EXECUTIVE COMMITTEE MEETING

TUESDAY, MARCH 3, 1992

U.S. Senate

Committee on Finance

Washington, D.C.

ORIGINAL

The meeting was convened, pursuant to notice, at 11:06 a.m., in room SD-215, Dirksen Senate Office Building, Hon. Lloyd Bentsen, (Chairman of the Committee) presiding.

Also present: Senators Moynihan, Baucus, Boren, Bradley, Mitchell, Pryor, Riegle, Rockefeller, Daschle, Breaux, Packwood, Dole, Roth, Danforth, Chafee, Durenberger, Symms, Grassley and Hatch.

Also present: Vanda McMurtry, Staff Director and Chief Counsel; Ed Mihalski, Chief of Staff, Minority.

Also present: Fred Goldberg, Assistant Secretary for Tax Policy, Treasury Department; Glen Hubbard, Deputy Assistant Secretary for Tax Policy, Treasury Department.

Also present: Harry Gutman, Chief of Staff, Joint Committee on Taxation; Marina Weiss, Chief Health Counsel, Majority; Liza Potetz, Health Counsel, Majority; Randy Hardock, Tax Counsel, Majority; Dr. Alan Cohen, Budget Economist, Majority; Sam Sessions, Chief Tax Counsel, Majority; Bob Kyle, Chief Trade Counsel, Majority; Maurice Foley, Tax Counsel, Majority; Susan Himes, Tax Counsel, Majority; Alan Auerbach, Deputy Chief of Staff, Joint Tax Committee.

(The prepared statements of Senators Moynihan and Symms appear in the appendix.)

(The press release announcing the meeting follows:)

OPENING STATEMENT OF THE HON. LLOYD BENTSEN, A U.S. SENATOR FROM TEXAS, CHAIRMAN, COMMITTEE ON FINANCE

The Chairman. If people would be seated and cease conversation, this meeting will get under way. Over the past decade, middle-income families with children saw their taxes go up and their incomes go down.

More and more families in America, middle-income families, have two wage earners, and even that is not enough. They have had to work a month of extra hours each year just to keep from slipping back. A 40 percent loss in discretionary time; less time for parenting and all the problems that brings about.

Today we can start putting back fairness for middle-income American families into the Tax Code. My Chairman's mark has three goals. Fair tax treatment for working families and the assurance that high income Americans pay their fair share of taxes; incentives for long-term economic growth, and fiscal responsibility.

The heart of the proposal that I am putting before the Finance Committee today would give middle-income families a permanent tax cut; a $300 credit for each child, each year until that child turns 16.

For a family of four with two children, that family making $35,000--and that is the median income in America--that is a $600 tax reduction; a 25 percent cut in their income tax.

Now, I know $600 may be peanuts inside the Beltway, but it is serious money to a family trying to make a car payment, pay medical bills, or buy food. About 20 million Americans would get this tax credit from the child credit alone.

In addition to that, you would have the IRAs, capital gains, and the earned income credit will cut taxes for millions of more families. On the other hand, the President wants to give a bigger tax break to a far smaller number of the very top income.

Some 535,000 people would get $12,700 worth of tax cuts, under the President's plan. That is the same group that saw their taxes drop $16,400, on the average, during the 1980s.

To pay for this, the President has indulged in some creative accounting--a borrow-and-spend package that, according to the Joint Tax Committee, would increase the deficit by $27 billion over that five years. By adding to the deficit, in effect, is asking our children to pick up the tab.

I had a difficult time putting this proposal together, because I insisted we would not bust the budget; we would not add to the deficit; that every item had to be paid for.

It would have been very easy to satisfy all the members' requests, had we resorted to the creative accounting and the administration's budget. The Chairman's mark and what I have seen in the House legislation are paid for.

This middle-income tax cut would be paid for by a higher tax rate at the top less than one percent of the income scale, restoring fairness to our tax system. Less than one percent of taxpayers paying for that higher tax rate.

Even so, their tax rates still would be far lower than our economic competitors--countries like West Germany, where the top tax rate is 53 percent; Japan, where it is 50 percent--and lower than it has been in this country for most of the time since World War II.

Now, despite these differences, one of the major points about the Chairman's mark is that it seeks a common ground among Congress and the White House; among Democrats and Republicans.

In an effort to conciliate, I have put all seven of the President's proposals in this mark; all seven of those things he wanted for economic growth.

I have also included the Bentsen-Roth IRA, which has a strong bipartisan support--78 percent of the 100 Senators are co-sponsors. In addition, the Chairman's mark includes the Better Access to Health Care Bill, a bipartisan bill I introduced with Senator Durenberger to help Americans who work for small businesses get and keep health insurance.

It addresses job-lock, where a person has a preexisting condition--a back problem; a health problem--or their dependent does, or the spouse, and they are afraid to try to change jobs because they will not have that coverage in the next job.

It bars cherry-picking, where you see some insurance companies cover only the healthiest workers. If you have 25 employees, we will cover the 24, but this fellow has a heart condition and we cannot take him. And, yet, that is the one that needs it the most.

The President has taken many of the provisions of this bill, which is a major part of the mark, and put them in his own health bill. The American people are looking for progress, not partisan bickering.

With this proposal, we are making an honest effort to enact legislation that will increase access to health insurance and help boost our economy and restore fairness to our tax system.

I hope that the President will work with us in this process. But if he wants to protect just the less-than-one percent at the expense of average Americans and veto this bill because it asks that seventh/tenths of one percent to pay their fair share, that will be his choice and not ours.

I yield now to my distinguished colleague, the Ranking Minority Member, Senator Packwood.

OPENING STATEMENT OF THE HON. BOB PACKWOOD, A U.S. SENATOR FROM OREGON

Senator Packwood. Mr. Chairman, thank you. I come to this meeting more saddened than in rancor, because we had a chance for grandeur in this committee, and we are going to settle, instead, for gristle.

We have been, in this country, on a bipartisan binge of buying for at least the last 20-25 years--buying, not saving.

And there is not a single bill that is before us--not the President's, not the House bill, and, with all deference, Mr. Chairman, not your bill--that is going to catapult us into the savings and investment that will produce family wage jobs and keep us competitive in the world that we need. None of them will do that.

I had thought that the President's bill, as just the seven proposals--not the $500 increase in the dependency deductions, but just the seven proposals--might have been a gentle shove--not unlike shoving a rowboat out of a languid eddy, hoping that it will catch in the current of the stream--might have been the best of the three in moving us in that direction.

But, I emphasize again, it would not have taken us to where we needed to be. We had a chance, had we wanted to do it on a bipartisan basis, to accomplish what, at the time, we thought was a great step when we did tax reform.

And you may recall how we did that. In a very short period of time, on a bipartisan basis, three Democrats--all three of whom are still on this committee--and three Republicans--two of whom are still on this committee--would meet in my office each morning and we would give and take until we came up with a bipartisan bill that President Reagan would accept that passed this committee unanimously and passed the Senate 97 to three, and we thought was good for the country.

But this is not a bipartisan bill, and I understand partisan politics. We have all been in it for a fair period of time. The Majority is convinced that if they can make the President veto this bill, that would be a political plus for them in the election.

I, on the other hand, look at it from a different standpoint. Forty years ago in this country we taxed 20 percent of the Gross National Product.

By we, I mean all of the governments in the United States: Federal, State, local, school districts, water districts; everybody. And we now tax about 33 percent of the Gross National Product.

And, if we continue on that binge, in another generation we will look like Norway or Sweden, and we will tax 45, or 50, or 55 percent of the Gross National Product, and will have tax rates that will truly jar the middle class if we are going to exempt the poor to produce the money that we will need to support the governments on that grandiose a scale.

