EXECUTIVE SESSION

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MONDAY, SEPTEMBER 11, 1978

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United States Senate
Committee on Finance
Washington, D.C.

The Committee met, pursuant to recess, at 10:15 a.m. in room 2221, Dirksen Senate Office Building, Hon. Russell B. Long (Chairman of the Committee) presiding.

Present: Senators Long, Talmadge, Byrd, Gravel, Bentsen, Haskell, Moynihan, Curtis, Hansen, Dole, Packwood and Danforth.

The Chairman. Let me call the Committee together.

The staff has done some very good work in getting up a list of suggestions from Senators and as I would have suspected, the Senators have been most imaginative, and we are aware of about 106 things that the Senators would like to do for the benefit of taxpayers that would cost money to the Treasury and, of course, some of them might make a little money for us, but generally speaking these are the various things that Senators would like to do one way or the other.

Some of them are so-called reform items that would bring in some revenue, such as repealing the DISC and others. Also, a different alternative tax, how we might save some of the revenue loss while getting the maximum benefit on a cost-effective basis

1 on some of the things that the House is suggesting, as well as
2 some of the things that we are suggesting.
3 I would like the Senators to study this and it would sort
4 of help if they would indicate their reaction on all of these items
5 considering the fact that, in any event, the things that we want
6 to do are going to cost more than we have the budget authority to
7 do.
8 Recognizing what we are up against, if you would just indicate
9 that, that that is not something that we are going to do, that
10 the majorities of Senators are going to be against it anyway,
11 knowing what our situation is.
12 I would hope that that would help us to work up a proposal
13 that would include at least some proposed suggestions to do as
14 much as we can on what everyone would like to do and leave out
15 the items that would seem to rank as the lowest priorities, all
16 things considered. There are some things that I would vote for
17 here if we could afford it, but we just do not have enough money
18 to do it. I would have to vote against it.
19 I think we need to look at all of this to decide where you
20 would come out. In other words, I know there are suggestions that
21 I, myself, would like to make. Some of them would have to drop
22 by the wayside if we did not have the money to do it.
23 I think everybody else would be willing to take the same
24 attitude. You cannot have your way about everything. You would
25 like to do so much, but if you have only one or two items, then

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1 we would want to zero in on certain ones and likewise, going
2 along with people on their suggestions, if you buy part of it,
3 you should not be expected to buy all of it.
4 This has been distributed. I would appreciate getting your
5 reactions on the things you strongly favor and things you think
6 would have to be of a low priority, and things that you do not
7 think that you could go along with at all.
8 Suppose you take us from there now, Mr. Shapiro, and tell us
9 what you think. I believe Senator Haskell wanted to talk today
10 about his suggestion about, what was it?
11 Senator Haskell. Yes, I would. I apologize for the tone of
12 my voice.
13 The Chairman. You sound like a man running for office.
14 Senator Haskell. What I would like to bring up, Mr. Chairman,
15 on behalf of Mr. Laxalt, Senator Gravel and Senator Matsunaga, is
16 the extension of the jobs tax credit that we adopted last year.
17 I would first like to state that this, in no way, impinges
18 or is in no way contradictory to the targeting credit suggested
19 by the Administration. The targeted credit goes to a special
20 group of people. The targeted credit, the testimony is, could
21 only be available to large business because obviously only they
22 have the facilities to train those people.
23 My credit, or our credit, rather, is an extension of what was
24 adopted last year and basically can be availed of by small business.
25 Now, in the proposal I have, there are several modifications.

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1 First, I would extend it to two years. Second, the credit
2 would be up to $2,100 per new employee. Third, we would eliminate
3 jwo tests that are mathematically not all that difficult, but
4 mathematically burdensome, known as the 102 and 105 percent test.
5 By eliminating those tests, of course, we would increase the
6 revenue loss.
7 Therefore, to keep where we were before, I have decreased
8 from $100,000 to $25,000 the amount any individual businessman
9 or corporation can take.
10 Senator Curtis. Would you answer a question right there?
11 Would you review, refresh our memory, as to what the present law
12 provides in this area you are talking about right now?
13 Senator Haskell. I will. The present law provides that you
14 get the same amount of credit if you increase your FUTA wage base
15 more than 102 percent of a prior year. In addition to that, you
16 would have to meet the 105 percent test, and I would ask Mr.
17 Shapiro to refresh me. The 105 percent test is what?
18 Mr. Shapiro. That is a test that limits the availability of
19 the credit, as long as the wages exceed 105 percent of the year
20 before. The idea is if you did not have such a test you could have
21 just an existing payroll, increases in payroll, but no new
22 employees. So you would have some adjustment.
23 If you had an existing number of employees and they were under
24 the limit, you just raise their salaries, but you would not get a
25 general jobs credit for hiring more employees. So you go a certain

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1 percentage above the prior year's payroll, assuming you are
2 acquiring additional employees.
3 Senator Haskell. The testimony in the hearing, and the
4 reasons for eliminating that, are twofold, Senator Curtis.
5 Number one, the difficulty of projecting whether you are going
6 to get the credit or not when you add a new employee. Number two,
7 it was uniformly testified to that it just is economically
8 inefficient to hire and fire employees. It takes a considerable
9 break-in time, as I am sure the Senator was aware, and you do not
10 want to hire a Floyd Haskell one month and fire him and then hire
11 Carl Curtis because there is a certain break-in point.
12 By lowering the base, so to speak, for increased employment,
13 it obviously would increase the revenue loss. So to compensate
14 for that and to bring the revenue loss to where it was undrer the
15 prior law, we have reduced our limit to $25,000 as opposed to
16 $100,000.
17 I would like to stress to all members of the Committee that,
18 at the hearings, the Administration did a very bad job of publici-
19 zing this jobs tax credit. The Labor Department did not even try
20 and publicize it at all. The Internal Revenue Service sent out a
21 little slip with the FUTA wage base, but they did a bad job.
22 The Governor of Vermont thought they did such a terrible job
23 that he, on his own initiative, sent out to all employers in
24 Vermont a description of the jobs tax credit.
25 Mr. Chairman and members, I would submit that the jobs tax

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credit is important; that the testimony, both from big business organizations and the National Alliance of Business and small businesses, that 80 percent of the increase in employment was by small business, and also I would like to point out that small business is labor intensive as opposed to capital intensive and the jobs tax credit -- that is, this one -- is basically to small business what the investment tax credit is to large business.

That, I believe, is the simplest and most direct way that I can try to explain it. I will try to answer questions or hear any comments.

The Chairman. Let me just say that the jobs credit, to create more jobs, in my judgment, is a good idea and still is. I would assume we are still going to have a jobs credit, one way or the other. The question is, to what extent should we target the jobs credit on people who are lower income people or people who otherwise would be on welfare, the young people in large measure being excluded from the employment market, especially the young blacks or the young women in cities and that type of thing.

Senator Haskell. If the Chairman would allow me to interrupt, that targeted credit and this credit for small business should basically be considered two separate items, I would submit.

The Chairman. Now, we will have to get the cost together. Could Treasury give me some idea as to what the cost of the two credits are -- this one, plus the one we have in the bill?

One is existing law and the other --

1 Mr. Lubick. The existing law, Mr. Chairman, is $2.5 billion.

2 Senator Hansen. $2.5 billion?

3 Mr. Lubick. $2.5 billion.

4 The House bill, the targeted jobs credit was $523 million
5 for 1979, so roughly speaking, on a calendar year basis, 1979,
6 the general jobs credit is $2.5 billion. The targeted tax credit
7 is a half a billion dollars, so that the savings by moving from
8 the general to the targeted was about $2 billion.

9 Senator Haskell. I guess all of us have our figures. The
10 figures I have for existing law and the jobs credit is $1.9 billion
11 and the figure I have for the amended jobs credit that I proposed,
12 along with others, is $2.1 billion.

13 But, given the difficulties of estimating, that is not too far
14 off.

15 Senator Curtis. May I ask Treasury a question?

16 What would it cost to make the payment of all wages tax deduc-
17 tible to the man who pays them? What I am thinking of, there are
18 many people who would hire someone to paint the buildings round
19 their barn or in their house, clean out the trees, some other
20 things. They might hire some domestic help to help three days a
21 week or a few hours a week.

22 It seems to me that if we wanted to promote the employment of
23 persons, that we would do for wages what we have dome for interest.
24 The payment of interest is a deduction, and it is a great help for
25 people buying homes. But to simplify it and to avoid confusion,

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1 we have deduction of interest for everything, even if they bought
2 something totally non-productive.
3 Do you have any idea what it would cost?
4 Mr. Sunley. Mr. Curtis, we do not have a firm fiture, but
5 maybe something like 3 percent of the wages paid in the United
6 States not associated with trade or business -- paying a ballet
7 teacher for your daughter or paying someone to clean your yard.
8 If that number is about right, the total we decided about $800
9 billion. You are talking about $24 billion to $25 billion for
10 deduction of wages.
11 Senator Curtis. You think so?
12 Mr. Sunley. It must be about $5 billion or $6 billion. I
13 would like to be able to think about it a little bit.
14 The Chairman. How much?
15 Mr. Sunley. It would be about $5 billion, I would say. If
16 I am right, I think total wages paid in the country must be
17 around $800 billion. If 3 percent of those are not part of a
18 trade or business, hiring a child care service, yard-care services
19 or what have you, therefore not currently deductible, that would
20 mean $25 billion in wages not now deductible; assuming the
21 marginal tax rate is about 20 percent, that is about $5 billion.
22 The Chairman. Senator Curtis has made a suggestion on one
23 occasion or the other that, for example, you ought to let people
24 deduct the cost of hiring somebody to help look after some elderly
25 person. If you move these elderly people off into a nursing home,

of course, but assuming the nursing home is paying some taxes, then you can deduct it into the retirement home or something like that -- if it is a private operation, they can deduct it.

But the sad situation is, when you try to keep them in their own homes, then you need somebody to come in and do some housework, do some yard work, fix a meal up for them or bring some food to them, generally speaking that is not deductible.

It is the kind of thing that, from the point of view of human compassion you would want. I know the labor people do not like to let somebody deduct the cost of household help. I think they would be willing to make an exception in the case of the elderly people.

If that someone is in the targeted area, someone you are trying to put back to work, but it is costing you money not having them work, in a case like that you definitely, it seems to me, should allow a credit. This bill does that.

I believe that is putting the targeted area to work, if it meets both standards -- putting people to work that would not otherwise be working and letting people have a deduction where it serves a good purpose, I would think if it meets those two standards it would be worth trying to do.

I would think that we would have a lot of objection where it is just a matter of let us say, a couple who can afford it, or especially if there is just one worker in the family, deduct the cost of help in the house.

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Senator Curtis. Mr. Chairman, we have a number of controversial items in this bill already, so I am not going to press this as a new item, but I do suggest that, if at any time, the government wants a real work program, that that has great possibilities. I would daresay that there would be a large number of chauffeurs hired in the city of Washington if it was tax deductible.

I am not going to push it at this time, Mr. Chairman, and I am not going to take any more time.

The Chairman. Let me just ask this --

Senator Curtis. If you want more people employed, you should create an incentive to employ them.

The Chairman. Let me ask this about the Haskell proposal. Compared to what the House bill would do, what would be the cost of the Haskell proposal, compared to the House bill?

Mr. Shapiro. The tax bill, Senator, has a calendar year effect, as Mr. Lubick indicated, of $500 million. The Haskell proposal would have a calendar year effect of $2.1 billion.

If you added the both together, it would be $2.6 billion, if you had the general plus the targeted.

The Chairman. That would be $2.1 billion over the House bill?

Mr. Shapiro. That is correct.

The Chairman. What Senator Haskell is seeking to do is to keep something that we have in present law that would expire, is that correct?

Mr. Shapiro. That is correct. He has made two provisions

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1 over present law. The present law, if you have the general jobs
2 credit, has a $100,000 cap for businesses that you cannot get a
3 credit of more than $100,000. He would reduce that to $25,000
4 and then there is also a provision of a 105 percent limitation
5 that it would repeal.

6 The central change that he is making, however, is the $25,000
7 limit. That would reduce the revenue from $2.5 billion to $2.1
8 billion.

9 Senator Haskell proposal -- the targeted jobs credit under
10 the House bill is $500 million, so it is $2.1 billion under
11 Senator Haskell's proposal and $500 million under the House bill.

12 Senator Bentsen. Would there not be some overlap? Would
13 it actually end up with the full amount, each being added to the
14 total?

15 Mr. Shapiro. That would depend on the proposal.

16 Senator Haskell. Let me interrupt. I simply would not want
17 that to happen.

18 Mr. Shapiro. I may have misunderstood what Senator Haskell
19 indicated. He said on top of the House bill. I guess what you
20 meant, to the extent you would not want double counting for some-
21 one who would get it for both, so to that extent, it would be
22 $2.1 billion to $2.6 billion.

23 I must say that would cause complexities in trying to work
24 the two programs where you would have to have one formula for
25 the targeted group, another formula for the general group, some

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reviewing of taking out the targeted from the general.

It could work, but it could be a very complicated procedure.

The Chairman. I would hope that we would not have to decide this this morning. The Senator has a good suggestion. I would like to vote for it.

I want to look at this in connection with all of the other suggestions that we have here, and see how much we can work in.

Senator Byrd. Before we leave it, could we get the viewpoint of Treasury on this?

Mr. Lubick. Senator Byrd, we believe that the approach of the House bill is the better approach. It is for a targeted credit that focuses the revenue cost on the serious problems of structural unemployment.

We think that there has been a significant improvement in the unemployment rate generally over the past year, therefore we do not need the general incentive. We are also afraid that the incremental credit, the general credit approach, is of particular use and favors those regions and industries already experiencing growth, and those areas where we have a shrinking employment base, where in effect we really need the stimulus for the employment, do not benefit from the general credit.

So we would prefer to go with the approach of the House bill rather than extend the general credit.

Senator Talmadge. Mr. Chairman?

The Chairman. Senator Talmadge?

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1 Senator Talmadge. As the original author of the Work
2 Incentive Program and the tax credit, I have worked in this area
3 for several years. I would ask that Mr. Galvin look into the
4 proposals carefully and be prepared to comment on them. I think
5 what we all want to do is target it in an area which would be
6 socially beneficial, to try to help people off the weofare
7 program, number one.

8 Number two, I think we ought to try to keep students in
9 school rather than dropping out. Your highest unemployment rate
10 in the country is among the youth in the country -- first blacks
11 and minorities and then white. I think that it ought to be
12 targeted particularly in that area, and I would ask Mr. Galvin to
13 look at it and be prepared to comment on it, and we will vote on
14 this issue then.

15 Senator Haskell. Mr. Chairman, also I would like to have
16 the comment be made as to what would happen if we put, instead of
17 putting it at the over-100 percent level, over 102 percent. My
18 understanding is that would bring it down to $1.4 billion.

19 Let me just stress one thing. The testimony at the hearings
20 was that on the targeted credit, large business could do that.
21 They have the facilities for training people. But small business,
22 that accounts for basically the growth of employment, they just
23 plain do not have the facilities for training the targeted people
24 and I am anxious to give the credit to the small businessman who
25 basically accounts for the increase in employment.

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1 I will not say anything more, but that is my feeling on the
2 subject, and I hope that will be taken into consideration.
3 The Chairman. Maybe we could turn to some other items.
4 Is there anything you particularly want to go to, Mr. Shapiro?
5 Mr. Shapiro. No.
6 The Chairman. Let me direct your attention to Item No. 18
7 which I think we will have to discuss at some point here, which
8 is the maximum tax on earned income.
9 When we went into this earned income matter some years ago
10 I think we made a wise decision. I believe the majority of the
11 people in the country favored what we did in pursuing the concept
12 that a person should not have to pay more than 50 percent of what
13 he makes in earned income -- which, incidentally, was subject to
14 rather strict rules under the old earned income credit that
15 existed before World War II, back where you had a 10 percent
16 allowance for earned income.
17 By that concept, we felt that a person should not pay more
18 than half of what he earns in earned income to the Treasury, and
19 then so we said well, we would hold to that. I think it was the
20 1969 Tax Act.
21 Then it was suggested, well, with regard to a person who
22 has various capital gains and tax preferences, it may be he should
23 not -- that that should count against him. So that, by doing that,
24 we got it to where the earned income credit -- this is the 50
25 percent limitation on earned income that did not do what it was

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1 supposed to do at all.

