROVISIONS OF H.R. 4242 AS APPROVED BY THE CONFERENCE COMMITTEE, FISCAL YEARS 1981-86

(In millions of dollars)

Provision	1981	1982	1983	1984	1985	1986
<b>Individual income tax provisions:</b>						
Rate cuts <sup>1</sup> .....		-25,793	-65,703	-104,512	-122,652	-143,832
20 percent rate on capital gains for portion of 1981 .....	-39	-355				
Deduction for two-earner married couples .....		-419	-4,418	-9,090	-10,973	-12,624
Indexing .....					-12,941	-35,848
Child and dependent care credit .....		-19	-191	-237	-296	-356
Charitable contributions deduction for nonitemizers .....		-26	-189	-219	-681	-2,696
Rollover period for sale of residence .....	( <sup>3</sup> )	( <sup>4</sup> )	( <sup>4</sup> )	( <sup>4</sup> )	( <sup>4</sup> )	( <sup>4</sup> )
Increased exclusion on sale of residence .....	( <sup>3</sup> )	-18	-53	-63	-76	-91
Changes in taxation of foreign earned income .....		-299	-544	-563	-618	-696
<b>Total, individual tax reductions .....</b>	<b>-39</b>	<b>-26,929</b>	<b>-71,098</b>	<b>-114,684</b>	<b>-148,237</b>	<b>-196,143</b>
<b>Business tax cut provisions:</b>						
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Credit for used property .....	-24	-61	-74	-85	-137	-198
Credit for increasing research activities .....		-448	-708	-858	-847	-485
Permit complete allocation to domestic deductions of all domestically performed R&D .....		-57	-120	-62	( <sup>2</sup> )	
Charitable contributions of scientific property used for research .....	( <sup>2</sup> )	( <sup>2</sup> )	( <sup>2</sup> )	( <sup>2</sup> )	( <sup>2</sup> )	( <sup>2</sup> )
Increase in accumulated earnings credit .....		( <sup>2</sup> )	-33	-36	-40	-44
Subchapter S shareholders .....		( <sup>2</sup> )	( <sup>2</sup> )	( <sup>2</sup> )	( <sup>2</sup> )	( <sup>2</sup> )
LIFO inventories and small business accounting .....		-68	-184	-192	-145	-64
Reorganizations of certain savings and loan associations <sup>5</sup> .....	( <sup>2</sup> )	( <sup>2</sup> )	( <sup>2</sup> )	( <sup>2</sup> )	( <sup>2</sup> )	( <sup>2</sup> )
Commercial bank bad debt deduction .....		-15	-15			
Conversion of mutual savings banks .....	-5	-10	-12	-18	-22	-25
Extension and modification of targeted jobs tax credit .....		-63	-13	57	117	161
Incentive stock options .....	( <sup>2</sup> )	( <sup>2</sup> )	( <sup>2</sup> )	( <sup>2</sup> )	11	21
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<b>Total, business tax cut provisions .....</b>	<b>-1,562</b>	<b>-10,657</b>	<b>-18,599</b>	<b>28,275</b>	<b>-39,269</b>	<b>-54,468</b>
<b>Energy provisions</b>						
\$2,500 royalty credit for 1981, exemption for 1982 and thereafter .....		-1,220	-947	-986	-1,193	-1,279
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Exempt independent producer stripper well oil .....			-525	-721	-762	-797
Exemption from windfall profit tax for child care agencies .....		-25	-15	-15	-15	-15
<b>Total, energy provisions .....</b>		<b>-1,320</b>	<b>-1,742</b>	<b>-2,242</b>	<b>-2,837</b>	<b>-3,619</b>
<b>Savings incentives provisions <sup>7</sup></b>						
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Exclusion of interest on certain savings certificates .....		-398	-1,791	-1,142		
15 percent net interest exclusion .....					-1,124	-3,126
Repeal of \$200 exclusion of interest and return to prior law \$100 dividend exclusion .....		566	1,916			

Table 2.—ESTIMATED REVENUE EFFECTS OF THE PROVISIONS OF H.R. 4242 AS APPROVED BY THE CONFERENCE COMMITTEE, FISCAL YEARS 1981-86—Continued

(In millions of dollars)