I might be able, if I was convinced it was going to reduce the deficit, to bring myself to supporting tax increases, but history just does not demonstrate that. We increase taxes and we increase spending.

And I do not care what we say we will do with it in this bill: year, after year, after year; decade after decade; generation after generation, for at least two generations we have increased taxes and we have increased spending.

So, when we had a chance bipartisanly to do what, in the back room last Thursday, we all agreed we needed--I will not mention which member said it, but he said it with a great degree of courage, and we all nodded our head--increased productivity, and increased savings, and decreased consumption.

And, for whatever reason, we have not had the courage to do that. And I do not mean that in a bipartisan sense. I am not sure that any of us have had the courage to do it.

But, Mr. Chairman, if we are going to do it, it can only be led by a Chairman. And the opportunity does not come often, and the opportunity is here, and it is still not too late.

So, if I might read a letter to the Chairman that all of the Republican members of the Finance Committee have signed, as follows:

"Dear Mr. Chairman: It is with the utmost respect for your leadership and vision that we are compelled to send you this letter. Although we may not always see eye-to-eye on every issue, we know you share our commitment to a strong and prosperous America.

As a highly-regarded member of the Senate and

Chairman of the Committee on Finance, we are calling upon you to put the good of our great country ahead of politics.

Throughout the country, people from all walks of life are counting on their elected officials to guide them through these tough economic times. Americans rightfully expect us to refrain from pursuing a short-sided strategy to score points in the next election.

Instead, they want us to shed partisan differences and work together to develop a bold, long strategy to strengthen our economy and propel America into the next century.

Over the last six months, many economists have appeared before Congress and advised us to proceed with great care this year. They cautioned against a short-term fix which would be counterproductive over the long-run.

There was a clear consensus that a significant tax increase at a time when the economy is struggling to get back on its feet will not stimulate economic growth and jobs creation.

Regretfully, the Majority in the Senate, like the majority in the House, appears intent on advancing legislation that will significantly raise taxes, while doing little or nothing to rebuild the competitive position of America.

This approach will not stimulate investment in productive endeavors so that Americans look forward to securing a good family wage, owning a home, raising a family, and enjoying a prosperous retirement.

Even the Chairman of the House Ways and Means Committee acknowledged that the House bill is essentially a political document, when he said last week, "I really do not want a bill if I can avoid doing it, but the political climate insists we have something."

Clearly, as long as the bill contains significant tax increases, it will be vetoed by the President, and the veto will be sustained. If the Majority insists on following this course, we urge that it be done expeditiously.

Vote the bill out of the Finance Committee today, waive the two-day layover rule, take the bill to the Senate floor immediately for final passage, conference quickly with the House, and be done with it.

However, we sincerely hope this futile course will not be pursued. We urge the committee to lay this bill aside and begin working together immediately to draft a plan to reinvigorate our economy and provide a blue-print for our future. This is no time for the Senate to succumb to political expediency.

Neither this bill, nor any bill that the House has considered, nor the President's bill, is a solution to the long-term economic problems facing this country, and we all know it.

We have the opportunity to rise above the fray and do something for the good of America. We should seize the opportunity now." Signed by all of the Republican members of the Finance Committee. And I thank the Chairman.

The Chairman. Thank you. Senator Moynihan, did you have any comments?

OPENING STATEMENT OF THE HON. DANIEL PATRICK MOYNIHAN, A U.S. SENATOR FROM NEW YORK

Senator Moynihan. Mr. Chairman, I am not sure he intended it, but our good friend and old colleague, Senator Packwood, prefaced the reading of that letter by the statement, "I do not mean it in a bipartisan sense." And I agree, once again, with my colleague. I also agree that if we are going to do this, let us do it quickly.

I have a statement I would like to put in the record.

The Chairman. Thank you.

Senator Moynihan. I yield the floor.

The Chairman. Are there others that would like to make a statement? If not, we can continue. Yes. Senator Dole.

OPENING STATEMENT OF THE HON. BOB DOLE, A U.S. SENATOR FROM KANSAS

Senator Dole. Mr. Chairman, I would concur with what has been stated by my colleague, Senator Packwood, the Ranking Republican on the committee.

This exercise reminds me of 1982, when Republicans had to get together in the back room and put together a package without any Democratic support because we were in the process of making some tax changes.

And, in that case, the bill finally was passed and signed by President Reagan, although he seemed to regret it the rest of his time in the White House, because Congress did not carry out on its promise to cut spending, and the taxes remained.

So, here we are in 1992 in a Presidential election year, where politics, certainly, are understood by the American people. I noticed a New York Times survey this morning said that even though they will take the tax cut, 60 percent say it is being proposed to get more votes for the Democrats.

We have had conferences and we have had meetings of Republicans on this side of the aisle, and it seems to me this is a preliminary bout. This is a warm-up for the main event.

And we have decided--I am not certain we are in total agreement with every Republican; I think we are in agreement on this committee--that we do not really enlighten the American public by playing games in the committee. They already understand that it is pure politics.

We will try to send a signal to the American people that we are ready to get down to serious business and not hold up this political document which raises taxes $57 billion and which does not create one job.

So, let us get on with it. Let us get it out of the committee. Let us get it onto the Senate floor. Let us work out some time agreement and get it out of here; get to conference; let the Democrats go to conference. There is no reason for us to go to conference; we have not been consulted up to now. Why would we be consulted in the conference?

And the bottom line is, as long as there are tax increases in this bill, it is going to be vetoed. And the veto is going to be sustained. And that is precisely what the Democrats want. They want the issue--the so-called class warfare, or fairness issue.

But if you ask most Americans, they are not going to distinguish. They know they are going to be next. They are concerned about the deficit. They understand a little tax cut may give somebody a little help, and, certainly, as the Chairman points out, it is a considerable amount of money.

But I would read a letter I got yesterday from a middle-class family in my state--just one paragraph. The letter is from Steven and Margaret Wolford. They are "tired about worthless lip service about how their hardships are of the utmost concern of our State and Federal Governments."

And they are especially sick and tired of the asinine partisan politics that, for all intents and purposes, paralyzes elected officials from doing anything about the crisis this nation faces. They are looking for jobs. They are looking for recovery. And they do not really see much gain in what we are going through here today, and I do not think there is much gain.

I do not think anybody doubts the President's veto can be sustained. He has said it over and over again. He is not going to change his mind, as someone indicated on Sunday.

He is going to veto the bill, and the veto is going to be sustained. And then the Democrats have what they want. They have the so-called fairness issue, but they all get to vote to raise taxes.

Everyone will get to vote to raise taxes, and they will get to explain to the people in their States why they voted to raise taxes.

And the people are going to fail to understand it is only the top seven-tenths-of-one-percent, though I note that members of Congress have been excluded from any tax increase.

So, we are going to have to explain to the people why we voted to raise taxes--those who vote to raise taxes. So, if this is the issue the Democrats want, we are prepared to cooperate to the extent to get it out of here and get on with the serious business of a growth package.

This is not a growth package. We have not had time to look at it. We only received it moments ago. But we have an outline of it, and it is not a growth package. It is not going to stimulate the economy. It is a tax cut bill for certain people, and I would just hope, in view of what Senator Packwood has said, that we can cooperate with the Majority Party.

We may offer some amendments on the floor to strike the tax rates; to have Social Security earnings tests; three-fifths vote to raise taxes-- little amendments like that that I think would be accepted. And then let the Democrats go to conference and bring back what they have wrought.

Senator Mitchell. Mr. Chairman.

The Chairman. I call on the Majority Leader, Senator Mitchell.

OPENING STATEMENT OF THE HON. GEORGE J. MITCHELL, A U.S. SENATOR FROM MAINE

Senator Mitchell. Mr. Chairman, I thank you and commend you for the diligent effort which you have made to present an economic growth and tax fairness program which I believe achieves those objectives.