2 As I understand it, the House has tried to say here that at

3 least the capital gains would not prevent you from getting the

4 benefit of the 50 percent limitation on earned income.

5 Is that right, Mr. Shapiro? Would you explain that a little

6 bit, just how that works out?

7 Mr. Shapiro. I am sorry, Senator. Do you want to know how

8 present law works?

9 The maximum tax on earned income was enacted in 1969 in the

10 Tax Reform Act. It is a 50 percent rate on earned income.

11 What you do is you take your earned income -- I am going to

12 describe the stacking aspect of it -- you take your earned income

13 first. You put all of your investment income on top of that, if

14 you had earned income that would be above the 50 percent rate.

15 Let's assume you have enough earned income without this percen-

16 tage you would be paying 60 percent tax on that amount of earned

17 income. The amount between 50 and 60 percent, that amount of

18 income would be taxed at no greater than 50 percent, rather than

19 60, but then your investment income would be taxed at the levels

20 above that level of earned income.

21 What I am trying to describe as the stacking. All your

22 earned income is taken into account, first on the bottom. All

23 your nonearned income investment comes on the top, which has

24 the effect of taxing your investment income at the rates above

25 50 percent up to 70 percent.

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1 There were times where there was consideration for
2 allowing a portion of the investment income to be stacked at the
3 lower level first so that your earned income could be at the top.
4 Some consideration was made that not all of your investment income,
5 not to reverse the stacking, but maybe an amount of investment
6 income that either equalled earned income or one-half of earned
7 income, but to give some investment income on the bottom of the
8 stacking schedule.
9 The reason for that, when you have enough earned income
10 that will push that investment up to the 70 percent bracket, there
11 is substantial disincentive for making investment which you would
12 have interest and dividends and other types of investment income
13 that would all be taxed at the 70 percent rate.
14 This has been a concern about the way the maximum tax works
15 with regard to investment income.
16 This particular provision, number 18 that Senator Long has
17 reference to, deals with the situation which is related to that,
18 that is, you have some individuals that work in businesses. There
19 is a question whether they are labor-intensive or capital-inten-
20 sive.
21 To the extent they are labor-intensive, it is clear that your
22 income is earned income. However, to the extent that some of your
23 return is based on capital, that is equivalent to a dividend and
24 not earned income.
25 Therefore, when it is not clear whether or not the income

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1 that you have earned is income earned from all of your services
2 or whether it is like dividend income because the capital that
3 you have invested, the '69 Act picked up a rule which previously
4 had been in the law, and still is, with respect to Section 911 --
5 income earned abroad -- which had the same problem.
6 When you have income earned abroad prior to 1976 you had
7 this flat exclusion and there was a question as to how much of that
8 exclusion should be on earned income and how much of that income
9 you earned is related to the capital you invested which had the
10 same effect as dividends.
11 This 30 percent limit was picked up straight from the Section
12 911 and has caused problems in certain businesses where there are
13 legitimate questions as to whether or not the income -- let me
14 give you an example of how it works.
15 The Chairman. Let me just stop you there. This provision
16 is not the particular thing that would seem to me that would be
17 wrong about this. When we put this 50 percent limitation on
18 earned income, in effect -- I was in the conference when it was
19 brought out, and I had the impression that we were saying at that
20 point that of the salary income you earned, you can keep half of
21 it. That is what we are saying.
22 Larry Woodworth, at that point, said do you want to do it
23 this way or that way and I did not understand precisely just what
24 the difference was. I do not th-nk most people did. And we asked
25 him, we will do it this way rather than that way, make people pay

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1 more taxes rather than less.

2 When we answered that question in that fashion, it looks to

3 me that for a great number of people, we just completely negated

4 what we thought we were doing in that conference.

5 For example, if you make, let's say, $30,000 of earned

6 income and when you put that in with your investment income, if

7 you make us put that on the bottom, if you start at the first

8 dollar and work up to $30,000, even if you are a single person

9 that is just getting you up to the 50 percent bracket, is that

10 not right?

11 Mr. Shapiro. Yes.

12 The Chairman. So if you make the taxpayer put that in first,

13 then he does not pay but 50 percent -- the government only takes

14 half of what he has. If he has, let's say, $30,000 of salary

15 income, even though he is going to pay in the 70 percent bracket,

16 what you have done for him is absolutely zero.

17 If you did it the other way around and say he puts all of the

18 other in first and then he puts the $30,000 on last, by that point

19 he is in the 70 percent bracket and that is worth something to

20 him. But the point is, if you go tell somebody well, my friend,

21 I am proud to tell you that I voted to say you do not pay but

22 half, the government only takes half of your earned income, you

23 had better duck as he tries to punch you in the nose, if he is

24 one of the people affected by this, because you did not do any-

25 thing for him. He is paying at 70 percent.

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1 The other thing that people complain about this is what
2 do we do about capital gains? Apparently that is the point where
3 the House tried to take care of it in their bill. Is that right?
4 Mr. Shapiro. Yes.
5 The Chairman. Would you explain what that is? Somehow or
6 other, if he has a capital gain, you do not even do that for him.
7 You do less than zero.
8 Mr. Shapiro. In 1969, when you passed your minimum tax and
9 your maximum tax, you had a maximum tax on income up to 50 percent.
10 Then you passed a minimum tax which included, as one of the
11 preference items, capital gains.
12 One of the provisions that was excluded, however, with
13 regard to the maximum tax was that all the preference items, the
14 total amount of the preference items offset the earned income
15 eligible for the maximum tax on earned income.
16 For example, if you had $100,000 of earned income and you
17 had $50,000 of preference income, you had $50,000 preference
18 income subject to the minimum tax, but at the same time, it would
19 offset the $100,000 of earned income. Instead of getting a
20 maximum tax of 50 percent on $100,000, you would only get a
21 50 percent tax on $60,000.
22 That is what is being referred to as a poison, or offset
23 of preference income, against the maximum tax on earned income.
24 What the House did was eliminate that offset with regard
25 to capital gains. The House bill does continue to offset the

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maximum tax on earned income with other preferences -- accelerated depreciation, percentage depletion. As far as capital gains are concerned, capital gains is no longer a preference item for the minimum tax under the House bill and therefore would also not be an offset against the maximum tax on earned income, either.

Senator Curtis. Suppose an individual earns $30,000 in earned income. He has the capacity to increase that two or three times.

Suppose also he has $45,000 investment income. That is static, remains the same.

Under the present way the law is, he cannot increase his earned income without paying considerably more than 50 percent? Is that correct?

Mr. Shapiro. Senator, let me make sure I understand you correctly. You are talking about $30,000 of earned income today, he can increase his earned income three times?

Senator Curtis. Two or three times.

Mr. Shapiro. To $90,000 earned income?

Senator Curtis. He has decided whether to do that.

Mr. Shapiro. How much investment income?

Senator Curtis. $45,000. He is a single man.

Mr. Shapiro. With $90,000 of earned income, it would be taxed at no greater than a maximum rate of 50 percent. The $45,000 investment income could be taxed at rates up to 70 percent.

Senator Curtis. If they considered the earned income first

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1 he could increase that $30,000 quite a little and still get to
2 keep $1 for every $2 that he earns. But if you put the $45,000
3 into the calculation first, he is not going to have any desire
4 to create, to have that earned income go to $60,000 or $70,000
5 or $90,000.

6 Is that not the problem?

7 Mr. Shapiro. That is the effect of the way that the maximum
8 tax works. That has been a concern that has been expressed by
9 some taxpayers, that by putting the investment on top of earned
10 income, it gets them to the higher rates and they question that
11 70 percent rate would be a disincentive to certain types of
12 investments from their standpoint.

13 Senator Curtis. A disincentive to earnings, is it not?

14 Mr. Shapiro. A disincentive in both regards. It depends
15 whether it is a disincentive to earnings or investment income, to
16 the extent they may decide to keep their earnings and not make
17 investments, because the earnings they get -- in the earnings
18 example, they could get two or three times and pay more than
19 50 percent and that individual may prefer to make the earnings
20 and not make the investment.

21 You can go either way. There is a disincentive. It depends
22 on the individual and the facts and circumstances as to which
23 way the disincentive would work.

24 The Chairman. I would like for the Treasury to help us get
25 some of these facts straight in our mind. We had a witness before

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1 the Committee that had been a former Treasury employee. He made
2 a very impressive statement before the Committee.
3 He was making the point that yes, we have a graduated income
4 tax but it graduates. If you are looking at it by class, it
5 graduates from zero to about 35 percent rather than graduating
6 from, let's say, 14 percent up to 70 percent.
7 I would like for you to take a look at that statement and
8 then say what Treasury thinks really is the case. Because, from
9 the Treasury's point of view, the high bracket taxpayers are not
10 paying 70 percent; they are paying more like 35 percent on the
11 average.
12 I know when we had the study of the so-called enemies list
13 back in the Nixon Administration, one of the tax returns that
14 was on the list was some fellow who was working hard, a very
15 successful man, but the man was paying two-thirds of his income
16 in taxes, and people had studied that and felt a little sympathy
17 for him. And if we do what I hope we will do, we are going to
18 zero-in a lot stronger in this bill on these people who are making
19 a lot of money, in economic terms, and paying less than 15 percent
20 in taxes on income.
21 We will do it to the benefit of those who are not making as
22 much, those who are paying 30 percent or more, or especially those
23 who are paying a 65 percent, would get some relief, while you
24 are trying to get more income out of those who are getting by
25 with paying very little.

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If Treasury will agree with us, what you are really collecting by what that witness said, or if you want to give us your own figures, what do you think we are collecting by classes of these people? Then we can come nearer to moving towards equal justice than shooting out blind, assuming those people are paying 70 percent of income in taxes.

What do you think you are collecting on the $200,000 and above taxpayers? You gave us that study. What do you think you are collecting, on the average, from those people? Mr. Lubick?

Mr. Lubick. We are trying to check that, Mr. Chairman. I think that when you get into the class of taxpayers whose annual income is $200,000 or more, we have a wide variation. As you indicated, some persons are paying very high effective rates because the sources of their income are primarily ordinary income items, dividends, interest, to a lesser extent, salaries and wages.

When you get to others who may have capital gains or tax shelters they get at the very low end of the spectrum. The average effective tax rate is 37.1 percent under present law, but that average is composed of a number of persons at wide extremes, and I think, if I understand you correctly, your objective is to narrow the extremes. Maybe the average is right, but you want to get more people in that category.

I think that is an appropriate objective.

The Chairman. That is the kind of thing I am contending. I am not here to contend that the people in that category are

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1 paying too much. All I am saying is if you are averaging out
2 to 37.1 percent and you have some people who are paying 1 percent,
3 I have asked the Treasury to start pulling those returns of people
4 paying less than 5 percent.
5 When we look at the people paying zero, those are the people
6 who do not owe us anything. You have 22 cases of people who have
7 paid nothing, and you take those 22 tax returns it does not
8 show you where to go in tightening up on the tax law, because
9 those people did not owe us anything, it looks to me.
10 So now we have to ask you to start pulling sample returns
11 on those people who are paying one-tenth of 1 percent, up to 5
12 percent, and let us see what percentage of those people are like
13 that 22 percent who pay nothing because they owe nothing. Let's
14 see what percent of those people are tax shelter cases that we
15 ought to be taxing. We should zero-in on them.
16 Then you are going to have to move over to 5 percent and 10
17 percent to show what it shows there by a sample study.
18 What I think we ought to be trying to do is come down to a
19 minimum tax that zeroes in on them. You have a lot of people
20 who are paying 25 percent and 30 percent who would be paying that
21 minimum tax as it stands now who are not really the people we are
22 after.
23 The new minimum tax, I would think, would not hit them as
24 hard. But, by contrast, you are going to find some people like
25 this man whose name was on the enemies list -- and I must say he

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1 had a right to feel that he had some enemies in government --
2 when he is really paying two-thirds of what he is making in taxes.
3 That fellow is the kind of person that a tax lawyer would call a
4 poor sap. There he is paying all of this money, and if he had
5 talked to that lawyer and let him show him how to do a little
6 tax planning he would not have paid that much.

7 We ought to be thinking how we can make this law so that that
8 poor sap comes down more towards the average --you are talking
9 about a 37.1 average -- while we are going after these people who
10 are really getting the best of it.

11 Mr. Lubick. We agree with that, Mr. Chairman. I might point
12 out, in connection with the poisoning effect on capital gains and
13 the maximum tax, I understand that one of the objectives of impos-
14 ing a 50 percent maximum tax on earned income was to encourage
15 executives and others in that category to be willing to work for
16 cash and to simplify their lives so that they were not diverting
17 all of their activities in seeking out tax shelters and devious
18 ways of minimizing their tax burden.

19 To that extent, when we reduce the availability of the earned
20 income maximum tax by reducing it if a man had a capital gain, we
21 were going to counter to that objective because, in the case of a
22 capital gain in many or most instances, we are dealing with a
23 legitimate investment which he makes and he is paying a regular
24 capital gains tax and, in addition, you are destroying the
25 availability of the earned income maximum.

1 It is quite different from a tax shelter that you were
2 trying to get him out of and over to genuine investment activity.
3 I think that we are in accord with the elimination of the
4 poisoning of the maximum tax that was contained in the House bill.
5 The Chairman. I regret to say that it was not my idea to
6 do it that way, but I regret to say that for people who have
7 other sources of income besides their earned income, the maximum
8 tax is a Catch-22 situation. You say you do not pay but half of
9 it in taxes, but that is before the tax comes into effect.
10 If they do, it does not work out that way at all.
11 It seems to me we ought to try to start moving towards making
12 it mean what it is supposed to mean -- you pay half of it in taxes.
13 Then, when those people take a look and find that those people
14 who have done all the tax planning, the lawyers and the accountants,
15 those people paid 37.1, but here is a tax law that represents
16 the theory, let's do good for the people who go out and earn
17 their money, to pay 50, they pay 70 percent of it.
18 I would hope that you would work with us to move towards
19 uniform justice for taxpayers to say that we are going after these
20 people who have benefited very greatly by tax planning. We ought
21 to do something for this poor fellow that did not do any of it.
22 Nothing moral about it -- he did not do any of it, except earn
23 some money. He did not try to avoid taxes, but as a result, got
24 stuck.
25 We ought to try to offset that. I hope Treasury will help us

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to do that. That is just good tax law.

Mr. Lubick. I think we are generally in accord with respect to the specific proposal that you have referred to. This is a situation which is primarily in the investment and banking field where you have an arbitrary allocation of the amount of income from the business which is, to a great extent, a personal services business, but because capital is the material income producing factor, there is automatically a limit on the amount that can be treated as earned income.

The result has been that most of the investment banking houses have incorporated. They can accomplish the same result by incorporating.

We are generally in agreement that this limitation is a very arbitrary one. We cannot think of any rational justification for it, nor do we think that it is particularly desirable to force all taxpayers into the situation to go into the corporate form of doing business where traditionally they have been in partnerships.

Basically we are in accord with the concept that is involved in this amendment.

The Chairman. I would hope that we can provide some justice and equity into this area that would be much broader than the very limited situation which this amendment would apply to, because while we do justice perhaps by a small number of taxpayers here, I think we should cover a larger group.

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1 I want to ask about another matter of Treasury about these
2 estimates.
3 Senator Byrd. Mr. Chairman, before you leave that subject,
4 could I ask one question?
5 The Chairman. Yes.
6 Senator Byrd. In regard to maximu tax on earned income, is
7 it poisoned by charitable contributions?
8 Mr. Shapiro. Not directly, Senator. To the only extent it
9 is is that the minimum tax is a limitation. One of the preference
10 items of the minimum tax is your itemized deductions in excess of
11 65 percent of your adjusted gross income is a preference item.
12 That was put in in 1976. A percentage of itemized deductions,
13 if you have a large amount, would be treated as a preference item,
14 and that would include everything -- charitable contributions,
15 medical expense, interest, taxes, that part of it would be the
16 poison.
17 Let me back up and explain a little more fully. The day that
18 came in as a part of the Tax Reform Act of 1976 showed that a
19 number of individuals paying no taxes were doing so because they
20 had a very large number of itemized deductions and one of the
21 provisions that was put in in 1976 was the new preference item that
22 said if you had itemized deductions above a certain percentage,
23 65 percent of your adjusted gross income, then that excess would
24 be treated as a preference item.
25 The fact that that excess was a preference item, that excess

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1 also poisons the excess tax. But charitable contributions does
2 not poison directly, only the indirect effect of the part of the
3 excess amount.