Provision	1981	1982	1983	1984	1985	1986
Reinvestment of dividends in public utility stock.....		-130	-365	-416	-449	-278
Employee stock ownership plans.....		( <sup>2</sup> )	-61	-628	-1,659	-2,188
Group legal service plans.....		-16	-24	-7		
<b>Total, savings incentives provisions.....</b>		<b>-263</b>	<b>-1,821</b>	<b>-4,215</b>	<b>-5,740</b>	<b>-8,375</b>
<b>Estate and gift tax provisions.</b>						
Increase in unified credit.....		( <sup>2</sup> )	-1,077	-1,981	-2,811	-3,834
Reduction in maximum rates of tax.....		( <sup>2</sup> )	-172	-371	-556	-890
Unlimited marital deduction.....		( <sup>2</sup> )	303	-304	-311	-300
Current use of certain farm etc., real property.....		-18	-280	-295	-326	-319
Extensions of time for payment of estate tax.....		( <sup>2</sup> )	-20	-16	-15	-12
Tax treatment of contributions of works of art, etc.....		( <sup>2</sup> )	( <sup>2</sup> )	( <sup>2</sup> )	( <sup>2</sup> )	( <sup>2</sup> )
Transfers of gifts with 3 years of death.....		( <sup>2</sup> )	-58	-50	-42	-38
Repeal of deduction for bequests to minor children.....		( <sup>8</sup> )	( <sup>8</sup> )	( <sup>8</sup> )	( <sup>8</sup> )	( <sup>8</sup> )
Increase in annual gift tax exclusion.....		-123	-204	-201	-187	-175
Annual filing and payment of gifts taxes.....		-63	( <sup>2</sup> )	( <sup>2</sup> )	( <sup>2</sup> )	( <sup>2</sup> )
<b>Total, estate and gift tax provisions.....</b>		<b>-204</b>	<b>-2,114</b>	<b>-3,218</b>	<b>-4,248</b>	<b>-5,568</b>
Tax straddles <sup>9</sup> .....	37	623	327	273	249	229
<b>Administrative provisions:</b>						
Changes in interest rate for overpayments and underpayments.....		100	( <sup>2</sup> )	100	-100	60
Changes in certain penalties.....	( <sup>8</sup> )	( <sup>8</sup> )	( <sup>8</sup> )	( <sup>8</sup> )	( <sup>8</sup> )	( <sup>8</sup> )
Cash management—changes in estimated tax payment requirements for large corporations.....		614	1,522	1,190	201	-142
Individual threshold for filing estimated payments increased to \$500.....		-44	-29	-38	-40	-38
Financing of railroad retirement system.....		512	555	604	657	712
<b>Total, administrative provisions.....</b>		<b>1,182</b>	<b>2,048</b>	<b>1,856</b>	<b>718</b>	<b>592</b>
<b>Miscellaneous provisions:</b>						
State legislators travel expenses.....		-9	-5	-6	-6	-7
Taxation of investment income of campaign funds.....	( <sup>2</sup> )	( <sup>2</sup> )	( <sup>2</sup> )	( <sup>2</sup> )	( <sup>2</sup> )	( <sup>2</sup> )
Tax-exempt bonds for volunteer fire departments.....		( <sup>10</sup> )	( <sup>10</sup> )	( <sup>10</sup> )	( <sup>10</sup> )	( <sup>10</sup> )
Charitable contributions by corporations.....		-44	-93	-102	-112	-123
Unemployment tax status of fishing boat services.....		( <sup>10</sup> )				
Excise tax on telephone service.....			435	766	309	
Amortization of construction period interest and taxes.....		-14	-33	-27	-23	-21
Amortization of low-income housing rehabilitation expenditures.....	-1	-8	-16	-25	-35	-39
Foreign investment in U.S. real property.....	( <sup>2</sup> )	( <sup>2</sup> )	( <sup>2</sup> )	( <sup>2</sup> )	( <sup>2</sup> )	( <sup>2</sup> )
Payout requirements of private foundations.....	( <sup>2</sup> )	( <sup>2</sup> )	( <sup>2</sup> )	( <sup>2</sup> )	( <sup>2</sup> )	( <sup>2</sup> )
Imputed interest rates on installment sales.....	( <sup>2</sup> )	( <sup>2</sup> )	( <sup>2</sup> )	( <sup>2</sup> )	( <sup>2</sup> )	( <sup>2</sup> )
Deduction for gifts and awards.....		-4	-5	-6	-7	-9
Industrial development bonds for mass transit.....		( <sup>10</sup> )	-7	-29	-54	-64
Deduction for certain adoption expenses.....		-9	-9	-10	-11	-12

Table 2.—ESTIMATED REVENUE EFFECTS OF THE PROVISIONS OF H.R. 4242 AS APPROVED BY THE CONFERENCE COMMITTEE, FISCAL YEARS 1981–86—Continued

[In millions of dollars]

Provision	1981	1982	1983	1984	1985	1986
Total, miscellaneous provisions . . . . .	– 1	– 88	267	561	61	– 275
Grand total all provisions . . . . .	– 1,565	– 37,656	– 92,732	– 149,944	– 199,303	– 267,627

<sup>1</sup> These figures include the increase in outlays attribute to the earned income credit which results from reduction in tax rates. These outlays are \$4 million in fiscal year 1982, \$31 million in 1983, \$44 million in 1984, \$41 million in 1985, and \$38 million in 1986.

<sup>2</sup> Loss of less than \$5 million.

<sup>3</sup> Negligible.

<sup>4</sup> Loss of less than \$10 million.

<sup>5</sup> This estimate is based on limited information about reorganizations that were planned even without this provision. If such reorganizations would have increased markedly without this provision, the revenue loss could be substantial.

<sup>6</sup> Includes a portion of the \$36 million in tax liabilities for calendar year 1980.

<sup>7</sup> These estimates were made using the rate schedule proposed by the bill. This approach results in a lower revenue loss than one that would have been obtained if the present law rates had been used.

<sup>8</sup> Gain of less than \$5 million.

<sup>9</sup> Revenue effects do not reflect transactions entered into after December 31, 1981. Total revenue effects of subsequent years might be affected by judicial decisions interpreting present law.

<sup>10</sup> Loss of less than \$1 million.

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