Listening to the earlier comments brings to my mind a day eleven years ago when we sat before this committee and a Republican administration came before the committee and said that the way to achieve growth in America is to cut taxes.

And most of the members of this committee agreed with that, encouraged it, re-stated it, and voted for it. For a decade, we have heard Republican rhetoric that cutting taxes is good for the country.

Now, when Democrats propose to cut taxes, we are told, it is politics. I ask the rhetorical question, why is it good for the country when Republicans propose to cut taxes, but politics when Democrats propose to cut taxes?

Secondly, on the question of tax increases, the bill proposed by the Chairman will increase taxes on less-than-one-percent of all Americans; more than 99 percent of all Americans will be unaffected by the tax increase, and many of them will share in the tax reduction.

This is a modest effort to redress the unfairness of the tax policies of the 1980s. During the 1980s, pursuing Republican tax policy, taxes on those at the very top of the income scale were cut dramatically.

Taxes on middle-class Americans rose. This bill is an effort to partially--not completely; not nearly enough--redress that imbalance. Less than one percent of taxpayers will be affected by higher rates.

Finally, on the question of the deficit, I share the view expressed by several of the previous Senators, that the deficit is a concern. The President's package--the seven points proposed by the President--will increase the deficit by $27 billion.

It proposes to give things away for people without paying for them. It invents a new fiction in budget terminology not heretofore used, even by the creative budgeteers of the past decade, and that is to assign a current cash value to savings and receipts to be received in the future.

If we succumb to that temptation, the potential is unlimited for assigning current cash values to future receipts. And, yet, that is what the President's package--the package which we have been urged to adopt--will do: increase the deficit by $27 billion by creating incentives without paying for them.

The Chairman's mark, by contrast, directly confronts the problem of paying for that which is provided in the bill. It does so by an increase in rates that will affect less than one percent of all Americans.

I honestly do not comprehend how anyone can express concern for the deficit, and, at the same time, urge adoption of the President's seven-point program, which will increase the deficit by $27 billion. The two positions are logically and totally inconsistent.

I do share the view, Mr. Chairman, that we ought to move as expeditiously as possible, consistent with a thorough examination of the issues. I believe we should act; I believe we should act promptly, and I hope that we will be able to do so. I thank you, Mr. Chairman.

The Chairman. Thank you. Let me get a feel for how many members are going to want to speak, because if each of you wants to, we will not get to starting on the bill before we have to break up. But let me get a feel for how many. Hold up your hands, if you will.

(Pause)

The Chairman. We are going to be awhile. All right. Let me say one thing, in fairness to the Chairman. When we talk about divulging the deal and talking to staffers, I started these meetings Friday with Democrats and Republicans getting into the details of what we are talking about in this legislation.

In addition to that, we have had three sets of staff meetings with Democrats and Republicans in getting into it. And one other point, insofar as Senators themselves.

We have done a survey, and over 70 Senators will be directly affected if the Democratic provision prevails with the addition of additional taxes. That is the point. We will have to pay more taxes, and some of them will be pretty hard-hit. And that includes the Chairman.

(Laughter)

The Chairman. Now, let us see who is next. Senator Roth.

OPENING STATEMENT OF THE HON. WILLIAM V. ROTH, JR., A U.S. SENATOR FROM DELAWARE

Senator Roth. Thank you, Mr. Chairman. I shall not repeat much of what has already been said, but I do think that it is critically important to understand that time is of the essence.

It is a grave mistake for us to go through this political charade of legislation that we all know, and know full well, will never become law.

What that does is delay the recovery now, because young couples who are planning to buy new homes are not going to make that decision today, because they feel that perhaps they will get some tax break if they wait.

And the same is true of the businessmen: why invest now when you do not know what changes in the taxation are going to be made that, again, might give them a tax break?

So, every day we delay action in the real bill that is going to become law--and that is not going to occur until we go through this, as I say, political charade--is going to delay the recovery.

The American people are concerned, and they are concerned about one thing. They are not interested in class warfare; they want jobs, and they want growth. They want to know that their children are going to lead a better life than they. And they see this Congress playing politics rather than addressing the real problems.

And, frankly, I am surprised to hear the Majority talk about a tax increase at this time. A major increase was put through as part of the budget summit, and that is what helped cause the economic stagnation we are now suffering.

But we never learn. Everybody knows that if you increase taxes, that to get anything very substantial is going to be paid by the middle-class.

What we stood for in the early 1980s, in contrast to this economic, or, rather, class warfare, was a tax break for everybody. And that tax break ended up with the longest growth period, the creation of more jobs, and we ought to look back at that lesson.

But, Mr. Chairman, I urge that we forego this mark-up and try to work together in creating a growth package where the key sole criteria is, will this tax create jobs and growth? Thank you, Mr. Chairman.

The Chairman. Thank you. Let me see on the Democratic side now if we have anyone that wants to speak. Senator Boren.

OPENING STATEMENT OF THE HON. DAVID L. BOREN, A U.S. SENATOR FROM OKLAHOMA, CHAIRMAN OF THE SUBCOMMITTEE

Senator Boren. Mr. Chairman, first I want to compliment you for the effort that you have undertaken to bring us together and to come forward with a proposal that makes sense.

I am going to vote to report this package out of the committee because I believe, on balance, while it is far from a perfect bill, it improves the Tax Code as it now exists.

I think it improves it in a number of areas. First, it does bring greater fairness to the Tax Code, and, with all due respect to others that have spoken today--and I do not say this in the spirit of class warfare, but in the sense of uniting our people in common purpose--over the past decade, the real income of the top one percent and the top five percent in this country has escalated significantly, while all of us know that those who make up the middle-income group have shrunk in numbers. And we all know that the middle-income people of this country are the real glue that hold it together.

And so, there is benefit in trying to move toward tax fairness. There is some benefit also in this bill in trying to reduce the cost of capital to encourage saving and investment--capital gains changes; the AMT, the Minimum Tax changes here--so we can begin to compete with the rest of the world. There is only modest progress in this area.

I wish there were far more, because I think, more than anything else, the American people want us to act to encourage saving and investment, to create jobs for their children.

The American people are not selfish; they would far rather sacrifice now to have a job for their children in the future, than to have a small tax cut for themselves now.

And I do think that we are, to some degree, in this bill, underestimating the intelligence and the patriotism of the American people. So, I wish we would go much further in this direction.

We continue to have a Tax Code that causes us to take three times as long in this country for companies that invest in new equipment to recover the cost of their investment as it takes, say, in

Germany or in Japan. One of these days, we are going to be out of business in the world marketplace.

And we ought to stop talking down to the American people and understand that the American people know what we are talking about--they are willing to make those sacrifices--and do it.

So, I would like to see far more progress in this area of really looking ahead; not to this election, but looking ahead to the opportunities we give to the next generation. But there is small progress in this area.

What I suppose does sadden me the most about the process is to hear what we have already had demonstrated on the committee: a sharp difference along party lines. I think, more than anything else, the American people wanted us to get together--more than, perhaps, even the detail of this bill.

If we could just find a way to demonstrate to the American people that we could work together for the interests of our country instead of as Democrats or Republicans; instead of supporting one side or the other in the upcoming Presidential election.

I think we would show ourselves most worthy of this institution and most worthy trustees for the future of this country. We have not yet succeeded in that undertaking, and I think that is tragic, and it is disappointing to this Senator.

I do not lay the blame on any individual. I know our Chairman, and I know our Chairman is not a person who is a partisan person. He tries to bring us together.

We have not yet succeeded, obviously, as we have heard the opening comments here today. I hope we will continue to try to work together, even as this bill goes to the floor.