4 Senator Byrd. Thank you.

5 The Chairman. Let me just try to illustrate this item that
6 we have had a lot of conversation about about these estimates.

7 When we changed the law on gift taxes, it shocks people that
8 that all happened as a result of the Curtis amendment when Carl
9 Curtis came here trying to look after small businessmen and farmers.
10 By the time they got through with it, we brought some monstrosity
11 in.

12 Senator Curtis. The House did.

13 The Chairman. The House had some idea that they could
14 improve on the Curtis amendment. By the time they did, people
15 paid a shocking increase in taxes, and I tried to explain to them
16 that that all started out with a Republican trying to help the
17 small businesspeople and the farmers in the country.

18 It shocks them, but by changing this gift tax compared to
19 previous law, I am told that Treasury estimates that that provision
20 was going to bring Treasury $400 million and when the returns
21 were in it brought $1.7 billion.

22 Is that correct, Mr. Lubick?

23 Mr. Shapiro. The information we have, Senator, in the periods
24 prior to the effective date of the 1976 Act with regard to estate
25 and gift taxes, gift taxes that were paid were running in the

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1 neighborhood of $400 million. It was anticipated that there
2 would be a slight increase in regards to taxpayer response, maybe
3 $100 million to $200 million.

4 The reason we do not have an exact figure is because there
5 are so many revisions. They are all lumped together.

6 Previously, it was a constant $400 million gift taxes, but
7 on the assumption that was taken into account that there would
8 be an increase of maybe $100 million, $200 million, the actual
9 increase that occurred was $1.7 billion and that is because the
10 effective date, January 1, 1977, at the estate gift tax changes,
11 the unification of the estate gift taxes and the new rates.

12 Previously, the rate for gift taxes were three-quarters of
13 that of the estate taxes, but taxpayers had an opportunity before
14 the effective date to make additional gifts and come under the
15 old law. At that time, that was because there was a dual system.
16 Gift taxes and estate taxes, rather than a unified system.

17 The Chairman. That gets me to the point I had in mind, which
18 I do not think ought to be overlooked in considering this tax bill
19 and that is that the Treasury estimate on that provision that we
20 brought out of that conference was a five to one as a minimum.
21 And I just do not think that we should have to come here with esti-
22 mates that are badly out of line when, by simple anticipation and
23 by estimating that something will have the effect that it will
24 likely have -- you have to guess, and admittedly it is a guess, but
25 we should not be acting on estimates that are off by 100 percent

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1 or 1,000 percent or 5,000 percent. We ought to try to estimate
2 what the taxpayer response to a tax change is going to be.
3 We looked with scorn at these HEW estimates that sometimes
4 they have missed the cost estimate by 100 to 1, but we ought to
5 try to get these estimates to where they anticipate a taxpayer
6 response to a change in the tax law.
7 That is basically what I have been advocating and pressing
8 for when I am asking for Treasury to assume that when we do some-
9 thing calculated to bring a taxpayer response that it will bring
10 one.
11 Mr. Lubick. Mr. Long, I think we agree with you fully on
12 the importance of trying to pick up the kind of effect associated
13 with this gift tax change. As you recall, the '76 Act was signed,
14 I believe, in October of 1976 and the effective date of this
15 particular change was at the beginning of 1977, January 1, 1977.
16 So, essentially, we had a two-month period there where you
17 could still get a free drink at the bar and you were told that
18 the bar was closing. This probably accelerating a significant
19 gift into 1976, many of which would have been made in 1977, 1978
20 or 1979. Also, the kinds of gifts that were accelerated were
21 within a family where the control of the property was staying
22 within the family, and this had a significant effect because tax
23 advisors were clearly advising wealthy clients if you are intend-
24 ing to make a gift next year or the following the year, the tax
25 consequences for making that gift are going to be significantly

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1 higher, and you would be better off making your gift today and
2 paying taxes at the lower rate which are about to disappear.
3 There are significant effects; although I was not at the
4 Treasury at that time, I suspect that the Treasury staff and
5 Joint Committee tax, that the estate gift tax compromise was put
6 together in September, were probably unaware that they were leav-
7 ing open such a major incentive to accelerate gifts.
8 I point out, though, that this is mainly a timing issue
9 between whether taxes are paid one year or the next. If the
10 taxpayer was not planning to make a gift, possibly letting the
11 property pass at the time of death, they would not have accelera-
12 ted the gift. Probably what we got were increased gift tax
13 receipts in 1976 following into fiscal year 1977 and then more
14 receipts the next few years because people had accelerated their
15 gifts into 1976.
16 I think you are right that when we can identify these kinds
17 of timing effects of tax changes we ought to try to estimate how
18 important they are going to be and what the revenue consequences
19 are going to be.
20 I am just citing that as an example. There will be a lot of
21 others where you have an excuse for being in error, if nobody
22 pointed out to you why they thought that that estimate was going
23 to be in error. But where it has been carefully studied by
24 people and pointed out that this is going to be in error for the
25 following reasons, and it has been pointed out that this would be

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in error for this reason, in that event, you ought to look at it and try to take it into account.

I am hoping that we are going to be able to get together on what we are trying to do here, but I am just saying that for better tax laws, we need better estimates and we need to overcome some of the errors of the past, just like we need to do on the spending side of it -- we need some better estimates.

Mr. Sunley. Mr. Chairman, if I may add, usually when we can identify those situations where we think that delaying an effective date is going to have significant revenue consequences, this is brought before the Committee and often the Committee takes action appropriately.

I can recall in the '69 Act when we were going to close down the production payments in the oil and gas industry, first there was some thought to have the effective date at the beginning of 1970. Then the Committee and the staffs realized that the revenue consequences of delaying that effective date would be very significant because people -- this is the last chance to have a production payment. You may have two, three years of production payments that year.

I think these consequences have got to be considered when we are trying to discuss effective date provisions. When they are significant, the revenue estimates have to be adjusted accordingly.

The Chairman. In years gone by, we have let these estimates

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1 oftentimes decide what the decision was going to be. Looking
2 back on it, when we try to say whose estimate was that, they would
3 say well, it is the Treasury's position. And you look at it and
4 you find out that it was not the Secretary of Treasury's judgment,
5 that was not the Undersecretary of Treasury's judgment, that was
6 somebody down in the ranks that made that decision.

7 Just like when we came up sometimes with our estimate, here
8 is what the Committee estimates this is going to be, I could
9 say that was not the Committee's estimate, it was not the Chair-
10 man's estimate, it was not Mr. Shapiro's estimate, it was not
11 Mr. Stern's estimate, that was Mr. Wetzler's estimate.

12 If it is wrong, I want Mr. Wetzler to get the blame for it.
13 However, if it is right, then I think we ought to discuss it.
14 Let Mr. Wetzler explain how he arrived at all of this and who
15 advised him. And I am led to believe that maybe going to talk
16 to somebody at Treasury about the matter -- not the Secretary,
17 but maybe somebody else down there, and we hve to find out how
18 they arrived at this, how they put the pieces in.

19 Then we come back later on and look at something that we
20 did, the horrible example is over in the social welfare area,
21 we brought in these things that cost 100 times the estimate,
22 a hundred times the estimate, and then you say, how did that
23 happen? It happened because nobody saw fit to go take the
24 piece of the pie and see how they were arriving at this and to
25 crank their own common sense into it because the basis upon which

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1 these things are arrived at should be something that a United
2 States Senator ought to be able to understand if his Committee is
3 going to take responsibility for it.

4 It takes someone doing business by the so-called standard
5 method, not understanding what the standard method is. We ought
6 to know it and then lay it out there so that everybody can pass
7 judgment on it.

8 What is the next item you are suggesting we suggest, Mr.
9 Shapiro?

10 Mr. Shapiro. I am not sure where the Committee may want to
11 go at this point. We have covered a good bit of the individual
12 last Friday.

13 One of the problems we have is that until the Treasury gives
14 you the amount that you can spend, it is not going to be clear as
15 to how much money you will have for the total package and be
16 able to allocate into each area. For example, it appears that
17 the Committee would very much like to make every taxpayer, ,at
18 least in each class, whole in the aggregate for the inflation
19 increase of '78 and the Social Security increases that will take
20 effect.

21 In addition to that, there is some discussion about some of
22 the corporate rate changes, additional depreciation that is made
23 available.

24 Until you actually know the amount of money that has been
25 allocated for revenues that has come out of a conference on the

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1 Budget Resolution between the House and the Senate, it would be
2 difficult to make the allocations.
3 The Chairman. Why do we not discuss this adverse limitation
4 that is on page 10 of the suggestions. We have a lot of different
5 suggestions.
6 Mr. Shapiro. In your folder as well is some material the
7 staff pointed out, II. Let me briefly outline it.
8 One of the concerns that came to the attention of the
9 Congress in 1976 was the loans that were made in some of the tax
10 shelter interests. This is where an individual investor who put
11 a sum of money and would have an amount equal to that, or greater
12 than that, allocated to his benefit on a non-recourse loan basis.
13 For example, the particular arrangement, oil and gas, farming,
14 movie deals and so forth, an investor may put up $10,000. That
15 partnership would borrow, in the name of that investor, an
16 additional $10,000 or more on a non-recourse basis, meaning that
17 the investor was not liable for the $10,000 if the venture went
18 bad. There was no recourse for that investor to lose anything
19 more than the $10,000 that the investor put up.
20 However, the way the tax laws worked before 1976, was that
21 the taxpayer could have allocated to his basis not only the $10,000
22 he put up but an additional amount, for example, an additional
23 $20,000 that was borrowed on a non-recourse basis. Therefore, the
24 taxpayer would get the benefit of deduction as much as the entire
25 amount, so that the taxpayer in the first year deducted $20,000

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1 on a $10,000 investment and that taxpayer was in the 50 percent
2 bracket, that taxpayer was gambling with the government's money.
3 He put up $10,000 and got a $20,000 deduction -- $10,000
4 put up, $10,000 borrowed in the 50 percent bracket, that $20,000
5 deduction was worth $10,000 so the taxpayer had recovered the
6 $20,000 that he would have invested and therefore whatever the
7 business venture did after that was gambling at the government's
8 expense.
9 To deal with that particular situation, the Congress passed
10 what is referred to as the at-risk rules that limits the taxpayer's
11 deductions to the amounts that the taxpayer actually has at risk.
12 If a loan has been borrowed on behalf of the taxpayer, the tax-
13 payer cannot have that allocated to his basis unless the taxpayer
14 is liable on that loan, that there is recourse.
15 Therefore, in the example that I used when the taxpayer put
16 up $10,000 and the $10,000 borrowed on his behalf, if the taxpayer
17 did not sign that note and is not liable, the taxpayer can only
18 deduct up to the first $10,000 he put up and these are referred
19 to at the at-risk rules.
20 In the 1976 act, they applied to four areas: farming, oil
21 and gas, air ventures, movie and videotape ventures, and leasing
22 activities. And they only applied to individuals,. they did not
23 apply to regular corporations. However, they did apply to Sub-
24 chapter S corporations.
25 There was also a general provision enacted in 1976 that dealt

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1 with the partnership at-risk rule which applied a general
2 at-risk rule to partnerships in general other than these areas
3 except real estate. That was a provision that was added on the
4 Senate Floor. I think it may have been Senator Haskell's
5 amendment on the Senate Floor and it was agreed to in the confer-
6 ence.

7 In the House bill, the Administration recommended, and the
8 House adopted, an expansion of the at-risk rule which, in the '76
9 Act, applied to the four areas -- to all activities other than
10 real estate, and in doing so, eliminating the general partnership
11 rules. Instead of having two types of rules, the at-risk rules
12 and the general partnership rule, the House bill provided the
13 general at-risk rule across the board to all activities.

14 They made certain other modifications. For example, they
15 provided a separate rule for aggregation. What that means, in the
16 1976 Act, you would take each investment on its own -- for example,
17 each equipment leasing deal was looked at separately and what
18 aggregated is that you take all of the business arrangements
19 together and aggregate them and look at the net rather than one
20 deal at a time.

21 The reason for that is you may have situations where a
22 regular business, if it is operating as a small business, what
23 they would have, some of the arrangements they have gotten to in
24 the past, were not sheltered arrangements, they actually had
25 profits coming out. If you do not allow the profits to offset

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1 some of the accelerated depreciation, it would have the effect
2 for any new deal or adventure or leasing arrangement that the
3 partnership would get into, so there are certain aggregation rules
4 that were provided in the House bill.
5 In addition to that, the rules were extended not only to
6 just partnerships and Subchapter S partnerships, but extended to
7 closely-held corporations. That has caused us certain concern
8 that I will go to in just a minute that goes to the problems listed
9 on page 10 in the staff document you received this morning.
10 Also, there was a rule in the House bill that recaptures
11 losses where the taxpayer is no longer at risk. This is a situa-
12 tion, for example, where the taxpayer may put up $10,000 in a year
13 and then have that $10,000 deducted because he had certain deduc-
14 tions for that investment, so the taxpayer no longer has anything
15 at risk.
16 After having the benefit of that $10,000 investment the next
17 year, the taxpayer pulls out $10,000 of the money that he would
18 have otherwise had at risk. What the House bill does is recap-
19 ture a tax benefit that the taxpayer had gained in that previous
20 year because the taxpayer had subsequently taken out the money he
21 had at risk.
22 These changes in the House bill did not have a significant
23 revenue effect. They increased liabilities to approximately $14
24 million in the calendar year, $2 million in the fiscal year-- not
25 significant tax reform itmes in the House bill. They were viewed

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1 as structural changes.

2 The effective date for all these changes were after this

3 year. They all go into effect next year.

4 The problems that have come up with this that are listed in

5 some of the alternative proposals the staff has, the proposals

6 are on page 10 of this material. One of them is in the case of

7 closely-held businesses -- this is the one that has come to the

8 staff's attention to a great extent, especially for equipment

9 leasing in small businesses, you have some legitimate small

10 businesses -- not tax shelter corporations -- that compete in the

11 leasing business against IBM, Xerox and some of the larger leas-

12 ing businesses.

13 The fact that they are small businesses, meaning closely-

14 held by two or three individuals, the extension of the at risk

15 rules were applied to them under the House bill. They indicated

16 for the most part they are legitimate small businesses and it

17 was not their intention to deal with non-tax shelters. It was

18 the intention of the House bill to cover cases where they were

19 able to avoid the Tax Reform Act of 1976 and therefore some of the

20 proposals that were made were to provide rules to deal with that

21 situation.

22 The problem about exempting certain types of small businesses,

23 you do not necessarily know a legitimate business that operates

24 in equipment leasing as a legitimate business venture and those

25 who are really tax shelters. You have to look at each one case

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1 by case. It is very difficult to enact any kind of rules that
2 does that.
3 There are a couple of rules that are suggested that deal with
4 that situation. For example one of the rules, instead of just
5 looking at a business at what they do after 1978, so that in all
6 the new tax sections you take up all the business arrangements in
7 the past, the advantage of that is to allow the businesses to
8 net their profitable situations from the past.
9 What I mean by that is this. Prior to 1978, you had, let
10 us assume, a leasing smaller business enterprise, that, for the
11 first time would be picked up by the at-risk rules, but in the
12 past, they, in operating each new lease, has excess production.
13 That would be picked up.
14 But you take some of the leases they have had for years,
15 they have a lot of profit under that, where you net the two out
16 and on the overall, they would not be picked up. But if you
17 just applied the rule to new leases after 1978, what you are
18 doing, you are saying each new lease would not be allowed to have
19 their accelerated deductions allowed.
20 However, if you went back and picked up prior leases and
21 looked at their total business, they could be covered. And
22 therefore, one suggestion is to cover that, to cover all the
23 transactions and not just look at the new leases. In addition,
24 that would have the effect of aggregating their entire business.
25 Most of the small businesses that have had discussion with

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us believes that that type of proposal would be appropriate. Although they believe they should not be covered on the provision they are not a tax shelter operation, the general feeling is with that type of change, to a large extent, they would not be adversely affected.

Senator Bentsen. That would still get at the tax shelter and not get at business that was legitimately in it for quite a period of time?

Mr. Shapiro. That would be the result, not to have an adverse effect on legitimate businesses. Let me go into an additional case that has come to our attention and represents another problem -- the noncorporate case.

The Chairman. What?

Mr. Shapiro. Non-corporate case, an individual.