As I say, I believe it should go to the floor because it is some improvement over the current tax law; both in terms of fairness and in terms of encouraging saving and investment for our future. I think we could do better.

I know one thing the American people want us to do: they want us to keep trying to find a way that we have common ground so that we can work together and serve the interests of all.

If there were ever a time, as we look toward the next generation and we look toward the challenges of the next century, when we need to think as Americans rather than as Democrats and Republicans, it is now.

So, while I am going to support this package, I will continue to work in every way that I can with the leadership on both sides in this committee, and the leadership on both sides in the Senate, to see if there is a way, before we come to a final vote on the floor, to bring us together.

And then, if we can come together, to go to the President and to challenge him to also set aside election-year politics and join us in a common effort. I express the hope that that is still possible.

Again, I compliment the Chairman for his leadership; for his effort to try to reach common understanding; for his continued efforts in that direction.

I am encouraging him to continue along those lines. I compliment him for the improvements that we have made, especially in the saving and investment area, in this bill.

The Chairman. Thank you very much, Senator. Senator Danforth.

OPENING STATEMENT OF THE HON. JOHN C. DANFORTH, A U.S. SENATOR FROM MISSOURI

Senator Danforth. Mr. Chairman, I would like to emphasize areas where I think that there is a strong bipartisan sentiment on the committee.

First of all, as the letter read by Senator Packwood states very clearly, there is, on both sides of this committee, Republicans and Democrats, a very strong respect for you as our Chairman.

We have been blessed on this committee since the time I have been on it with outstanding Chairmen--Senator Long, Senator Dole, and now, you, Mr. Chairman. And Senator Packwood, of course.

(Laughter)

Senator Danforth. And, yes, even Senator Packwood.

(Laughter)

Senator Danforth. And I am certain that all Republicans share that view. Secondly, as was stated by one of our members in our closed meeting last week, there is enormous pride in the Senate

Finance Committee. This is an outstanding committee. It contains some of the most able members of the United States Senate. People are very serious about the work of the committee. They attend to the business of the committee.

And I think that there is a tremendous sense that we have been able to work together in the past on many, many things. And the times when we have divided on a partisan basis have been relatively few, compared to other committees.

And the times when we have been able to get together, regardless of party identity, have been very, very numerous.

The third thing is, I guess, more debatable, although I sense a very strong bipartisan agreement on this as well, with, I am sure, some dissent.

And that is a fundamental disbelief in the wisdom and in the efficacy of a so-called middle-class tax cut. Not to say that people would not gladly take $200 or $300 at the end of the year; not to say that it might have some marginal effect with respect to fairness.

But, when people are worried about the economy of the country, and when they are worried about the future of America, I have not found anybody who really believes in a so-called middle-class tax cut. I have not found any constituents; I have not found any economists.

And, while some people in the Senate have expressed belief in it, I think that in the heart-of-hearts of many of us, Republicans and Democrats on this committee and in the Senate, most people believe that the so-called middle-class tax cut does not get us anywhere with respect to rebuilding our economy.

And the middle-class tax cut has been part of the President's program, as well as part of the Rostenkowski program, and part of the Bentsen program.

It is more than half, in fact, of the proposal that you have unveiled, Mr. Chairman. And I do not think very many people really believe in it.

Fourth, I am convinced that there is a basis of consensus in the committee to pass tax legislation this year. Certainly on at least some items where there would be virtually universal agreement--extenders; doing something serious about the luxury tax--repealing it; the health care proposals that you have come forward with--there is a lot that we could do, and I think we could do it in very short order.

Fifth, and finally--and, I think, more important than anything else--I think that there is, on a bipartisan basis, an increasing sense that there is something seriously wrong with the present state of our tax laws in America.

We are the only industrialized country, I believe, that does not have some sort of consumption tax.

Our savings rate in the United States is the lowest of the industrialized world; our investment rate is the lowest in the industrialized world; our growth rate is the second-lowest in the industrialized world.

We have a tax code that encourages consumption; it discourages savings and investment; and, I believe that in the very near future--maybe this year; certainly next year--we should proceed in the Senate Finance Committee to move toward a major change in our Tax Code in the direction of encouraging savings and investment and discouraging consumption.

The Chairman. Senator Baucus.

OPENING STATEMENT OF THE HON. MAX BAUCUS, A U.S. SENATOR FROM MONTANA

Senator Baucus. Thank you, Mr. Chairman. Mr. Chairman, essentially, after we have had our opening partisan shots, I think that, based upon the comments of the Senator from Missouri and comments of others here, it is becoming more clear that, while not perfect, your bill is about as good a bill as we can have, given the current circumstances.

The problem, obviously, is that we have a very large budget deficit. There is not a lot that we can do if we want to lower taxes, to provide incentives to help stimulate certain aspects to the economy, we have to pay for it. It is that simple.

This is an honest bill. There are no gimmicks in this bill. It is a pay-as-you-go bill. I think the American people want a pay-as-you-go bill.

Nevertheless, we do take a step toward addressing some of the points I think the Senator from Missouri was getting at, as well as the

Senator from Oklahoma: namely, our country has to begin to work with the Code to help stimulate more savings, more growth, more investment, more productivity, so there are more better-paying jobs in America than there now are.

It is very hard to do that at this point. We are hemmed in. There is not a lot we can do today, this year. Nevertheless, this bill does have incentives.

There's a capital gains provision: it is modest, but it tends to go in the right direction; its IRA provisions, I think is in your bill, goes in the right direction; there are some education provisions; extension of R&D tax credit.

These are steps, albeit, not major steps, nevertheless, steps in the direction in which I think most members of this committee want to go.

Second, as has been stated, there is another issue: it is fairness. I think most Americans believe that the tax policies in the 1980s were unfair, insofar as they lowered taxes for the most wealthy and increased taxes for virtually everyone else.

This is a good faith effort to address the issue of fairness to try to make our Tax Code a little bit more fair.

And, finally, I urge us to just get on with it; to do the best we can, given these present circumstances. I agree with the Senator from Missouri: I would like to begin to work on changes in the Code that move us more toward consumption taxes.

I think that makes more sense for the future, so long as they are properly designed and not regressive, and so forth. I think we can do that, and should do that.

But I do not think we are able to this year. I mean, to be honest with you, there is one player here in this whole process who is not with us here today, and that is the President.

The President, so far, has given no indication that he wants to pursue down the road that many of us want to go. I mean, he has made this a very partisan, very political issue already.

Now, if the President is willing to change, and if he is willing to undertaken some of the efforts that we are now talking about, then I think that, perhaps the efforts that the minority wants can be undertaken also in a bipartisan way by the Majority side, as well.

But, in our divided form of government--our constitutional form of government--it is not just the United States Senate Finance Committee; it is not just the United States Senate; it is not just the Ways and Means Committee; it is not just the Congress--that is only a small part of it. The other side is the President.

And if the President wants to do what the Minority say should be done, then I believe that we will accomplish the results that the Minority would like us to pursue.

The Chairman. Thank you. Senator Chafee.

OPENING STATEMENT OF THE HON. JOHN H. CHAFEE, A U.S. SENATOR FROM RHODE ISLAND

Senator Chafee. Thank you, Mr. Chairman. Mr. Chairman, when we look at your bill, it increases taxes in five years by $57 billion.

And of that $57 billion, over half of it--$31.5 billion--goes toward this tax credit--this $300 tax credit--for a very limited group of children. You have limited it by age, and you have limited it by income category.

Now, that $300 tax credit per year works out to 84 cents per child, per day. And, Mr. Chairman, I really do not think that is going to get our country stimulated. I do not think that is going to improve job opportunities. It is not going to do anything for the nation, as a whole.