The corporation, for the first time, has been covered under the House bill but there is also the case of individuals who are indicating they are operating an equipment leasing business. They are not in corporate form, but they are coverered under the Tax Reform Act of 1976 and they believe they are operating legitimate small businesses or legitimate business and equipment leasing, not primarily intended for sheltering, and the rules should not be aimed at them, but should be aimed at your high-income investors who are in professions or who earned income for other businesses and go into these shelter arrangements.

The proble about dealing with that, you do not know how to

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1 distinguish an individual who is in a profession making $100,000-
2 plus a year and getting into an investment in equipment leasing
3 or someone who is in that business. It is very difficult to make
4 a distinction.
5 We have been discussing it with some of the individuals.
6 We feel that to the extent it is a legitimate equipment leasing
7 business and not a tax shelter that Congress did not intend to
8 deal with that particular type of situation. That is not an easy
9 one to get at.
10 Senator Gravel. Could you not set a criteria that if they
11 were involved in the active management of that business they
12 obviously would not be doing this, it is this shelter process?
13 Could you not set that type of criteria?
14 Mr. Shapiro. You can, Senator, but you can take an individual
15 who is in a profession making $100,000 a year making an investment
16 of $10,000 in business and could be involved in certain manage-
17 ment decisions that would qualify him for being in management.
18 It is difficult to draw the line.
19 The suggestion you made is well-intentioned, meaning that
20 someone who is in the active management is not in a tax shelter,
21 yet it is tough to distinguish someone who decides he wants to get
22 into active management.
23 Senator Gravel. We certainly would not want to set up a
24 monopolistic type situation where those that are in the business
25 because they are small get some succor and those individuals who

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1 want to get into the business would not get the same succor as
2 those who are in the business, albeit they are both small.
3 Mr. Shapiro. That is clearly the case. That is understood.
4 That is what I am saying. It makes it so difficult to try to rule
5 in some situations. It is clearly not a tax shelter and you do
6 not want to aim it at that individual.
7 The Chairman. Let me just point out how I think that this
8 thing is going to be changed, or how I would urge that we would
9 consider changing it.
10 It seems to me that we know a lot more about how a minimum
11 tax should be drawn now than we did when we were working at it
12 under the previous law. We have some studies that can be thoroughly
13 analyzed to see how it should work, and we also know better how
14 to keep score than we did back at that time, just by what we have
15 to look at.
16 You can look at each tax return -- and I am asking Treasury
17 to bring us some of these horrible examples of people who ought
18 to be paying more taxes to help us to have guidance in passing a
19 better minimum tax law.
20 I think that most people would agree -- I know that most
21 businesspeople feel that a minimum tax ought to be an alternative
22 tax. If someone makes a very substantial amount of money, if he
23 is paying very little, then we ought to look at his situation and
24 see if he ought not to pay more on a somewhat different basis.
25 If you are working on an alternative tax which is not an add-on

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1 tax such as we have on, but an alternative, then you would be
2 justified in having a much higher rate. It would be a rate that
3 most people would not pay at all. A lot of people who would be
4 paying it would not be paying any minimum tax, if that were the
5 case, but those who would pay it could expect to pay more. Those
6 who are paying 1, 2, 3 up to 10 percent of their income in taxes
7 and making $200,000 of economic income should expect to pay a
8 great deal more.

9 If that minimum is assessed against the preference items
10 so that assuming an equipment leasing firm is paying very little
11 in taxes, then perhaps only paying 5 percent of their real
12 economic income in taxes, then we change that over to where we
13 have a taxpayer paying 30 to 35 percent in taxes assessed on those
14 preference items, they would be paying just a good deal more in
15 taxes than they are paying now.

16 You are trying to help me work up an alternative suggestion
17 along this line, Mr. Shapiro, and it would seem to me -- I assume
18 you have told Treasury the kind of thing you are looking at, or
19 have you?

20 Mr. Shapiro. Yes. We have discussed with Treasury the types
21 of alternatives that we are looking at -- a pure alternative tax
22 that would eliminate the present law's add-on tax. Essentially what
23 it would do is start from taxable income. You add back the
24 preferences to the taxable income and after an exemption that you
25 would apply rates that would go up to 30 percent and you compare

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the alternative taxes against the regular taxes and pay whatever is greater, the pure alternative tax.

The Chairman. That tax, assuming you did not do anything about the limitation, would not that tax make these people pay a great deal more money, assuming that they are not paying that much now?

Mr. Shapiro. This tax would only apply to individuals. It would, in many cases -- but the real question that applies is with regard to these non-recourse loans. That is not that the income that they might get, but where they go to the bank and borrow money and are not liable on that loan, to the extent that they should get credit and the liabilities that would have to be paid, even if it went bad.

On the non-recourse loans, your point is well-taken. In regard to every preference item in the tax the at-risk is not a preference item. It limits the amount of deductions you get on the investment you are not liable on.

Mr. Lubick. Mr. Chairman, one thing I would like to say in this whole area, I think generally we are in accord with the approach you are suggesting, that we are working ourselves with the same objective.

It should be made clear that even if we come up with a very small minimum tax, there still remains the problem with respect to taxpayers who get very large deductions that are not preference items through depreciation. One can have straight-line depreciation,

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1 either through the use in real estate of component depreciation
2 or through non-recourse financing, that the at-risk is apt to
3 build a very large base towards depreciation without having very
4 much investment there through the use of leverage transactions.
5 You are still going to have problems with taxpayers who are
6 able to shelter most of their income from taxes through straight-
7 line depreciation, and I think that the risk area is attempting,
8 in some measure, to deal with part of that problem.
9 The Chairman. I must say we are making some headway if we
10 get to the point where we look on straight-line depreciation as
11 a tax gimmick.
12 Senator Haskell. Mr. Chairman, I would like to ask Mr.
13 Shapiro -- at risk? If I have a $10,000 investment and a $100,000
14 asset and I borrowed $90,000 but am not obligated to pay it back
15 to the bank, what we have done is limit my depreciation base to
16 $10,000. Am I not correct?
17 Mr. Shapiro. If you were in a real estate transaction, it
18 would not apply.
19 Senator Haskell. Real estate is a bad example, because that
20 is an exemption from the at-risk, but the purpose of the at-risk
21 rule is to limit my deductions, be they depreciation or otherwise,
22 to my financial exposure. Am I not correct?
23 Mr. Shapiro. That is correct.
24 Senator Haskell. I would think that would be desirable,
25 whether it was done with malice aforethought or otherwise. I

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1 would love to be able, of course, to do such a thing, but it
2 does not seem to me to be economically sound. I think that was
3 the purpose of the at-risk rule.
4 Mr. Shapiro. That is correct.
5 Senator Packwood. May I ask a further question, then?
6 The reason real estate was exempted, was it not, Bob, the
7 creditor had another asset to go against other than the individual
8 and that was the real estate.
9 Mr. Shapiro. It is the question as to that. There were a
10 number of reasons why real estate was excluded. It was a
11 traditional way of financing real estate, and not one put together
12 in recent years as a tax shelter.
13 In addition, you had problems in the housing industry at
14 the time, and were concerned about making changes that would
15 adversely affect the real estate industry, that would possibly
16 present economic problems. There were a whole series of reasons
17 surrounding the real estate industry in that regard.
18 I am not sure if it is adequate, if there was one reason,
19 but there were a series of reasons of why it was exempt.
20 Senator Packwood. What would be the harm in limiting the
21 adverse limitation, however, to those things where there is no
22 significant asset for the creditor to have a lien against? I
23 see no home in having a deduction larger than at-risk if, indeed,
24 the creditor has an asset that he can levy against. if it is
25 some form of personal property.

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1 Mr. Shapiro. When that was discussed, brought into
2 consideration in the tax bill, the question that was raised at
3 that time was if the asset is adequate, should not the taxpayer
4 be willing to go at-risk because he is covered by the asset, and
5 that is the way it was responded to.
6 There was concern that the tax shelter arrangements, the
7 way they were being offered, was you just put up a certain amount
8 of money. You did not risk anything else. Your asset covers
9 your loan and you get this big write-off and these tax shelter
10 arrangements were publicized in every newspaper, magazine and
11 so forth and brought a great deal of concern.
12 Senator Packwood. If you have an asset that is worth the
13 cost of a loan and the bank has a lien on that asset, you risk
14 the loss of that asset.
15 Mr. Shapiro. If that were the case, the taxpayer should be
16 willing to go on. All the taxpayer has to do is sign the note,
17 and he has all the deductions. If the note is taken out on the
18 taxpayer's behalf and he signs it --
19 Senator Packwood. If it is with recourse --
20 Mr. Shapiro. With recourse, because all the deductions --
21 if the taxpayer thinks that that asset is adequate security, then
22 the taxpayer would be willing to sign a note and avoid the at-
23 risk rule.
24 Senator Dole. As I understand it, the at-risk rules were
25 designed to take care of individuals and partnerships. Now they

1 to bring in closely-held corporations, five or more shareholders,
2 is that correct?

3 Mr. Shapiro. Five or less.

4 Senator Dole. Excuse me. Five or less.

5 That is Section H202 in the House bill. We are talking about
6 $14 million.

7 Will this same thing apply to large corporations? Why do
8 we single out the closely-held corporations when we are talking
9 about the need for capital formations? It seems to me that the
10 best thing to do would be to strike H. 202 and adopt the rules
11 you mentioned earlier.

12 Mr. Lubick. It was basically found that there was a
13 significant employment of the small closely-held corporation to
14 engage in tax shelter activity towards some of these uneconomic
15 and unrealistic evaluations.

16 Senator Dole. Are there actual cases of that?

17 Mr. Lubick. Yes, Senator Dole.

18 I think, in our basic presentation, we gave some illustra-
19 tions in the green book which we will be glad to furnish to you.

20 Senator Gravel. In point of fact, will we not pick up those
21 people that you are talking about through the suggestion of the
22 Chairman that we do away -- if we do that, if we pick them up
23 straight away, there is no reason for us to discriminate against
24 the people who have an operating business either because they
25 are a small corporation, or closely-held, or individuals.

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The large companies, like Xerox et al., they are not at-risk. We are winding up with a theory of at-risk here.

Mr. Lubick. I think we can take care of these situations through the extensions that Bob talked about and the extension of the aggregation laws, both old and new releases that give them an investment base. We have not seen any illustration that once that aggregation rule is extended that anybody who is in an active business who is being hurt -- there may be some, but they have not been brought to our attention.

One can concoct a case theoretically, but as a practical matter, all of the ones we have seen seem to be taken care of.

Senator Curtis. How much is the Treasury gaining out of this at-risk?

Mr. Lubick. The changes, I believe Bobby indicated, were relatively inconsequential in revenue, about $14 million. It is not a large revenue increase.

Senator Curtis. Under existing law, how much are you gaining by all of this web and entanglement of at-risk?

Mr. Lubick. I think the problem involves more than the direct revenue that was collected as a result of the provisions. I think that they have a prophylactic effect.

It is the loss of revenue that you avoid through deterring and discouraging these kinds of transactions that are artificial and non-economic that is important.

I think that we wouldhope, as we do with the personal holding

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1 provisions, we would hope that the direct revenue pick-up would
2 be zero, because that would mean the provisions would have been
3 effective inprevengint the avoidance techniques that they are
4 seeking to prevent.
5 Senator Curtis. Suppose that there is a small business, a
6 truck line, several trucks. His indebtedness is $190,000. He
7 says to his seller, I will convey this to you for $10,000 subject
8 to the indebtedness. Not an agreement that he assumes or agrees
9 to pay, just sells his personal property in good will subject to
10 the indebtedness.
11 The man buys it. He throws all of his mind, heart and energy
12 into it. He has the hopes that he can make it succeed and that
13 it will have a capital growth and that he will have a valuable
14 asset there. He pays the interest regularly on the $190,000.
15 But under existing law, he would get no deduction for that,
16 would he?
17 Mr. Lubick. For the interest, or for the depreciation?
18 Senator Curtis. The interest.
19 Mr. Lubick. I think the interest is not a question of at-
20 risk at all. I do not see any problem.
21 Senator Curtis. It is confined to depreciation.
22 Mr. Lubick. The problem is basically depreciation.
23 Senator Curtis. I will reword my question; I was in error.
24 He pays $10,000 and assumes this small business subject to
25 its indebtedness, which is $190,000. He has the hopes that by

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giving his best effort, and so on, that it will become a valuabl[illegible] asset.

In what way does the present law deny him the depreciation?

Mr. Lubick. I do not think the present law affects him. I assume it is not within one of the four categories that the present law covers, not in movies, agriculture or equipment leasing or oil.

Senator Gravel. If he leased these trucks he would be the lessor. He acquired the trucks, had the indebtenedss, put up $10,000. Now he is leasing the trucks out to operators.

Mr. Lubick. An equipment-leasing business you are talking about?

Senator Curtis. I am just trying to illustrate the difficulty and inequity to apply this rule. I am wondering how much the Treasury is gaining.

Mr. Lubick. Basically, Senator Curtis, I would like to point out, first of all, if real estate is involved in the business, the depreciation with respect to the real estate portion is exempt.

Senator Curtis. You do not depreciate real estate, do you?

Mr. Lubick. The improvements on real estate are depreciable.

Second, it is important to recognize that as he amortizes his investment, he pays off the principle out of his profits. He is securing additional basis for depreciation.

So really, the at-risk situation only applies in a situation

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1 where you have a very large, inflated price that was not a
2 realistic price with no real investment being made by the
3 purchaser. If he does not have any equity in there at all, in
4 effect what he is doing is depreciating and getting deductions
5 against his other income for money that he does not have invested.
6 To the extent that he amortizes the principle, even if he is on
7 a non-recourse basis and makes payments to the sellers, he is
8 adding to the basis and you are not limited to your original
9 down payment by the way of depreciation.

10 Each time he pays the principle off, he is getting additional
11 basis. If, indeed, he is not paying any principle at all, it
12 looks to me as though the transaction is not really a bona fide
13 sale. It is some sort of profit-sharing arrangement between the
14 seller and the buyer.

15 I think that one can derive hypothetical cases where it
16 would cut in, but I do not think that you see those cases as a
17 practical matter.

18 In the rare case where an operating business is sold on a
19 non-recourse basis, it is very rare to find the at-risk rule
20 cutting in.

21 Indeed, if I were in the position of the purchaser that
22 you described and I was concerned only with respect to the prifit-
23 ability of that business, I think I can avoid the at-risk rule
24 completely simply by forming a corporation with no other assets
25 other than those that it is acquiring and the corporation could

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1 sign the note for the purchase price of the business and it would
2 be at-risk and there would be no limits on that corporation's
3 depreciation.

4 Senator Curtis. That leads me back to my question on how
5 much money do you get out of all of this? Is it worthwhile?

6 Mr. Lubick. My answer to your first question is that we do
7 not get a lot out of it. My answer to your second question is
8 that it is worthwhile because we are preventing serious losses
9 in revenue through non-economic transactions. We are sort of
10 staunching the flow of blood.

11 Senator Curtis. You are forcing them to form a corporation.

12 Mr. Lubick. That corporation cannot shelter those losses
13 as against other unrelated income.

14 The Chairman. Senator Dole?

15 Senator Dole. If you just added one more, if you add six
16 people this would not apply, would it?

17 Mr. Lubick. That is not true, Senator Dole. Five or fewer
18 owning 50 percent or more. You have to get up to 11 or more,
19 I think, to avoid it.

20 Senator Dole. Why is there more likely to be abuse in a
21 closely-held corporation than in some giant corporation where you
22 have a concentration of ownership you are suggesting there
23 could be abuse where in diffuse ownership we do not have the
24 problem?