Now, I, for one, do not get excited by tax increases, and I think most who have sat on this committee know that. But I do become deeply disturbed when we take a substantial amount of money in new taxes--$57 billion over five years--and pay no heed whatsoever to addressing the number one problem that is overhanging our economy, and that is the deficits. Not a nickel of this goes for the deficit.

Now, Mr. Chairman, as you know, in the hearings in connection with the efforts to stimulate our economy, we had witness after witness come before us.

And the gist of the testimony, if you needed to summarize it, is two-fold, I think. First, there is not much that we can do here that is going to drastically change the economy.

But the second point that they hammered at is that this recession is different because of these overhanging deficits.

And if we really wanted to do something about this economy and the future of this nation in every respect, whether you are talking interest rates or investment, it is to do something about the deficit.

And, as I say, the tragedy of this legislation is that of the $57 billion, none of it goes to the principal problem facing the country, and that is the major flaw. And, that, Mr. Chairman, is why I am against your bill.

Now, what about, what can we do? Well, we can get together and we can address some of these problems.

It seems to me there ought to be three things we ought to be trying to do: do something about jobs; do something about stimulating real estate; and do something, if we can, about health care.

And we can do something on each of these levels. The health care you have touched on, but we can do more. We can do something about jobs; the R&D tax credit; the repeal of the luxury tax; some capital gains relief; something about the ITC, or some form of it.

And, in real estate, we certainly ought to do something about the extenders on the mortgage revenue bonds; the low-income housing tax credit; and the passive loss rules. Something in each of these areas.

But, Mr. Chairman, I think we are making a great mistake to take $57 billion out of the economy and do nothing whatsoever about addressing the deficit. Thank you.

The Chairman. Thank you. On the Democratic side, let me see who else would like to speak. Senator Riegle.

OPENING STATEMENT OF THE HON. DONALD W. RIEGLE, JR., A U.S. SENATOR FROM MICHIGAN

Senator Riegle. Thank you, Mr. Chairman. And let me say that I think you have given us a wise, and balanced, and fair plan. I want to make reference to a poll today in the New York Times, done by New York Times and CBS News.

The Senator from Missouri said he has not been able to find anybody that he has spoken to that is interested in a tax cut for the middle-class.

This poll published today by two leading news organization, conducted a nationwide poll, and they found that 68 percent of the people of the country favor a $400-a-year tax cut for middle-income families.

And it indicates that, even in the Senator's own party, that 73 percent of the people polled here so indicate. In another area of the poll they are asked whether the $400-per-couple tax cut would help the economy, and the majority of the people responding said they thought it would.

Now, you have obviously had a different

experience. I find, in talking with middle-income people--and I have talked with a great number of them--who are trying to pay tuition payments, or house payments, or car payments, they feel that they got left out of the tax cuts in the 1980s, and they did.

The tax cuts in the 1980s went to wealthy people. And wealthy people have done very well; have gotten huge tax cuts, in many cases, in the amounts of tens of thousands of dollars.

And now they do not want to give any of it back in the name of fairness. They do not want to give one thin dime to the middle-class, most of which saw their taxes go up in the 1980s.

And it was in the name of a different economic theory. It was Reaganomics: trickle down, give the big tax cuts to the wealthy, and you would have a huge renaissance in the country and great economic performance, and lots of jobs. It turns out it was a fraud, and it did not work.

And we have got 16 million people in the country today needing and wanting full-time work and not able to find it. And every poll that is taken in America today says that the American people want to change course. They do not want to pursue that course any longer. One, because it is unfair; and, two, because it did not work.

Now, what the Chairman has put together here is a plan that does change course. It maps out a new economic path for America and it lays out ways in which to stimulate savings and investment, to create jobs, and it also provides, finally, some fairness in the Tax Code.

Now, I realize that the people that got the big tax breaks have enjoyed them, and they do not want to give them back. They frankly do not want to give them back, and perhaps that is understandable.

It is time they gave some of it back. They got too much. And it is unfair, and it has hurt the country. It has not helped the country. Piling all that money up at the top of the income scale has not helped America, it has hurt America.

And, so, when I hear people in the administration and elsewhere who are very removed and distant from this problem, and to talk about how folks in the middle do not want it and do not need it--folks in the middle do want it, they do need it, and they need it now.

I was out in my hometown of Flint yesterday.

One of the GM plant closing announcements, 4,000 jobs in an engine plant in Flint, Michigan. The average seniority of workers in that plant: 27 years.

These are the most skilled workers in our country. They have given their life to these jobs. The plant is closing, and there is no alternative for them. And that is going on in 50 States, not just in my State.

Now, we need a tax plan passed here that is going to provide jobs in America. And the people of the country are saying, change course. And we need to change course.

And if the administration and the people around the administration do not understand it, then they are not going to be around after November. That is also what the polling numbers are saying.

So, let us pass a plan out of here that does this. The Chairman has given us a plan like that, and I thank you for putting forward a plan that changes direction.

The country needs to change direction. We need tax fairness for a change, and we need to create jobs in America. And our people are desperate for the help. Maybe the people at the top of our government are not needing the help, but most of the rest of the country needs the help, and they need the help now. And this will help. Thank you, Mr. Chairman.

The Chairman. Thank you, Senator. Senator Durenberger.

OPENING STATEMENT OF THE HON. DAVE DURENBERGER, A U.S. SENATOR FROM MINNESOTA

Senator Durenberger. Mr. Chairman, let me begin by thanking you for your generous comments about bipartisanship, particularly in the area of health care reform.

And I will say I have very much appreciated working with you on the design and the implementation of small group insurance reform.

My remarks this morning will be addressed to the tax portion of this bill, because I believe what we have here, and heard it illustrated this morning, I guess, is politics, taxes, and budget policy bringing out the absolute worst in each other.

I want to say from my colleague from Michigan, if he reads all of this New York Times poll this morning, yes, people favor or will accept the $400-a-year middle-income tax cut for families, but read the next question in this poll where they are asked, "Why do you think the Congressional Democrats have made this proposal for the tax cut?" And 60 percent of the people say it is for them to get more votes. But you can say the same thing about our side, I suppose, but that is the reality. People out there believe these cuts are being made by and for politicians.

People in Minnesota have come to believe, over the last six or seven weeks, that everybody seems to come to this table with kind of an old grudge to settle, including the President.

We have heard about the fairness debates of the 1980s, the 1990 budget debacle, the so-called Pennsylvania message of last year, and on, and on.

It appears that we have all allowed what is politically urgent to obscure what is economically important. It seems to me, Mr. Chairman, that the first responsibility of leadership is to define reality.

And reality in 1992 is that we need to lower the deficit and we need to raise people's confidence that somebody here is in charge of their future. And the process we are engaged in is almost certain to do the opposite, on both counts.

My colleague from Montana said that there are not any gimmicks in this bill, and I am instructed, as a Republican, to agree with him.

But, Mr. Chairman, I do not think we need economic lollipops like 84-cent-a-day tax cuts for the middle class. We do not need big tax breaks for people who build homes, but not for those who buy or rent.

We definitely do not need quick-fix investment incentives financed with debt. And I agree with what the Majority Leader said about these PBGC savings.

Every economist that we have listened to has told us that that is really giving with one hand and taking away with the other. And it seems to me the last thing we need in these uncertain times in our country is the classic display of the same old Washington stuff; that is noisy, expensive futility.

Too much politics and too little discipline got us to where we are today: a $1 billion-a-day increase in the Federal deficit.

How about these for national priorities, gentlemen: we spend $10 on interest for every one we spend on education; we spend more to service the national debt today than we did to run the whole government in 1974.

The reality is, we need a new way to decide how to spend money, or not spend money in this government; and we need a new way to decide where to raise the money we need to run it.

But I doubt we are going to find those new ways or the character to enact them here, or anywhere this year. So, if we cannot do any good, at least let us resolve not to do any major harm.

I asked myself, as many have asked me in my State of Minnesota, what good can we do for the economy and for the American people?

And I will say to my colleagues that we have in this package two very helpful steps to solve the problems that people in Minnesota tell me they really care about.

And the first is to begin the process of comprehensive health care reform. Adopt the small group health insurance reforms that are urgently needed and included in the Chairman's package. It is the best substantive thing we can get done this year to improve American health care.

There are some who think that the Majority in the Congress is determined to put a mandated, universal coverage bill to a vote this year, instead of the bipartisan beginning of reform, which the Chairman has proposed in this bill.

And I would say to them, there is too much at stake here to pull the political stake out of the heart of the tax bill and ram it into the heart of health policy reform. So, I say to my colleagues, please do not do that.

Secondly, we should adopt the education financing proposals which are included in the Chairman's package, and which have not been referred to yet.

Senator Bradley, Senator Simon, and I have worked hard to find a way to ease the burden of higher education on American families, and we think we have found it. The idea self-reliance proposal is in this bill. It has bipartisan support, and we can do it this year.

Then I think we should spend the remainder of the year holding hearings to re-examine the nation's entire approach to taxation.

And after the political moment has passed in November, we can return in January and mark-up tax legislation that lays out a path to the future of this country: not a tax bill for the short-term, but a Tax Code that will set the country on a path toward long-term investment, growth, and jobs.

The best thing that I can do for this

economy, for the future of the people in Minnesota, is to vote, no, on all the big tax bills.

And I urge my colleagues and the administration to open their eyes, lay down their swords, and decide to limit the damage and do the good we can.

The Chairman. Thank you. On the Democratic side, do I have others who would like to comment? Senator Daschle.

OPENING STATEMENT OF THE HON. TOM DASCHLE, A U.S. SENATOR FROM SOUTH DAKOTA

Senator Daschle. Mr. Chairman, I will be very brief. I commend you for your leadership, as so many others have, for good reason. I think you have done yeoman's work in trying to bring about the compromise and bringing about the kind of package that we all can support.

As I listen to all of the opening remarks, there appears so much that we all are in agreement upon. I am convinced that each one of us is here this morning convinced we are doing the right thing.

I do not think that anyone ought to question another's motives, frankly. The fact is that I honestly believe we are doing the right thing. I think each one of the Republican members here this morning believe they are doing the right thing.

We are at an impasse on what the right thing is. But I do not think anyone ought to question whether or not, in our heart-of-hearts, we believe we are doing the right thing.

The fact is, that if the President's proposal is any guide, 80 percent of what we are suggesting this morning is something that Republicans and Democrats agree upon.

The Chairman made a very good point about the fact that we have gone to great lengths in trying to accommodate many of the proposals made by the administration itself. I support many of them; I oppose some of them.

But, nonetheless, in the interest of trying to accommodate the needs of this country and move ahead, I believe that incorporation of all of those principles was meritorious and ought to be supported.

There appears to be two fundamental points of disagreement. One relates to how we pay for this package, and whether it ought to be paid for.

I am very concerned about whether the Republican proposal--proposed in good faith, I am sure--actually brings us the kind of revenue that is going to be required to pay for all of the things that they claim it will pay for. I know, with every good intention, they suggest that it does; I frankly disagree.

The other point has to do with whether or not this is the time to begin to restore fairness. I think we went too far in the 1980s in bringing about the burden on the middle-class that we have heard so much about.

This will not resolve that matter, but I think a down payment in restoring some fairness is essential if we are going to open up the Tax Code at all. That is what this bill does, is to begin to restore fairness.

I think the most important thing, however, is what economists tell us again and again, that, if, indeed, we are going to bring about long-term economic growth, we are not going to find it in the Tax Code.

The Tax Code, in and of itself, is incapable of delivering the kind of economic growth we need. All we can do is to begin that process here.

The more important process, through investment, can be done in the appropriations process; can be done with an investment in infrastructure; an investment in the future and our young people; investment in various ways to bring about the kind of economic vitality that we all want.

So, really, we are only making a first step--a down payment, really--to that long-term commitment to two ideals that I believe are very important. The first is fairness, and the second is investment.

Our commitment to investment must be far more significant and far more apparent in the appropriations process than it is in this bill.

But, I end the way I began, in commending the Chairman, and hoping that, in the best interests of all those concerned, we can reach some accommodation and ultimately get this country moving again. I thank you.

The Chairman. I thank the Senator. Senator Symms.

OPENING STATEMENT OF THE HON. STEVE SYMMS, A U.S. SENATOR FROM IDAHO

Senator Symms. Mr. Chairman, I would like first to ask unanimous consent to submit two statements for the record, and I will be very brief, because --

The Chairman. Without objection, that will be done.

Senator Symms. -- I see the hour is late. But I do think that some of the things that my colleagues have said on the other side of the aisle simply have to have a response. They cannot go unanswered, or it is as though we accept them.

The distinguished Majority Leader mentioned the rhetorical question of, what is different about the 1981 tax bill and this bill?

I would simply say that the tax changes we made in the early 1980s would be considered, compared to this bill, a well-balanced, healthy, nutritious meal, compared to a meal of Twinkies. And there is a big difference.

People seem to forget that during the 1980s we created almost 20 million new jobs, and, notwithstanding, many of my colleagues on the other side of the aisle like to say they were all McDonald's. The record does not show that. There are a lot of good jobs; $50,000 and up paying jobs that have been created, and a lot of growth took place for a long, sustained period.

The other factor that I think we need to make is that after the 1986 Tax Reform Act, six million low-income Americans were taken off of the tax rolls. Six million low-income Americans were taken off the tax rolls. They do not pay any taxes now.

And now, if you go analyze who is paying the taxes, the top 20 percent of earners in the United States are paying 70 percent of all the Federal tax payments. So, who is kidding who?

If I believe, as Ranking Member Packwood said, that somehow we could raise taxes and reduce the deficit, that would be one thing.

The record clearly shows that every time that taxes are increased, the Federal Government spends $1.59 for every dollar that is increased. That is the record. What does it take for us to learn our lesson? I would ask my rhetorical question: why do we not simply freeze Federal spending? We have cut defense spending already.

Why do we not freeze Federal spending, and then we would have some money that we could use for the kind of tax cuts that various members of this committee think would be good for growth, and good for equity and fairness in the Tax Code?

I think that the people outside of Washington, D.C. could understand that very well, if we would freeze spending, show the savings, and then use that in a tax bill. I suppose that makes too much sense.

But, Mr. Chairman, I would have to say that if we continue down the path to raise taxes, somehow to think that we are going to improve things, it is just simply like a drunk trying to drink himself sober; it does not work.

It has not worked in the past, and it is not going to work today. So, I will not be voting for this package. I am sorry about it.

I will not be back on this committee next year, but I do have some personal amendments for constituents of mine that I think are good policy amendments that I want to offer.

I hope there is a package before the year is over that we will be able to go back to a bipartisan understanding on this committee.

And I just throw one idea out there, but I do have an amendment that deals with transportation. We wanted to have it in the transportation bill. It is good for jobs; it is good for transportation; it is good policy, and it is good for one of my constituents, and that means it is good for America.

(Laughter)

Senator Symms. So, I am not going to offer that amendment and have any chance that in this partisan rancor here in this room today that it gets voted down, because it is too good for the country.

The Chairman. Thank you very much, Senator Symms. Let me see. On the Democratic side, Senator Bradley.

OPENING STATEMENT OF THE HON. BILL BRADLEY, A U.S. SENATOR FROM NEW JERSEY

Senator Bradley. Mr. Chairman, I was not going to speak, but Senator Symms' candor jogged me into deciding to speak.