25 Mr. Lubick. I think that it is generally true that if you

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1 have large, widely-held corporations that you do not have people
2 are manipulating the provisions of the Tax Code to do a non-
3 economic transaction. You cannot get 2,000 people together and
4 operate --
5 Senator Dole. You do not need 2,000. They are still invest-
6 ing to reduce their tax liability and I just think maybe we
7 could strike H202 and I will make that motion at the appropriate
8 time.
9 Mr. Lubick. I thought your suggestion was maybe the rule
10 ought to go from 11 to some higher number?
11 Senator Dole. I think we are looking at that. This is
12 precedent for that. Next time we will be including all corpora-
13 tions. Maybe we should, I do not know. I do not know why we
14 single out closely-held corporations for special treatment, or
15 maltreatment.
16 Senator Haskell. Mr. Chairman, I wonder if I could, to the
17 extent I can, speak to this. I would wonder why we would want
18 anybody to depreciate on a sum of money that they have not got
19 invested?
20 I wonder if the simple and proper economic thing to do is
21 to allow depreciation to the extent that you are at-risk?
22 Mr. Lubick. I think that one could make a very good case
23 for that. I think historically, as Bobby indicated, in real
24 estate non-recourse financing has been a conventional activity.
25 Very frequently, the seller would agree to look only at the real

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1 property as his security and it has this historical background
2 and I assume that you are reluctant to disturb it, because there
3 are very many legitimate deals that operate this way and rather
4 than go to the logical conclusion -- and I think there is a lot
5 of logic in your conclusion -- I think that you wanted to cover
6 those cases where this principle that frequently was used in
7 legitimate economic ways has been transferred to be used in ways
8 that seemed to produce only tax deductions and not economic
9 benefit.

10 Senator Haskell. I think the reason for the exclusion of
11 real estate was a very distinguished gentleman, long connected
12 with housing, suggested that real estate be excluded and I think
13 it was so adopted on the Floor. I just was curious. I just
14 personally do not have the experience, perhaps, on what is
15 generally done in real estate, but the only time that I could see
16 that you would not ask the person to become liable on a note
17 would be if the real estate had immensely appreciated in value
18 over a period of years and therefore you felt reasonably safe.

19 That would be the only way that I could see that anyone
20 would do it.

21 Mr. Lubick. Usually, you loan up to only a certain percen-
22 tage -- 50 percent or two-thirds of the value of the real estate
23 and therefore you regard the real estate as having ample margin
24 for security. In addition, when you get into the law, foreclosure
25 is very difficult in many states to take a judgment. Many do not

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1 even bother to do that. When they look at this type of lending
2 they say all we are looking at is the security.
3 The Chairman. Senator Byrd, then Senator Gravel.
4 Senator Byrd. I want to follow up on Senator Packwood's
5 question to Mr. Shapiro. I am not clear as to your reply. Take
6 this example: if an individual puts up an item valued at $100,000
7 and borrows, say, $80,000 on it, what is his situation under the
8 at-risk?
9 Mr. Shapiro. When you say "put up," do you mean collateral?
10 He has it covered if he puts anything up.
11 That is the same thing as being liable. A txpayer would
12 get the full benefit, under present law, on anything that he has
13 personal liability on, signing a note or putting up collateral.
14 The only limitation that the '76 Act went to, was when the tax-
15 payer gets something that was to his benefit -- for example, a
16 non-recourse loan which said that if $10,000 were borrowed in his
17 name if the business went bad he would never have to pay it.
18 So the question the Congress raised in '76 was should a
19 taxpayer be allowed to get a deduction on $10,000 borrowed in
20 his name if he never has to repay it if it went bad, but he is
21 not liable on it. Should he get the benefit of it?
22 If a taxpayer wanted the benefit of it, the '76 Act said
23 the taxpayer should sign for the note or put in collateral. The
24 taxpayer has to put up collateral and has something to lose, cash
25 or property and then the law would apply completely.

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1 Senator Byrd. If collateral is involved, it is a recourse
2 loan.
3 Mr. Shapiro. That is correct.
4 Senator Packwood. I misunderstood the way you answered my
5 question. I do not understand. What was the difference in the
6 situation I posed to you from what you just answered to Harry?
7 Mr. Shapiro. We are talking about two different situations.
8 I am asking what you are saying. I was talking about where you
9 put up collateral that is unrelated to the asset that is being
10 purchased. Let's assume that you are buying an airplane and you
11 are putting up a piece of property that you have that is worth
12 $100,000 plus a $10,000 investment and they give you a $100,000
13 note.
14 You would get a $110,000 deduction, the $10,000 you put up
15 in cash plus the $110,000 that is being borrowed, because you
16 put up $100,000 worth of property against that note. You would
17 get $110,000 depreciation because you are liable, not only for
18 the $10,000 but for the $100,000 piece of property.
19 Senator Packwood. You are not liable. They can seize it.
20 As I posed my question, you borrow $100,000, you sign a note
21 for $10,000, you put up a piece of property that they have a lien
22 on or a mortgage or whatever you want to call it. If you do not
23 pay off the $100,000 they take your property, and you say, well,
24 the property is worth $100,000, the taxpayer should be willing to
25 sign a note for $100,000.

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1 Mr. Shapiro. Let me get the situation. I thought you had
2 reference to that you put up against the asset itself, the
3 airplane.
4 Senator Packwood. What difference does it make? You buy
5 an airplane for $100,000. The bank is financing it. They take
6 a mortgage against the airplane, a personal property mortgage
7 against the airplane. It is worth $100,000. Nobody is arguing
8 the value of it, and you have $10,000 at-risk.
9 All you have done is mortgage the airplane rather than some
10 other personal asset you might have had that would have been
11 collateral.
12 Mr. Shapiro. Your point is a good one, Senator. It was
13 one that was discussed quite frequently during the Tax Reform Act
14 and what is behind that, if the airplane is sufficient collateral
15 for the loan -- I am reversing it. It is the only way I can do
16 it, because that is the way it was discussed and the way the
17 Congress came out on the matter.
18 If the aqrplane was worth $100,000 and the taxpayer was
19 clearly protected, why should not the taxpayer sign the loan?
20 Senator Packwood. How about the asset that is unrelated
21 to the business transaction?
22 Mr. Shapiro. The taxpayer can actually lose that. That can
23 come out of his personal estate. The taxpayer has a piece of
24 property in his personal estate. If that is gone, he has some-
25 thing he really can put on his financial statement that he has.

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If you are talking about an airplane that is not paid for, that is being paid for out of profits, the taxpayer cannot put that on his financial statement as something that is in his equity. He is not losing his own equity at that point.

Senator Gravel. One point that Mr. Lubick made on aggregate, the same point I made with Bobby earlier, and I will make it again and that is fine if you have an operating business. Tomorrow, if you and I want to go into the equipment leasing business in a legitimate fashion, we are a small operator, we cannot do it because we are disadvantaged, not only by the large corporations, but those presently in the business. I do not think it is a healty situation.

We are back -- the proposal made by Senator Long does pick up, does close this loophole another way, but does close this loophole.

Senator Haskell. I think it is a different loophole.

Senator Gravel. No. If he picks up, if these people have to pay taxes, they pay taxes. The fact you may consider that a loophole, you have not closed it, but they are paying taxes and it is no longer a loophole. It is a legitimate operating business.

If you insiste on closing the loopholes this way, you disenfranchise people in a competitive fashion, and these are small businesses. You cannot touch Xerox. You are not touching IBM. The two or three people that want to make a living at this,

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1 they cannot compete with the corporations and under your solution
2 you will save these little guys that are in business but will not
3 let anybody else get in the business.
4 Mr. Lubick. They can always get in, Senator Gravel, by going
5 at-risk for a part -- they do not have to go at-risk for the whole
6 amount.
7 Senator Gravel. That is not competitive where the other
8 guy is not at risk and you are at risk, that is not competitive.
9 Not only is it hard to break into business, but you are going
10 to make it twice as hard because he is going to have different
11 ground rules than the guy who is already in business.
12 The Chairman. Gentlemen, could I ask to move us away from
13 this, because there have been some good points made, and I think
14 maybe we could benefit from all of this in trying to put
15 something together that reflects the consensus of what has been
16 expressed here.
17 I would just like to see if I could get some of the Commit-
18 tee's sentiment on this item that starts on page 11, that is
19 these varying tax rates with regard to small business.
20 The witness for The Business Roundtable who speaks for most
21 of the larger companies and chief executive officers indicate
22 that they worry about the graduated corporate income tax, that
23 when they see these rates coming in here at 17 percent, then up
24 to 20 percent, then up to 30 percent and up to 40 percent, they
25 advocate, as I recall it, about a 20 percent tax rate on the

1 $75,000 as an alternative.

2 Mr. Shapiro. Number 41, Senators. That is a 17 percent

3 rate on the first $75,000 of income; a 45 percent rate on every-

4 thing above $75,000 and then going down to 42 percent by 1982.

5 The Chairman. We do not know just how the decision is going

6 to go in the Committee as to whether we are going to go to take

7 the rate on down to 44 percent.

8 I know there are some who have indicated to me that they

9 would like to see us go down to 44 percent, eventually down to

10 42 percent with a top rate on corporations.

11 There is a lot of support for that, but we are going to have

12 to choose. Are we going to go in that area? Are we going to go

13 for accelerated depreciation? Are we going to go for the rate

14 cut?

15 I am not trying to decide that right now. We will have a

16 chance to decide as we go along as to which approach we are going

17 to make, whether we do or do not, when we move over here to this

18 suggestion 42, that raises a point as to what should we do about

19 small business.

20 Are we going to have four tax rates for small business

21 concerns, or are we going to have one tax rate? I am willing to

22 go whatever way the Committee wishes to go. I would like to have

23 some indication from the Committee about having 17, 20 and 30.

24 Will we do better to say we will have one tax rate for small

25 business or we want three tax rates for small business?

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Senator Gravel. 20 percent makes sense.

The Chairman. From my point of view, I rather like the suggestion that you just have one tax rate for small business up to whatever given figure you want. I can go either way, if the Committee wants to do it.

I found a lot of appeal, if you are a small business, take 20 percent, take your average rate, and go with it.

How does Treasury feel about it? Do you want a graduated rate, three different rates, or one?

Mr. Lubick. I think that the choices that have been presented -- one was the 17 percent on $75,000; the other was the House bill -- that we prefer to go with the House bill. We feel there are fewer opportunities to use the corporation as a tax shelter, because you get up to rates of 30 to 40 percent that are closer to the surtax rate.

I think our inclination was to go that route, although we recognize that there was a simplification benefit to the single rate.

Senator Dole. 41 there?

The Chairman. As I understand it, the Treasury would prefer, rather than having 17 percent up to $75,000, the present rate is 20 percent, is it not?

Mr. Shapiro. 20 percent of the first $25,000 of income; 22 percent on the income between $25,000 and $50,000; and then 48 percent on all income above $50,000.

The Chairman. The lowest tax rate you have for small businesses now is 20 percent?

Mr. Shapiro. 20 percent.

The Chairman. I find some appeal to the idea of saying take the 20 percent rate, but apply it to more income. 20 percent up to $75,000, $70,000, somewhere around there. You would do about the same thing for those up to about $100,000 of income. You would do the same thing for them that you would do otherwise. You would not have this 40 percent rate between $100,000 and $200,000.

Senator Curtis. Under that proposal, would the corporations making $49,000 now get any tax reduction?

Mr. Lubkck. Yes, Senator Curtis. At the 22 percent rate today between $25,000 and $50,000.

Senator Dole. What if we made it 17 percent on the first $75,000 and anything over that 45 percent in '79; 44, 43 and 42?

Mr. Shapiro. That is suggestion 41.

The Chairman. 17 percent on the first $75,000?

Senator Dole. $0 to $75,000, and over $75,000 you would reduce it 1 percent in '79 to 45 percent. It is number 41 there. It is on the page right in front of you.

Mr. Lubick. That has a revenue effect of $2.2 billion primarily because -- over the House bill -- primarily because of going from 46 percent to 45 percent.

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1 As I recall, the 17 percent on the first $75,000 and the
2 46 percent rate, which was the top rate under the House bill,
3 cost about one-half a billion dollars over the House graduated
4 method.

5 The Chairman. What do you think, Mr. Lubick?

6 Whatever rate we decide to go with for the top bracket
7 with the 17 percent -- how would the cost of that compare with
8 what is in the House bill?

9 Mr. Lubick. The 17 percent would cost about a half a
10 billion dollars more than the 17-20-30-40, four steps to $100,000.

11 The Chairman. If you took the 17 percent, then cut it off
12 at $75,000 --

13 Mr. Lubick. $75,000 was what we were comparing. It would
14 have to be something lower than $75,000. If you said 17 percent
15 of $68,000, maybe you would come out -- I am just pulling that
16 number out of the air; some number between $50,000 and $75,000 --
17 you would come out with the equivalent of the four steps through
18 $100,000.

19 The Chairman. You say it would cost about $500 million to
20 take the 17 percent up to $75,000?

21 Mr. Lubick. Over the House bill.

22 The Chairman. Over the House bill.

23 Mr. Lubick. Four steps over $100,000.

24 Senator Bentsen. The House was 17 at $25,000 and 25 at
25 $50,000; 30, $50,000 to $75,000; and 40, $75,000 to $100,000?

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1 Mr. Lubick. That is correct.

2 Senator Bentsen. Let me say, Mr. Chairman, as I think I
3 have said to you before, that I am going to urge that we modify
4 some of the corporate reductions and instead of going that far
5 on corporate reductions that we look at increasing the deprecia-
6 tion system in order to try and see if we cannot get more spending
7 back into the improvement of the manufacturing capacity of this
8 country along the lines that Bill Miller was talking about when
9 he testified.

10 Senator Gravel. I would add to that that I agree with that
11 concept very strongly, that I think there might be some merit in
12 trading off the revenue loss against the investment tax credit.

13 The investment tax credit is skewed to one sector of the
14 economy. A corporate reduction does away with that skewedness.

15 I happen to believe that a simple investment tax credit is
16 sort of a given. It has an effect to propel the economy
17 initially, but after these corporate decisions are made anyway.

18 So if we could be more aggressive in lowering the corporate
19 rate, and also accelerated depreciation which I think targets
20 a good portion of the money and then just offset it against a
21 lowering where there is a move to guarantee the investment tax
22 credit permanently, I would say have a lower rate.

23 The Chairman. Let me just tell you what one person says who
24 is highly regarded by the business and financial world, what he
25 told me after he heard that. We were considering going for

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1 a more generous depreciation allowance rather than buying the
2 Administration reduction for further rates.
3 He said, Senator, you are getting this country to become
4 more and more a service-oriented economy and you have more and
5 more companies in the service end rather than in the manufacturing
6 end.
7 I have difficulty deciding among businessmen which guys are
8 the good guys and which fellows are the bad guys. He said some
9 of these people in the service industries seem to be nice people
10 themselves.
11 He says, since I have difficulty in deciding that one group
12 is the fellows with the white hats and the others are the fellows
13 with the black hats, my inclination is, if you are going to give
14 them a tax credit, you should spread it among them, than trying
15 to decide these fellows are good guys and those fellows are bad
16 guys.
17 Senator Bentsen. The only trouble with that, Mr. Chairman,
18 and I understand that, what we are deeply concerned about is the
19 loss in productivity in this country and our balance of trade and
20 the modernization of the manufacturing capacity of other coun-
21 tries is far beyond what we have been able to do.
22 So I would differ with my friend from Alaska on the invest-
23 ment tax credit, but I would also push very strongly for accelera-
24 ted depreciation in order to get that carried out to get these
25 people to make those investments in the modern machinery that

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will help increase productivity in this country, and also to help on the add-ons that we have had because of environmental protection and to make jobs safe. That would, in turn, help.

The Chairman. Incidentally -- Senators, if you have no objection to this appearing in the record, this is a thoughtful letter from Arthur Andersen company having to do with the at-risk rules. I think it should be put in the record and made a part of it.

(The material referred to follows:)

COMMITTEE INSERT

1 The Chairman. Senator Danforth?

2 Senator Danforth. On this point, I have been making this

3 point about productivity and capital formation since the hearings

4 began and I do not have any particular axe to grind for one

5 approach or another.

6 As a matter of fact, last March Senator Javits and I put

7 in some bills on this subject and we covered everything. We

8 covered expanding the asset depreciation range which Senator

9 Bentsen thinks is important. We covered increasing the invest-

10 ment tax credit to 12 percent. We covered reducing the corporate

11 rate.

12 So I entered this whole thing with a comletely open mind and

13 began asking questions of as many people as I could find and

14 while Mr. Miller did a very good job of making the case for

15 depreciation when he appeared before us last week, he really is

16 in a minority.

17 The same day that Chairman Miller appeared before the

18 Finance Committee, a group of about nine or ten economists,

19 business-type people, met with some Republican Senators, part

20 of our Republican Policy Committee.