I am a little dismayed by the process we are going to go through, because I do not think that, in the Finance Committee, it is best. I do agree with the previous speakers who have said that when we have done things well, we have done things together.

But here we are. I mean, my personal view is we are in the middle of three economic phenomena in the country. We are in a cyclical recession that I frankly think, given the expansion of the monetary base, is going to be looking better in another six months.

I think the last thing we need to do is to put a lot of tax benefits for special interest in the Code under the assumption that that is going to help us out of a cyclical recession. I think we are already headed out of it.

We are in the middle of structural

adjustment, international competition, and, too, the end of the Cold War. Those do not require investment incentives, those require investments in education, health, and pension security. Those are things we should be doing.

And, third, we are continuing down the path of a fiscal binge with deficits continuing to go higher and higher. We live in Never-Never Land. We have a lot of talk about savings and investment.

If you really want to improve savings in the country, the most efficient, effective, and quickest way you can do that is to reduce the deficit, and it is beyond me to believe that you will be able to do that by either just cutting spending, or just increasing taxes.

Sooner or later we are going to have to do both, or we are going to give our kids something that they can never overcome.

So, that brings us to this bill. I tend to agree with the sentiment in the committee that we will pass it out of the committee.

We will probably make some moves and efforts, as always happens in the Finance Committee, but it will probably pass out. It might be changed on the floor; it might not. The President will veto it, and then we will be back here.

And I would hope that we could focus on a second bill that would begin to redress some of the issues that are raised on the Democratic side about the inequities of the 1980s. A millionaire surtax is really not too much to ask.

And I would hope that we would use that money to address the problems of education, health, and pension security.

Lt the recession take care of itself with monetary policy, and then come back after yet another election--this is the third election that I have heard we cannot do anything about the deficit because there is an election coming up, so hope springs eternal--and get serious about doing something about the real issue that confronts us all, which is the size of the deficit.

The Chairman. Thank you. Senator Grassley.

OPENING STATEMENT OF THE HON. CHARLES E. GRASSLEY, A U.S. SENATOR FROM IOWA

Senator Grassley. Mr. Chairman, I commend you for bringing a bill forward that has a number of very good provisions in it. Just like everybody else, there are some good provisions in this bill, and things we do not like; things that are good for the taxpayers, and things that are good for the country.

You have included in your mark some proposals that I have been working on for a very long time. Since 1987, I have been introducing legislation to restore the interest deductibility of student loans.

Finally, this year, along with Senator Boren, we introduced legislation that would allow either a credit or a deduction for that interest paid on student loans.

So, I am very encouraged and happy that you, Mr. Chairman, have agreed to include this pro-education, pro-growth legislation in your mark. In addition, long ago, I introduced initiatives for middle-class tax cuts, as well as the extension of first-time farmer bonds.

I have also been working with Senator Pryor in pushing a second Taxpayer Bill of Rights. These are all very positive additions that you have included in your mark.

So, the problem that I am facing today, and the problem that a lot of people are facing, is whether we are going to agree to a major tax increase. We should have learned that great tax increases in the past, and particularly the most recent one of 1990, exacerbate recessions.

Some even think that it was a contributing factor to the recession that we are in. Increasing taxes now will only further the economic downturn.

Some cynics might say that what some politicians want to do, do it in order to make political gains in November. I can only hope that the cynics are wrong.

Mr. Chairman, I think the thing that bothers me most about the whole discussion of increasing taxes--and I guess I would say to those who want to raise rates--I just wish you could tell me, maybe tell the American people, how high taxes must be raised to satisfy people who want to raise taxes. How high is high enough?

If I knew what the level might be, and that it would not cause taxes to be raised yet higher in the future; and if the increased revenue were going to be earmarked to reduce the deficit, I might be one on this side of the aisle encouraged to vote for it.

But my guess is that the money will be spent like it was spent in 1990, and still not satisfy our appetites to spend money.

I guess I just simply believe you cannot raise taxes high enough to satisfy the appetite of us here in the Congress of the United States to spend money. You just cannot raise them high enough.

So, budget deficits keep getting bigger if we raise taxes. Tax increases do not reduce deficits, but they simply are a license for us to have a higher level of expenditure.

One last comment, and a little more general than just this bill, at least once this morning, and maybe more often, I have heard people say that, on this issue of taxes--and I have heard it on other issues in recent months--the President is not at the table, or the President does not have his program up here for us to consider.

It seems to me like we, as an institution, have become an institution that only reacts; that we are not an acting institution; that we are not a leading institution.

Now, we are all very mature adults here, elected to a co-equal branch of government, with our own constitutional powers, and with our own constitutional responsibilities.

We should exercise our constitutional powers and we should not sit around wringing our hands like the nervous Nellies we tend to be, waiting for the President to act first; waiting for the President to send a program up here.

We should do what we were elected to do, and do it when we want to do it--not when the President wants us to do it, or waiting for him to act first.

In other words, I believe that we are elected to lead, and that we should lead.

The Chairman. Thank you, Senator. On the Democratic side. Senator Breaux.

OPENING STATEMENT OF THE HON. JOHN BREAUX, A U.S. SENATOR FROM LOUISIANA

Senator Breaux. Thank you, Mr. Chairman. I would like to also commend you for the truly tireless effort that you have made in trying to put together this package; the long hours and the weekends that we worked in trying, along with the staff, to put together a package that we could all begin the dialogue, and hopefully the ultimate product, which we began today.

You know, there are hundreds of thousands of people lining the streets in New Orleans today reaching their hands out to masked men riding floats saying, "Throw me something, Mister."

Well, I think the American people, in general, are not asking that Congress throw them anything, but, rather, that we do something, and do something about two of the main problems that I think most Americans feel that we are facing.

One is jobs and economic growth, certainly; and, I think secondly, tax fairness is high on their list of what we should be addressing.

Tax fairness, if we look at what has happened in the decade of the 1980s, it is not a pretty picture for people who are struggling in America.

The statistics are in, and the graphs and the charts have been drawn. And if you look at those statistics, and those graphs, and charts, you will find that, for middle-income families in America during the 1980s, that the things that were bad went up, and the things that were good for them went down.

And we ought to look at this bill as a means to try and address those inequities. As a quick example: real after-tax income--what people have to spend after taxes.

If you look at what happened in the 1980s with middle-income families, the real after-tax income in 1992 is less than it was in 1980, while, for the top one percent of the families in America, their real after-tax income more than doubled between 1980 and 1992. Average increase: $243,400 a year for people in the top one percent.

The second statistic: the tax cuts that we passed in the 1980s, CBO tells us that those changes had the effect of cutting the Federal taxes on the top one percent by approximately an average of $42,300 apiece; while, for those middle-income families, we raised their taxes because of the tax policies of the 1980s, by an average of $436 apiece.

And, finally, if you look at the total tax burdens on families in this country in the 1980s, the total Federal tax rate or burden on middle-income families is higher in 1992 than it was in 1980; while, for the top one percent of the families in America, their total tax burden decreased by 7.5 percent.

Something happened in the 1980s, I would say to my colleagues, and tax fairness is needed in order to correct it. Now, I am really tired of people saying a $300 tax cut to families in the middle-income range is not going to mean anything.

Some of my Democratic colleagues hold up a dollar bill and say, this is not going to bring about economic growth.

But if you look at what it does for a typical middle-income family of $35,000 with two children--and folks, there are a lot of them out there in that category--for them, that is a $600-a-year tax credit at the end of the year, off the bottom line of taxes owed. And CBO tells us that middle-income typical family making $35,000, for them, that is a 25 percent tax cut.

It is not just a dollar they have been waving, that is a 25 percent tax cut on their taxes that they owe to Washington at the end of the year that they will see and put in their pocket. That is significant, and that is real, and it addresses the question of tax fairness.