21 I put the question to them, and they, including Arthur

22 Burns and Alan Greenspan and Reg Jones from General Electric,

23 Bruce McClory from Brookings and so on, and Arthur Andersen,

24 and said if you had X number of dollars to work with and you have

25 to choose between putting it into rate reductions or putting it

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1 into accelerated depreciation or putting it in the investment
2 tax credit?
3 And every single one of them said they would rather have
4 that in rate reductions.
5 Senator Bentsen. I understand that very well. It gives
6 them much more freedom. They can decide what to do. They can
7 decide whether they are gong to pay off some of their debts, make
8 an acquisition of another company, or whether they want to
9 increase their dividends. I understand that is their choice.
10 What I am talking about is trying to direct it to something
11 that will put that incentive for them to do modernization of
12 their manufacturing capacity.
13 If you put it to a vote of businessmen, they would rather
14 have a tax-cut than accelerated depreciation.
15 Senator Danforth. These were economists also. They said,
16 even from the standpoint of capital formation that the major
17 problem that they have is to look down the road at the rate of
18 return they are going to get on today's capital investment, and
19 the issue between a corporate tax cut and accelerated depreciation
20 is really in what years do you see your taxes reduced?
21 Accelerated depreciation would tend to reduce your taxes
22 more on the front-end years where a tax cut, particularly a phase-
23 down tax cut, which is what they seem to be talking about, would
24 put that tax cut more in future years. And the preponderance
25 of the testimony that we got from the witnesses and the preponderance

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1 of opinion of the people, not only the business people, but the
2 economists as well, not unanimous, because there really is a
3 difference of opinion, but a preponderance of testimony is that
4 in making investment decisions they are tending to look farther
5 down the road than maybe they used to a few years ago. And
6 even from the standpoint of capital formation -- which I could
7 not agree more -- is the big question now.
8 Their view is the way to accomplish that is by a phased
9 rate reduction.
10 The problem with the House bill is, while the Administra-
11 tion proposed reducing the corporate rate down to 44 percent,
12 the House bill has it as 46 percent,and one of the concerns that
13 I have is that if we keep that at 46 percent and then go to
14 ADR, we did not have anything n the way of rate reduction in
15 conference.
16 Senator Bentsen. I think that is a good point. I am trying
17 to look at the future, any rate reductions beyond the initial
18 one.
19 The Chairman. Let me just bring up one other item. I would
20 like to have the Senators think about it. It is very attractive
21 to say that we would take the capital gains tax off the first
22 $100,000 on people's home, that I must say that the House
23 performance -- I know how these things happen. The House
24 performance on the minimum tax has been to go from one extreme
25 to the other extreme.

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The House, a year or two ago, was asking that we have no allowance whatsoever that the people have already paid, so that the minimum tax would have been an outrageous tax at that point if we had completely eliminated the consideration of the taxes people already paid, and that would be an add-on tax.

Then the House comes back to us advocating something that would repeal the minimum tax as far as a lot of people were concerned and then they came in with what the Treasury calls the "micro-mini" tax. It still has a minimum tax but it is so minor that you cannot find it, the microscopic tax.

What concerns me about the $100,000 exemption, we now have a situation where taxpayers making over $200,000 are paying that tax. If they owe us something, they are paying us something. I am very much concerned about someone in the future saying you have the thing down now where you have pretty well covered the situation of a person making $200,000 but let's just drop it down $100,000 and see where you stand on people who are making $100,000. How many of them are paying us no tax?

At that point, they would be able to show us thousands of people -- perhaps 1,000, perhaps several thousand taxpayers who have paid us no income tax because they have made $100,000 and paid no tax. That would be the basis of it right here on the $100,000.

I am not seeking to arrive at some situation where we penalize unduly some dear old couple who have sold their home and

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1 had a one-time capital gain of $100,000 but when we fix it that
2 they pay no tax at all, I can see the basis for a new Treasury
3 study showing a lot of taxpayers who made substantial income --
4 perhaps some with $200,000 or more and paid no tax.
5 What is the potential of that, Mr. Lubick?
6 Mr. Lubick. In the case of the residence, if you have
7 $100,000 of gain and you pay zero tax, I guess there could be some
8 potential for that. Again, if we move in the direction of the
9 true alternative minimum tax that we have been talking about,
10 one could include -- I do not know what your attitude was on
11 including the $100,000 of capital gains from the sale of a
12 residence. If you included that, of course you would avoid that
13 outcome that could be a way out.
14 The Chairman. It seems to me that now we have our minimum
15 tax and we are working to a point where we are not showing these
16 horrible examples, that we should not all in the trap where it
17 happens all over again.
18 One thing that I can anticipate, once you get one thing under
19 control, people start keeping score on you on a different basis.
20 For the rank and file people, $100,000 is still a good chunk of
21 income. If a tax applies in that situation, then I would think
22 that the minimum tax ought to apply to it.
23 I take it Treasury would favor that?
24 Mr. Lubick. Our original proposal at present, made in
25 January, was to take capital gains on the sale of residences out

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1 of the minimum tax altogether. That was in the context of a
2 very different minimum tax, and in the context of full taxation
3 of capital gains rates, or capital gains on the sale of residences,
4 except where the roll-over applied for those persons over 65.
5 To the extent that what you put the new exclusion in the
6 minimum tax, it might introduce an element of balance to what
7 may well be regarded as an excessively generous exemption.
8 The Chairman. I am not thinking of putting a huge tax on
9 somebody. I am thinking of the taxpayers' concept that is out
10 of date now, when they think that half the millionaires pay no
11 income tax -- but that is badly out of date. But it never was
12 that bad.
13 But it was bad at one point, and at 23 percent we are
14 getting away with it, because of the charitable deduction.
15 I just want to go to a point where people have substantial
16 income in the economic sense, that they pay us something, that
17 they do not pay us practically nothing.
18 What is your thought about that, Mr. Shapiro?
19 Mr. Shapiro. I think that you are expressing concern, that
20 the statistics are coming out and the totals are being looked
21 at, is how many people are getting by paying no taxes, not the
22 reasons.
23 For example, there are some who pay no taxes because of high
24 medical expenses, large losses. Some have foreign taxes that
25 they pay which are credited against the U.S. taxes.

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The statistics do not ncessarily discuss why these non- or low-taxpayers are accounted for, but that there are so many numbers.

I think the concern you are expressing, that we should try to have all taxpayers pay some amount of tax, and if you have an exclusion on residence, no matter how meritorious it may be for a once in a lifetime capital gain, it would lead to some statistics that would go back to a number of taxpayers on those rolls who are not paying any tax.

The Chairman. It seems to me that we have to improve our score-keeping. One of the things that ought to be done where a person has paid a tax to a foreign government, that ought to be regarded as a tax that he has paid. We make these treaties with foreign governments where we agree that we will tax your people who are doing business over here and you will tax our people who are doing business in your country. Where we, by treaty, agree to do that, we should regard that as a tax paid.

The same principle, if you have a sales tax in two states, you pay the sales tax in one state, but not in both states.

So out of these four ways that we are looking at score-keeping, I think that we might have enough where we have one we like the best for score-keeping purposes, then we ought to say all right, let us draft our law so it is going to show who the people are that are not paying enough and hereafter we will try to see that they do pay enough.

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1 Mr. Shapiro. What I was referring to, of the 22 taxpayers
2 that are indicated in the Treasury's most recent study that had
3 high incomes and paid no taxes, 14 are there because of a foreign
4 tax credit. They did pay taxes, but they were foreign taxes, and
5 most, if not all of the rest, were because of casualty losses or
6 high medical expenses.

7 The Chairman. The way I look at those 22, if we are keeping
8 score the way we ought to be keeping score, we would not be
9 picking out any of those, because the whole 22 of them are people
10 that are regarded as high-income earners only because you do not
11 look at the casualty losses, the taxes paid to foreign governments,
12 the state and local taxes, that which falls below the line which
13 is called adjusted gross income.

14 If we go to a concept of expanded income, or something of
15 that sort, where you are taking those expenses into account and
16 then we add back in the preferences to see what they really made,
17 then from that point then say how much do these people pay in
18 tax, I would think we would have a better score-keeping, and
19 hopefully something we could agree to, and try to zero this
20 minimum tax on that group to see how many have gotten by paying
21 us nothing. Those who did, should be made to pay something
22 substantial.

23 In other words, maybe for future years and this year
24 will not do it very well because the taxes we are applying this
25 year cannot be fairly applied to income that is already earned,

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1 but for the future, starting in the next calendar year, I would
2 hope that we could have a score-keeping arrangement that we
3 could agree on and the Treasury could support, too, that would
4 appeal to both the conservatives and liberals and then we could
5 say all right, on this basis, let us try to see to it that people
6 pay a fair amount.

7 Mr. Sunley. Mr. Chairman, as you know, there are four
8 different income concepts used in the income report and the report
9 this year, the foreign tax credit was not treated separately.
10 Possibly what we could do, is have Committee Report language that
11 allows us to have only two income tax concepts.

12 I think you want to keep the adjusted gross amount.

13 We would be perfectly in agreement, if the only reason a
14 person is not taxable is a foreign tax credit, treat them as
15 being taxable for the purposes of high income.

16 The Chairman. It seems to me that if you are going to keep
17 the AGI -- the expanded gross income -- at all, you ought to work
18 it out that that is a very inadequate, poor comparison to make,
19 because there are all sorts of people that have a lot of adjusted
20 gross income and did not have any real net income at all.

21 The most obvious example is a businessman who made $300,000
22 before you looked at his casualty loss. For that particular
23 year, his place of business burnt down and he lost $1 million
24 when the business burnt down.

25 I can think of a friend who suffered a disaster. It took

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1 twenty years to get over it. They had a fire in his building
2 and it was an absolute disaster. The story of the man's life, you
3 might say, because as hard as he had worked for everything he had,
4 he was absolutely wiped out by that disastrous fire.
5 Based on the way that the AGI concept would work, that would
6 have been a good year, made a ton, paid no taxes. That would be
7 the year that he got wiped out because of fire, but the casualty
8 loss would not appear if you are just looking at adjusted gross
9 income.
10 Maybe we can agree that from hereafter we will just use the
11 AGI for comparative purposes, but perhaps we could agree on one
12 of these other three methods, whichever seems the best.
13 Mr. Sunley. Maybe we could write the report in terms of
14 one income set and see how this relates back to the adjusted
15 gross income.
16 The Chairman. I would hope that we would get together on one.
17 It seems to me when you are talking about what one actually has
18 made -- it is confusing if you talk about three concepts. You
19 have to get down to it for the purpose of tax justice. We have
20 to think in terms of just one.
21 Mr. Shapiro. I think there is general agreement that
22 Treasury is expressing now, and I think that we can work with
23 them for an appropriate change. If it needs report language, we
24 will bring that. If it needs legislative language, we will bring
25 that, but I think the point is appropriate.

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The Chairman. It seems to me that for all the controversy and discussion we had on the matter in the previous Tax Reform law -- I had a suggestion; Senator Haskell had a suggestion; someone else had a suggestion: we said, let's try all three. Now we have had a chance to look at all three and Treasury says you ought to continue the old one, because otherwise you would have no basis for comparison.

Now I think we have what we need to arrive at one. Maybe the one would not be any one of our suggestions. It may be a mix of all the suggestions that are made, but in my judgment, it definitely ought to include all the itemized deductions that fall into place after you arrive at adjusted gross income and it ought to include adding back the preferences when you get all that.

Hopefully we will have something that everybody could agree on, that this is a fair way to keep score, and on that we should be judged.

Senator Byrd. I would like to throw out a suggestion for the Committee's consideration. It comes to mind because the Chairman mentioned gift taxes today.

I would like to throw out the suggestion that the Committee consider increasing the annual $3,000 exclusion. It seems to me that is pretty much outdated now. It goes back to 1942. I do not know what how that is equivalent to 1978 dollars, but it is something to consider that the Committee might want to consider --

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at least this member would like to consider it.

The Chairman. Does Treasury have a suggestion?

Mr. Lubick. I think, Senator Long, with the unified tax, you would probably be better off dealing with the appropriate level of the overall exclusion, lifetime and deathtime, rather than focusing in on the annual lifetime. The fact that a person happens to dispose of his property during his lifetime ought not to give him an advantage as opposed to that person who leaves it under his will.

If you think that the overall level of exemption is inadequate, I think you would be better off dealing with it in terms of the unified exemption and the unified credit as opposed to the annual exclusion which has as its purpose the elimination of de minimis Christmas gifts and things like that that you do not want to take into account in the overall transfer of wealth.

So if you expand the exclusion on an annual basis, I think you would be getting into a situation where you would be allowing greater and greater transfers to avoid the whole system altogether.

If indeed you want to have an increased level of exempt transfers, I think you would be better off treating it on a uniform basis.

Senator Byrd. This deals with the annual exclusion which has been in the tax laws ever since we have had tax laws. The suggestion is that the $3,000 annual exclusion is pretty much outdated now.

Mr. Lubick. Actually, it was higher between 1942.

Senator Byrd. It was, and it went back to $3,000. It has been at $3,000 ever since 1942 and it seems to me that it is pretty much outmoded. You ought to consider raising that to $6,000 or $5,000 or something like that.

The Chairman. Here is what concerns me about that. If we could actually get a rate to the point where people would not be engaged in a constant scramble and a constant tax-planning arrangement to try to keep from paying the amount that the rates would indicate we might be able to raise as much money, and maybe more, and avoid this thing of people setting up foundations when those are not the people who have charity in mind. They set up the foundation for the purpose of saving taxes, not for the purpose of helping any particular group.

When we first got into the foundation scheme, we came across the fact that people did not have any idea of helping people. It was just to avoid taxes.

For example, one tax lawyer told me, if the top rate were 50 percent his client would put all of his money, and just leave it to his heirs, but at a 70 percent rate, the client is going to put most of it into a foundation and a lot of cases, of course, the government gets nothing out of it.

Maybe Treasury could come up with suggestions that they could help us along that line. If they could, that would be very useful. Otherwise, what will happen, Mr. Lubick, is people saying,

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1 gee, that $3,000 used to mean something. It does not mean half
2 that much now.
3 If the rate is still going to be one that people are going
4 to spend their time trying to get out of it, and they can use
5 insurance as one device and use others, if you show us what the
6 principal devices are used to make it more attractive for people
7 to go ahead and pay the money rather than to engage in the alter-
8 native, I would think that it would be useful.
9 Senator Byrd. This is really not an alternative to getting
10 out of taxes. People ought to have an opportunity to make gifts
11 of a reasonable nature, of a reasonable amount, to their friends or
12 children or whatever. The law has recognized that over a period
13 of many years.
14 The only point is whether it should be $3,000 or whether it
15 should be increased because of the rate of inflation that the
16 Congress has helped create.
17 The Chairman. I see your point.
18 Well, then. We will meet again tomorrow at 10:00 o'clock.
19 (Thereupon, at 12:35 p.m. the Committee recessed, to reconvene
20 at 10:00 a.m. on Tuesday, September 12, 1978.)
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Joint Committee on Taxation
September 11, 1978

PROPOSALS TO H.R. 13511

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JOINT COMMITTEE ON TAXATION
September 11, 1978

I. PROPOSALS DEALING WITH INDIVIDUALS

A. General Tax Cuts, Rates, Personal Exemption, ZBA and Credits

1. Rate Reductions

The proposal would provide additional individual rate reductions (as compared to H.R. 13511) to make sure that all income classes receive income tax cuts which compensate for the tax increase resulting from the expected tax increase from inflation in 1978 and for the employee's share of the social security tax increase enacted in 1977 and scheduled to take effect next year. Revenue effect.--

2. Indexing

The proposal would index for inflation all the fixed dollar amounts used in determining individual income taxes. Alternatively the rate brackets, zero bracket amounts, the general tax credit, personal exemption and the earned income credit would be indexed. Revenue effect.--This would reduce budget receipts by $5 billion in fiscal year 1979, $12 billion in fiscal year 1980, and $21 billion in fiscal year 1981.

3. Indexing Tax Brackets

The proposal would widen the income tax brackets by an additional 1 percent as compared to H.R. 13511 (i.e., 7 percent instead of 6 percent). Revenue effect.--This would reduce tax liabilities by $670 million in calendar year 1979.

4. Personal Exemption

The proposal would convert the current personal exemption into a $275 credit. Revenue effect.--This would reduce tax liabilities by $1.6 billion in calendar year 1979 and $550 million in calendar year 1980.

5. Additional Exemption for Disabled

The proposal would provide an additional personal exemption for the permanently and totally disabled. Revenue effect.--This would reduce tax liabilities by $1.3 billion in calendar year 1979 if the additional exemption is $1,000 and $1.0 billion in calendar year 1979 if the additional exemption is $750.

6. Increase Standard Deduction

The proposal would increase the zero bracket amount (standard deduction) and personal exemption in States where the cost of living exceeds an amount which is 115 percent of the national average (Alaska and Hawaii). Revenue effect.--This would reduce tax liabilities by $70 million in calendar year 1979.

7. Zero Bracket (Standard Deduction) for Single Heads of Household

The proposal would raise the zero bracket (standard deduction) for single heads of household to the level applicable to married couples filing a joint return instead of that applicable to single persons. Revenue effect.-- This would reduce tax liabilities by $702 million in calendar year 1979.

8. Earned Income Credit

The proposal increases the earned income credit to 10 percent of the first $6,000 of earnings with a phaseout between $6,000 and $9,000 to $12,000. The proposal would also modify the earned income credit in several other respects. Revenue effect.-- This would reduce tax liabilities in calendar year 1979 by $900 million, if the phaseout is $6,000 to $9,000, by $1.2 billion if the phaseout is $6,000 to $10,000, and by $1.8 billion if the phaseout is $6,000 to $12,000.

9. Earned Income Credit

The proposal increases the earned income credit to 10 percent of the first $5,000 of earnings with a phaseout between $5,000 and $10,000. The proposal would also modify the earned income credit in several other respects. Revenue effect.--This would reduce tax liabilities by $800 million in calendar

10. Credit for Social Security Taxes

The proposal would provide a refundable tax credit to employers, employees and self-employed equal to 5 percent of social security taxes. Revenue effect.-- This would reduce tax liabilities by $5.6 billion in calendar year 1979.

11. Tax Credit for Care of the Elderly

The proposal would increase the maximum amounts of income eligible for the elderly credit from $2,500 to $3,000 for single persons and from $3,750 to $4,500 for married couples. In addition, the adjusted gross income level above which the credit phases out would be increased from $7,500 to $15,000 for single persons and from $10,000 to $17,500 for married couples. Revenue effect.--This would reduce tax liabilities by $70 million in calendar year 1979.

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B. Itemized Deductions

12. Charitable Contributions

The proposal would permit a charitable contribution deduction by taxpayers who do not itemize their deductions. The deduction "above the line" would be subject to a dollar floor such as $100. Revenue effect.-- With a $100 floor, this would reduce tax liabilities by $1.3 billion in calendar year 1979.

13. State and Local Income Taxes

The proposal would permit a deduction above the line for all or a part of State income taxes. Revenue effect.--

14. <u>State and Local Real Estate Taxes</u>

The proposal would provide a 50-percent tax credit for the first $1,000 of State or local real estate taxes on a taxpayer's principal residence. The deduction for taxes paid would be reduced for taxes which are taken into account for the tax credit. <u>Revenue effect</u>.--This would reduce tax liabilities by $3.1 billion in calendar year 1979.

C. <u>Deferred Compensation</u>

15. <u>Public Deferred Compensation Plans</u>

The proposal would remove the $7,500 limitation under H.R. 13511 as to State and local government plans. The proposal would also apply the limitations and requirements for public plans to other tax-exempt organizations. <u>Revenue effect</u>.--This would have no significant effect on revenues.

16. <u>Public Deferred Compensation Plans</u>

The proposal would permit an eligible participant in a State and local government deferred compensation plan to elect to defer compensation on a monthly rather than an annual basis. <u>Revenue effect</u>.-- This would have no effect on revenues.

D. <u>Other Proposals</u>

17. <u>Income Averaging</u>

The proposal would eliminate the reduction in the benefits of income averaging resulting from the 1977 introduction of the zero bracket amount. <u>Revenue effect</u>.-- This would reduce tax liabilities by $150 million in calendar year 1979.

18. Maximum Tax on Earned Income

The proposal would eliminate the limitations that earned income be limited to 30 percent of total income from a business in which capital and labor are both material income-producing factors, and provide that the 50-percent maximum tax applies only to income that constitutes reasonable compensation for services actually rendered. Revenue effect.--

19. Increase Dividend Exclusion

The proposal would increase the present $100 dividend exclusion ($200 for joint returns) to $150 for single returns ($300 for joint returns). Revenue effect.--This would reduce tax liabilities by $249 million in calendar year 1979.

20. Exclusion for Dividend Reinvestment

The proposal would provide an annual exclusion of up to $1,000 for a single taxpayer ($2,000 for a joint return) in the amount of dividends that are reinvested to purchase original issue stock. Revenue effect.--This would reduce tax liabilities in calendar year 1979 by $900 million assuming a low participation and $1.5 billion assuming a high participation.

21. Taxable Bond Option

The proposal would permit the holder of a bond (which can qualify for tax exemption under present law) to elect on an annual basis to treat the interest either as tax-exempt interest or taxable interest. If the holder elected to treat the bond as taxable, he or she would gross up a percentage of the interest and include this amount in income and receive an offsetting percentage credit. Revenue effect.--

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22. Exclusion for Uniform Services, Health Professions, Scholarship Program Awards

This proposal would extend the temporary exclusion for amounts received by participants in the uniformed services, health professions (including the armed forces and public health services health programs) for those students entering the program in 1979. This extension would apply through 1983 and generally would cover participants in the 1979 freshman medical school classes for their 4 years of training. Revenue effect.--

23. Employer Educational Assistance Programs

This proposal would exclude from an employee's income amounts paid for expenses incurred by the employer for educational assistance for the employee if such amounts are paid or such expenses are incurred pursuant to a qualified, nondiscriminatory program. Revenue effect.--

24. Moving Expense Deduction

The proposal would provide a deduction for moving expenses incurred by a taxpayer over 60, even though the move was not job-related. The deduction would be allowed on a one-time basis. Revenue effect.--

25. Business Deductions for Members of Congress

The proposal would modify the present $3,000 limitation on the deductibility of living expenses by Members of Congress. It generally would conform the deduction to that permitted to other businessmen. Members of Congress would be allowed to deduct as an ordinary and necessary business expense, without the requirement of detailed recordkeeping, $44 per day times the number of days that the Member was away from home on legislative business. Revenue effect.--

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26. Limitation on Investment Interest Deductions

The proposal would repeal the existing limitation on investment interest deductions. Revenue effect.--This would reduce tax liabilities by $100 million in calendar year 1979.

27. Foreign Conventions

The proposal would eliminate the recordkeeping requirements that are required to substantiate attendance at a foreign convention. Revenue effect.--This would reduce tax liabilities by less than $10 million in calendar year 1979.

28. Report of Tips

The proposal would amend the recordkeeping and reporting requirements relating to tips by providing (1) that the only records which an employer would be required to keep in connection with charged tips would be charge receipts and copies of statements furnished employees; (2) that the only tips the employer must report would be those reported to the employer by employees; and (3) that Forms W-2 filed by an employer would satisfy IRS information reporting requirements with respect to tip income of employees. Revenue effect.--This would reduce tax liabilities by less than $5 million in calendar year 1979.

29. Nonqualified Stock Options

The proposal would permit the taxpayer to allow to treat a qualified stock option as a nonqualified stock option. Revenue effect.-- This would reduce budget receipts by $5 million in fiscal year 1979.

30. Teacher Annuities for Mutual Funds

The proposal would liberalize the restrictions against withdrawal from a sec. 403(b) plan. Withdrawals would be permitted when the employee retires, dies, separates from service of the employer at any age, becomes disabled, attains age 59-1/2, or encounters hardship. The term "hardship" includes the need for funds to purchase a home or for college education. Revenue [illegible]--This would have no effect on revenues.

31. Simplified Pension Plans

The proposal would enable employers to establish simplified pension plans using individual retirement accounts to hold plan assets. Under a simplified plan, paperwork and complexity would be substantially reduced. Contributions for an employee would be limited to $7,500 or 15 percent of pay, whichever is less. Revenue effect.--

32. Deduction for Certain Employee Retirement Savings Contributions

The proposal would allow a participant in a tax-qualified plan to deduct amounts contributed to an IRA, to a qualified plan, or both, up to a maximum aggregate deduction of $1,000 or 10 percent of compensation, whichever is less. Also, the bill would allow a participant in certain group retirement trusts to deduct contributions to the trust, to an IRA, or both, up to certain maximum aggregate amounts. Revenue effect.--This would reduce tax liabilities by $870 million in calendar year 1979.

33. Limited Individual Retirement Deduction for Plan Participants

The proposal would permit a plan participant, etc. to make a deductible contribution to an IRA in an amount equal to the difference between (1) the current-law dollar limitation on IRA contribution deductions, and (2) the amounts contributed by or on behalf of the individual to a tax-qualified plan, to a government plan, or to a tax-sheltered annuity. Revenue effect.--

34. Individual Retirement Accounts

The proposal would index the $1,500 limitation on annual contributions to an IRA. Revenue effect.--

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35. Pensions--Lump-Sum Distributions

The proposal would provide that a distribution from a qualified plan could be rolled over to an IRA, if, solely because of the aggregate rules, the distribution failed to qualify as a lump-sum distribution. Aggregation of separate trusts under a single plan would continue to be required and 10-year income averaging would not be provided. Revenue effect.--

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II. PROPOSALS DEALING WITH TAX SHELTERS

36. At Risk -- Transitional Rule

The proposal would provide a transitional rule for partnerships subject to the at risk rule to treat all partnership pre-1977 obligations as recourse obligations. Revenue effect.--

37. At Risk for Equipment Leasing

The proposal would modify the at risk rules to provide an aggregation rule for closely-held corporations which are engaged in equipment leasing similar to the aggregation rule for newly covered activities. Revenue effect.--

38. At Risk for Equipment Leasing

The proposal would modify or eliminate the at risk rule in the case of equipment leasing by noncorporate and Sub-S corporate lessors who compete with larger corporate equipment lessors. Revenue effect.--

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III. PROPOSALS DEALING WITH BUSINESS

A. Corporate Tax Rates

39. Corporate Rate Reductions

The surtax exemption could be increased to $150,000. For taxable years beginning after December 31, 1978, a tax of 20 percent would be imposed on the first $150,000 in taxable income and 48 percent on taxable income in excess of that amount. Revenue effect.--This would reduce tax liabilities by $3.7 billion in calendar year 1979 and budget receipts by $1.7 billion for fiscal year 1979.

40. Corporate Rate Reductions

The surtax exemption could be increased to $200,000 and the following rates could be imposed:

Taxable Income	Tax Rate Percent
0 to $50,000	15
$50,000 to $200,000	22
Over $200,000	44

Revenue effect.--This would reduce tax liabilities by $11.9 billion in calendar year 1979 and budget receipts by $5.3 billion in fiscal year 1979.

41. Corporate Rate Reductions

A tax of 17 percent could be imposed on the first $75,000 in taxable income and a tax of 45 percent on taxable income in excess of that amount for 1979 but with an additional one percentage point reduction annually until the highest corporate rate reached 42 percent in 1982. The following rates could be imposed:

Taxable Income	Tax Rate Percent
0 to $75,000	17
Over $75,000	45 in 1979 44 in 1980 43 in 1981 42 in 1982

Revenue effect.--This would reduce tax liabilities by $7.3 billion in calendar year 1979 and budget receipts by $3.3 billion in fiscal year 1979. Calendar year 1983 liabilities would be reduced by $17.4 billion and fiscal year receipts by $16.2 billion.

42. Corporate Rate Reductions

For 1979, the provisions of the House bill could apply. For 1980, the top rate could be reduced from 46 percent to 44 percent, the 30-percent bracket could be increased to taxable income of $50,000 to $100,000 (rather than $50,000 to $75,000), and the 40-percent bracket could be increased to taxable income of $100,000 to $150,000 (rather than $75,000 to $100,000). For 1981 and succeeding years, the following rate schedule could apply:

Taxable Income	Percent
$ 0 to $25,000	17
$25,000 to $50,000	20
$50,000 to $100,000	30
$100,000 to $200,000	40
Over $200,000	42

Revenue effect.--This would reduce calendar year liabilities by $5.1 billion in 1979, $9.8 billion in 1980, and $14.3 billion in 1981. Budget receipts would be reduced by $2.3 billion in fiscal year 1979, $7.2 billion in 1980, $11.8 billion in 1981, and $14.9 billion in 1982.

43. Corporate Rate Reductions

The surtax exemption could be increased to $100,000 beginning in 1978 and the rates could be reduced over a 3-year period as follows:

1978	19% on the first $25,000
	21% on the next $75,000
	47% on the excess over $100,000
1979	18% on the first $25,000
	20% on the next $75,000
	46% on the excess over $100,000
1980	17% on the first $25,000
	19% on the next $75,000
	45% on the excess over 100,000

Revenue effect.--Assuming a January 1, 1979, effective date, this would reduce revenues by $1.8 billion in 1979, $5.1 billion in 1980, and $7.9 billion in 1981.

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B. Investment Credit

44. Investment Tax Credit

The proposal would make the investment tax credit refundable (or allowable against the 100-percent tax liability) to the extent of the first $25,000 of the credit. The limitation would be 90 percent of tax liability above $25,000. Revenue effect.--This would reduce revenues by $2.4 billion in calendar year 1979.

45. Investment Tax Credit

The proposal would increase the limitation against tax liability to 90 percent beginning in 1979, rather than being phased in by an additional 10 percentage points per year (as under H.R. 13511). Revenue effect.-- This would reduce tax liabilities by $1 billion in calendar 1979.

46. Investment Tax Credit

The proposal would increase the limitation against the tax liability to 100 percent by 1983. The additional 10 percentage points (as compared to H.R. 13511) would apply beginning with taxable years which end in 1983. Revenue effect.--This would reduce tax liabilities by $200 million in calendar 1983.

47. Investment Credit for Rehabilitation Expenditures of Certain Structures

The proposal would provide a 10-percent credit for qualified rehabilitation expenditures of all existing structures which are 20 years old (including owner-occupied residential property). The amount of the credit would be limited to $2,000. Revenue effect--

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48. Investment Credit for Rehabilitation Expenditures of Certain Structures

The proposal would provide a 10-percent investment credit for certain rehabilitation expenditures for industrial, retail and warehouse buildings which are 10 years old if the amount of the expenditures are more than 25 percent of the adjusted basis of the building. Revenue effect.--This would reduce tax liabilities by $1.2 billion in calendar 1979.

49. Investment Credit for Certain Structures

The investment credit would be extended to all industrial and utility structures including the cost of new buildings. Revenue effect.--This would reduce tax liabilities by $1.6 billion in calendar 1979.

50. Investment Credit for Certain Structures

The proposal would extend the investment credit for structures to the construction of new industrial and retail structures and warehouses. Revenue effect.--This would reduce tax liabilities by $2.1 billion in calendar 1979.

51. Investment Tax Credit

The proposal would increase the used property limitation from $100,000 to $200,000. Revenue effect.--This would reduce tax liabilities by $100 million in calendar 1979.

52. Investment Tax Credit

The proposal would shorten the useful life of an asset for purposes of the investment tax credit. If an asset had a useful life of 3 years or more, it would be eligible for the full 10-percent investment tax credit. Revenue effect.--This would reduce tax liabilities by $1.3 billion in calendar 1979.

53. Investment Credit for Research and Development Expenditures

The proposal would allow a credit against income taxes equal to 5 percent of the eligible research and development expenditures in addition to the 5-year amortization rule. Revenue effect.--This would reduce tax liabilities by $800 million in calendar 1979.

54. Investment Tax Credit for Agricultural Structures

The proposal would provide that special purpose structures or enclosures used for single purpose food or plant production are eligible for the investment credit. To be eligible, the structure would be required to be specifically designed and used solely for the production of poultry, eggs, beef, pork, or plants. Revenue effect.--

55. Investment Tax Credit for Cooperatives

The proposal would expand the investment tax credit that is available to cooperatives. The credit would be computed by the cooperative without regard to the deduction for patronage distributions. Revenue effect.--

56. Additional Investment Credit for Recycling Equipment

The proposal would permit an additional 10-percent investment credit for investment in solid waste recycling equipment. This additional credit would be available for equipment which is used exclusively for one of two purposes: either (1) to sort, prepare, and recycle solid waste to recover usuable raw materials or a fuel, or (2) to burn solid waste as a fuel to create heat, steam, or other useful forms of energy. Revenue effect.--This would reduce tax liabilities by $30 million in calendar 1979.

57. Investment Credit for Railroad Property

The proposal would permit a lessor of railroad property to be eligible for the increased limitation for railroads if the lessor corporation was 25-percent owned by a corporation which manufacturers railroad property. Revenue effect.--This would reduce tax liabilities by less than $10 million in calendar 1979.

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58. Investment Tax Credit Carryovers

The proposal would allow additional one-year carryover for investment tax credits which would otherwise expire at the end of 1977 in the case of credits from airline property which could not be used in earlier years because of net operating losses. Revenue effect.--This would reduce 1979 budget receipts by less than $2 million and it may reduce budget receipts by a maximum of $7 million in future years.

59. ESOPs

The proposal would increase the additional investment tax credit for ESOPs to 2 percent and allow an alternative 1-percent credit for compensation paid to ESOP participants. The proposal would also make several technical changes in the ESOP rules. Revenue effect.--This would reduce tax liabilities by $1.8 billion in calendar year 1979 and $4.2 billion in calendar year 1983.

60. ESOPs

The proposal would increase contributions to 50 percent of payroll for leveraged ESOPs. Revenue effect.--

C. Jobs Credit

61. Expanded WIN and Welfare Recipients Credit

The existing WIN credit would be expanded to 50 percent of wages and related expenses in the first twelve months of employment, 33-1/3 percent in the second twelve months, and 25 percent in the third twelve months. In 1979, the maximum wages per employee eligible for the credit would be $6,000. The amount would be increased to $6,500 in 1980 and $7,000 in 1981 to approximate the increases in the minimum wage (at an annual rate) currently scheduled to take effect in those years. The total amount of credit allowed for any taxpayer when combined with the wage deductions would not exceed 100 percent of the tax benefits of both. The credit would also be applied to nontrade or business employees. Revenue effect.--This would reduce liabilities in calendar year 1979 by $0.2 billion, and $0.8 billion in 1983.

62. Modified Targeted Jobs Credit

The employees eligible for the jobs credit would be limited to those currently eligible for the WIN and welfare recipient tax credits, Vietnam veterans with service connected disability and recipients of SSI disability beneifts. The credit would be extended to employees outside of a trade or business (like the existing WIN and welfare tax credits). The rate would be 80 percent of the first $6,000 of wages for the first year of employment, 60 percent for wages in the second year of employment and 30 percent for wages in the third year of employment. However, the wage deduction would be reduced by the amount of wages offset by the credit. The maximum amount of earnings on which the credit would be computed would rise to $6,500 in 1980 and $7,000 in 1981. The credit for any taxpayer with respect to employment outside of a trade or business would be limited to two employees per taxpayer. Revenue effect.--

The targeted jobs credit could be available with respect to employment of persons in families receiving payments under the AFDC or AFDC-UP programs, persons aged 18 to 24, and Vietnam era veterans who are from economically disadvantaged households, handicapped individuals, and recipients of disability payments under SSI. The amount of the credit could be one-third of the first $6,000 in wages for the first year of employment (maximum credit of $2,000), and one-fourth of such wages for the second year (maximum credit of $1,500). The employer's deduction for wages would be reduced by the amount of the credit.

63. General Credit Extensions

The existing general jobs credit could be extended with certain technical additions and modifications. Revenue effect.-- This would reduce tax liability by $2.5 billion in 1979.

D. Depreciation

64. ADR Depreciation System

The present ADR range which allows a taxpayer to use a useful life within a range of 20 percent below or above the presently determined useful life for the guideline class would be increased to 30 or 40 percent. Revenue effect on tax liabilities.--

	1979	1983
If ADR range is increased to 30%	-0.5	-3.0
If ADR range is increased to 40%	-1.1	-6.0

65. Additional First-Year Depreciation

The proposal would increase the dollar amount of property which can be taken into account which is eligible for additional first-year depreciation to $50,000 ($100,000 for individuals who file a joint returns). In addition the proposal would increase the percentage of the cost of such property to 30 percent. An additional proposal would eliminate the $1 million asset limitation under H.R. 13511. Revenue effect.-- This would reduce tax liabilities by $-920 million with $1 million asset limitation, and [illegible] asset limitation.

66. <u>Special Amortization for Tangible Personal Property</u>

The proposal would permit a taxpayer to elect to amortize up to $100,000 over a 3-year period and allow one-half (or all) of the investment tax credit with respect to property for which an election has been made. <u>Revenue effect</u>.--

67. <u>Current Deduction for Certain OSHA Expenses</u>

The proposal would provide expensing over a 3-year period for expenditures required by the Occupational and Safety Health Administration in addition to the investment tax credit. <u>Revenue effect</u>.-- This would reduce tax liabilities by $-3.0 billion in 1979.

68. <u>Current Expensing for Pollution-Control Facilities</u>

The proposal would permit the current expensing of costs for Federally mandated pollution-control equipment. Eligible costs would be limited to $200,000 annually. Current expensing would be permitted in lieu of allowing the investment tax credit for costs deducted. <u>Revenue effect</u>.--This would reduce tax liabilities by $450 million in calendar year 1979.

69. <u>5-Year Amortization for Low-Income Rental Housing</u>

The proposal would modify the definition of the minimum tax preference for 5-year amortization of low-income rehabilitation expenditures so that the preference amount would be the excess of 200 percent declining balance depreciation of straight-line based on the actual useful life rather than rapid amortization of straight-line. <u>Revenue effect</u>.-- This would reduce tax liabilities by less than $5 million in calendar year 1979.

70. <u>Indexing for Depreciation</u>

The proposal would expand the indexing provisions in H.R. 13511 to depreciation. <u>Revenue effect</u>.-- This would reduce tax liabilities by $0.4 billion in 1979 and $4.6 billion in 1983.

E. Small Business

71. Subchapter S Corporations

The proposal would repeal the current passive investment income limitation which provides that no more than 20 percent of the corporation's gross income can consist of passive investment income. Revenue effect.--

72. Credit for Investment in Original Issue Stock of Small or Medium-Sized Corporations

The proposal would allow a nonrefundable credit equal to 10 percent of the first $7,500 of investment in qualifying new stock issues during the taxable year. It would be limited to $750 ($1,500 in the case of a joint return), and would be subject to recapture on an early disposition of the stock. Revenue effect.-- This would reduce tax liabilities by $70 million in 1979.

73. Product Liability

The proposal would allow a deduction for contributions made to a product liability trust. The deduction generally would be limited to 2 percent of gross receipts or $25,000. Revenue effect.--

F. Other Proposals

74: Industrial Development Bonds

The proposal would increase the amount of the small issue limitations from $1 to $2 million (or $3 million) and from $5 to $15 million. Revenue effect.-- For the $2 million small issues, this would decrease tax liabilities by $3 million in 1979 and $54 million in 1983. For the $[illegible] million small issues, this would decrease tax liabilities by $[illegible] [illegible]on in 1979 and $60 million in 1983.

75. Industrial Development Bonds for Water Facilities

The proposal would extend the tax-free interest treatment for industrial development bonds to all water facilities whether or not for the general public. Revenue effect.--This would reduce tax liabilities by $4 million in 1979 and $79 million in 1983.

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76. Deficiency Dividends for Regulated Investment Companies

The proposal would provide a deficiency dividend procedure for regulated investment companies that are also small business investment companies. Under this procedure, a corporation could make qualified distributions after the normal period for making distributions when an adjustment by the IRS occurs that either increases the amount which the corporation is required to distribute or decreases the amount of the dividends previously distributed for that year. Revenue effect.--This would reduce tax liabilities by $-500,000 in 1979.

77. Real Estate Investment Trusts

The proposal would provide a safe harbor rule for income of a Real Estate Investment Trust derived from property held for sale to customers in the ordinary course of the REIT's trade or business. The proposal would exempt from the 100-percent penalty tax gain from the sale of property where (1) the property was held by the REIT for a minimum of 4 years, (2) the REIT made no more than 5 sales of property in the taxable year, (3) the REIT did not make improvements to the property during the 4-year period prior to sale in excess of 20 percent of the net selling price, and (4) the property was held for rent by the REIT for at least 4 years. Revenue effect.--

78. Arbitrage Bonds

The proposal would reverse the effect of recently issued proposed regulations dealing with arbitrage bonds, investment sinking funds, and advanced refunding. The proposal also prohibits future regulations relating to these issues from being issued until the end of 1979. Revenue effect.-- This would reduce tax liabilities by $15 million in 1979 and $0.2 billion in 1983.

79. Advanced Refundings

The proposal would permit industrial development bond advanced refundings of pre-1968 bonds to qualify for tax-exempt treatment if they satisfy certain conditions. Revenue effect.--This would reduce tax liabilities by $10 million in calendar 1979.

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80. ERISA Paperwork

The proposal would reduce filing requirements imposed on employee plans under the Employee Retirement Income Security Act of 1974 (ERISA). Revenue effect.--

81. General Stock Ownership Plans

The proposal would permit a State or local government to acquire corporate stock with borrowed funds, retire the debt with the dividends paid on the stock, and distribute the stock to residents of the State, etc. Dividends paid on the stock would be deductible by the corporation and stock distributed to residents would not be taxed to them until it is sold. Revenue effect.--

82. Life Insurance Companies

The proposal would treat annuity contracts sold by a life insurance company to a governmental pension plan or a governmental deferred compensation plan as pension plan reserves. Treatment as pension plan reserves would generally reduce the company's tax on its reserves under the contracts. Revenue effect.--

83. Contributions in Aid of Construction

The proposal would provide that gas and electric utilities do not receive taxable income from contributions in aid of construction. Revenue effect.--

84. Unrelated Business Income of Pooled Pension Funds

The proposal would provide an exemption from the unrelated business income tax in the case of investment funds created by qualified pension plans. Revenue effect.--

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85. Foreign-Source Income of Certain Savings and Loan Associations

The proposal would provide that interest earned on accounts in savings and loan associations located in Puerto Rico would be treated as foreign-source income rather than United States source income. Revenue effect.-- This would reduce tax liabilities by less than $5 million in 1979.

86. Special Limitations on Net Operating Loss Carryovers

The proposal would delay the effective date of the changes made by the 1976 Act with respect to the provisions dealing with the carryover of net operating losses in cases of acquisitions of loss corporations until January 1, 1980. Revenue effect.--

87. DISC

The proposal would retain the DISC provisions only for the first $1 million of total export profits. Revenue effect.-- This would increase tax liabilities by $1 billion in 1979.

88. Method of Accounting for Depreciation of Railroad Tracks

The proposal would legislatively sanction the present method of accounting permitted by the Internal Revenue Service for the replacement costs of railroad tracks. Presently, the IRS permits a railroad to currently expense the replacement cost. Revenue effect.-- This would not affect revenues.

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IV. PROPOSALS RELATING TO CAPITAL GAINS AND MINIMUM TAX

89. Sec. 1202 Deduction

The proposal would increase the present 50-percent exclusion from gross income for long-term capital gains to either 60 percent or 70 percent. Revenue effect.--Based on static estimates, this would result in reduced tax liabilities in calendar year 1979 by $2.7 billion if the exclusion is 60 percent and by $4.2 billion if the exclusion is 70 percent.

90. Sliding Scale Exclusion

The proposal would provide a sliding scale exclusion for capital gains depending upon length of time the asset was held by the taxpayer. The additional exclusion (above 50 percent) would be 3 percent per year for each year the asset was held up to 10 years, thereby resulting in a maximum exclusion of 80 percent. Revenue effect.--This would reduce tax liabilities by $2 billion in calendar 1979.

91. Special Exclusion

The proposal would allow individuals to exclude from gross income $1,500 of net capital gains ($3,000 in the case of a joint return). The section 1202 deduction would apply after the exclusion. Revenue effect.-- This would reduce tax liabilities by approximately $800 million in calendar year 1979.

92. Indexing of Certain Capital Assets

The proposal would extend the indexing provisions provided in H.R. 13511 to permit indexing on stock in a Real Estate Investment Trust and a Regulated Investment Company. Revenue effect.--

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93. Rollover of Gains from Equity Capital and Small Businesses

The proposal would provide that gain from the sale of a qualified small business investment would not be recongized to the extent investments are made in other qualified small businesses within 12 months from the time of the sale. A qualified small business investment would be an equity or unsecured investment in a small business concern (under section 3 of the Small Business Act) which is a capital asset in the hand of the investor when held for 12 months or longer. Revenue effect.--This would result in reduced tax liabilities of $600 million in calendar year 1979.

94. Alternative Tax

In addition to changes relating to the minimum and maximum tax under H.R. 13511, the proposal would provide a 25-percent alternative tax on capital gains without a $50,000 limitation. Revenue effect.--Based on static estimates, this would reduce tax liabilities by $800 million in calendar year 1979.

95. Minimum Tax

The proposal would repeal the present add-on minimum tax and the tax preference offset to the maximum tax. A "true" alternative minimum tax would be adopted, and would be payable only if it exceeded regularly computed tax. It would be graduated and would be based on taxable income, increased by tax preference items, and decreased by an exemption. Gain on the sale of a principal residence would not be a preference item for purposes of the alternative minimum tax, and the intangible drilling cost preference would apply only to those costs in excess of oil production income. Revenue effect.--This would reduce tax liabilities by $1.9 billion in calendar year 1979, and $2.1 billion in calendar year 1980.

96. Minimum Tax

The proposal would provide that the minimum tax would include as an item of tax preference only the amount of intangible drilling costs in excess of income from oil and gas properties. Revenue effect.--This would increase tax liabilities by $27 million in calendar year 1979.

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97. Personal Residence

The proposal would allow a once-in-a-lifetime exclusion of $75,000 on the gain from the sale of a taxpayer's principal residence if the taxpayer was either age 55 or older, or disabled. Revenue effect.-- This would reduce tax liabilities by $465 million in calendar year 1979.

98. Personal Residence

The proposal would make the $100,000 exclusion from the gain from the sale of a taxpayer's principal residence cumulative rather than on a one-time basis. Revenue effect.-- This would reduce tax liabilities by $40 million in calendar year 1979.

99. Personal Residence

The proposal would increase the present law exclusion ratio from $35,000 to $60,000 and lower the eligible qualifying age from 65 to 59. Revenue effect.-- This would reduce tax liabilities by $202 million in calendar year 1979.

100. Rollover of Gain on the Sale of a Residence

The proposal would change the effective date with respect to the provision in H.R. 13511 which permits rollover on gain realized on the sale of more than one principal residence where an individual relocates for employment purposes more than once within an 18-month period. The effective date would be changed from sales after July 26, 1978, to sales after December 31, 1975. Revenue effect.-- This would reduce tax liabilities by less than $5 million.

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V. MISCELLANEOUS PROVISIONS

101. Unrelated Business Income Tax on Bingo

The proposal would specifically provide that income derived by a tax-exempt organization from bingo would not be treated as unrelated trade or business income. Revenue effect.--This would reduce tax liabilities by $15 million in calendar year 1979.

102. Exemption from Private Foundation Rules for Certain Charitable Trusts

The proposal would provide that a charitable trust would be subject to the private foundation provisions only if a charitable deduction was actually allowed to the grantor for the amounts distributed to the trust. In addition, the proposal would provide that the self-dealing trust would be imposed only once for each act for the self-dealing. Revenue effect.--

103. Estate Tax on Appreciation

The proposal would repeal the present carryover basis rule and in its place provide a 10-percent additional estate tax would be imposed on the appreciation after assets imposed on a decedent's estate. The appreciation tax would apply with respect to property acquired from a decedent dying after December 31, 1979. Revenue effect.--

104. Widow's Estate Tax Exemption

The proposal would provide that the spouse of a decedent is deemed to have furnished consideration with respect to property in which a qualified joint interest is held in an amount equal to 2 percent of the unpaid mortgages or indebtedness on such property multiplied by the number of years the property was held by the decedent and the decedent's spouse. The maximum amount of the consideration that the spouse would be deemed to have furnished could not exceed 50 percent. Revenue effect.--This would reduce tax liabilities by $200 million in calendar year 1979.

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105. Carryover Basis

The proposal would delay the effective date of the carryover basis provision to apply with respect to decedent's dying after December 31, 1980. Revenue effect.--This would reduce tax liabilities by $36 million in calendar year 1979, $93 million in 1980, and $162 million in 1981.

106. Technical Corrections (H.R. 6715)

The proposal would add the substance of the Technical Corections Act (H.R. 6715) as reported out by the Senate Finance Committee. Revenue effect.--This would reduce budget receipts by $36 million in fiscal year 1979.

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