Finally, on the question of jobs and economic growth, which this package should have, I think it does. I think the Chairman, in putting seven of the tax incentives that President Bush requested, is doing something about jobs and economic growth.

It is what the President asked us to do, and it is in this package. There is a capital gains tax reduction in this bill. It is not as much as I would have liked, but it is progressive, and it is significant, and it is going to unleash frozen capital in this country in order to create new businesses and new jobs.

And, finally, we have a youth skill training program which I think is going to help our workers be more competitive and produce a better product and be more productive, because we have to remember that over half of the kids in high schools never go to college.

This bill, for the first time, puts some real funds in the programming to create youth apprenticeship programs for those youngsters who never go to college so that they can be more productive and more competitive.

The bill addresses the two main concerns: tax fairness, and jobs and economic growth; and I commend the Chairman for putting the package together.

The Chairman. Thank you, Senator. Senator Hatch.

OPENING STATEMENT OF THE HON. ORRIN G. HATCH, A U.S. SENATOR FROM UTAH

Senator Hatch. Thank you, Mr. Chairman. I am fast coming to the conclusion that the best thing Congress could do for the economy and the country is to wrap up shop and go home for a year. I really believe that there are no answers here today.

I do appreciate the Chairman putting seven of the President's approaches into this bill. But, just to correct a few things, I tend to look at it as the percentage of how much people pay into the income tax program in this country.

According to the Congressional Budget Office, the top one percent, in 1980, paid 18.2 percent of the total Federal income taxes. In 1990, the top one percent is paying a total of 25.4 percent. That is up 40 percent.

The top five percent in 1980 paid 36 percent of the total income taxes paid, and in 1990, 44.1 percent. That is up 23 percent.

The top ten percent was 48.8 percent in 1980; now it is up to 56.1 percent of the total income taxes paid in this country. That is up 15 percent.

And the top 20 percent paid 60 percent of all income taxes paid in 1980. Now they are up to 72 percent in 1990.

If you really look at it, the top 50 percent of wage earners in this country are paying 95 percent of all of the income taxes paid into this country.

And why is the middle-class hit so hard? Well, I will tell you why, because we have increased Social Security taxes so high that they are getting killed with Social Security payments.

And that is going to go up, and up, and up, from here on it, it looks like to me, as we get down to two persons paying into the Social Security system for everybody on Social Security. And part of that is our fault, because we are unwilling to really look at the spending processes of this government.

Think about another thing: since the second World War, for every dollar increase in taxes, we wonderful members in Congress spent $1.59. Now, that is since the second World War, averaging all of those 45 years together.

If you add since the late 1980s and 1990, we are talking about \$1.70 and \$1.90. For every dollar increase in taxes, we spend \$1.70 to \$1.90. Now, that is ridiculous. You wonder why some of us do not support tax increases? Because we know it just fuels the spending practices of Congress.

Now, I come from the Labor Committee, and I have to tell you that I know people on the Labor Committee who, alone, could spend another \$300 billion in new spending programs this year; maybe \$1 trillion, if they had a chance and if the monies were there.

Look at the bottom part of it. The bottom 60 percent, in 1980, only paid 13.8 percent of all income taxes paid. That is now down to 11 percent. That is 20 percent down.

The bottom 40 percent of all taxpayers paid 3.6 percent in 1980. That is now down to 2.4 percent of the total taxes paid in. That is down 33 percent. And the bottom 20 percent, of course, they paid -0.2, now it is -0.5, down 150 percent.

Now, look, I do not think any of us, if we thought we could pay off the deficit and start paying down the national debt; if we knew that every penny would go to pay off those things, I think all of us would consider all kinds of innovative things.

The problem is, our record is dismal; it is pathetic. And here we are, going to increase taxes again, albeit on the little less than one percent. The little less than one percent changes dramatically. They are paying a hefty share of the taxes now.

Every time we increases taxes we add disincentives to our economy, and, in the process, what do we do? We have a lot of short-term things to dislocate the economy out of every tax bill that we come up with. It does not take any brains to figure out that what we are doing to this country is really pathetic.

And I know that the Chairman is having a rough time with this, and it is going to be a straight-down-the-middle partisan vote, and there is good reason for it: we have not worked together to try and put something together that will work.

And, frankly, I am sure that nobody on the Majority side is trying to give an 84-cent-a-day tax cut for political reasons. They are not trying to buy votes with that, are they? I mean, they surely would not do that.

And, secondly, I have got to say, you know, if you add it all up, why can we not get together and do some long-term things that will make a lot of difference, give some stability to our economy, and, in the end, get the economy back on its feet?

There is nothing this country cannot do if we will give it a chance. But every time we play around with taxes we dislocate whole sections of the economy, and that is generally increasing taxes rather than, of course, cutting them for everybody across the board.

Now, if you look at what really happened for 1982 to 1987, the number of black-owned firms increased by nearly 38 percent. Hispanic businesses increased by 81 percent. That is during the Reagan years.

Once Reagan's policies took hold, inflation-adjusted median household income for Black Americans jumped by 16.5 percent between 1982 and 1989, after declining 10.2 percent during the Carter years.

Well, I could go on and on. The fact is that women got significant benefits. The poor--the fact that the poor suffered under Reagan, that is false, too. The average inflation-adjusted income of the bottom 20 percent of families rose 11.9 percent. You can go on and on. You can make anything sound good, I suppose, but I am concerned about it.

The Chairman. Thank you, Senator. Are there those on the Democratic side? Senator Pryor.

OPENING STATEMENT OF THE HON. DAVID PRYOR, A U.S. SENATOR FROM ARKANSAS

Senator Pryor. Mr. Chairman, I want to take two minutes. Mr. Chairman and colleagues, I think it was about 60 years ago that Huey P. Long, of Louisiana, was elected to the United States Senate.

It took him a year to come to the Senate and take his seat because he was under indictment by the Grand Jury in Louisiana, so he was afraid to leave. But he ultimately came, and on his first day in the Senate, he offered a proposal to redistribute the wealth. Well, that was 60 years ago.

Well, today, here we are, and we are not redistributing the wealth. But what Chairman Bentsen has done is an attempt--and it may be a first attempt, but I think a very sound attempt--to redistribute the burden; to redistribute the responsibility of making this country function.

For the past decade, that burden has basically fallen on the middle class. This is what the Chairman's bill is addressing, and this is what it is about.

My friend, Senator Chafee, a few moments ago talked about doing something about the deficit. Let us lower the deficit. I think all of us would agree; let us do something about the deficit.

But, in all due respect, the thing not to do about decreasing the deficit at this moment, I say to my friend from Rhode Island, is to support the President's tax proposal.

Because that particular proposal--according to the Congressional Budget Office; according to the Joint Tax Committee--increases the deficit or the national debt by $27 billion.

I think that that figure so far is irrefutable. I think that is the fact, that we must go on at this time. The third point, if I could, I would just say, Mr. Chairman, in all due respect to my colleagues; those who might support the President's proposal here that is laid before us, I think we have got to look very carefully at their middle-income cut on that side.

The difference in the middle-income tax cut offered by the President that differs with ours is that we pay for our tax cut. We pay for it by adding that responsibility and additional burden where it belongs: on those who have gotten by with a great deal, and who have profited from the past decade. It is that simple, and I hope we can start on that premise.

Mr. Chairman, as I believe you know, I have been working on an amendment to extend your important "job-lock" and other insurance market reform protections to people who want to start their own self-employed business but do not do so for fear of losing their current employer-provided insurance. Particularly during a time of economic downturn, we do not want people to not start businesses simply out of fear of losing health insurance.

Since there are outstanding issues that have yet to be resolved on this amendment, I will not offer it today. I do strongly believe, Mr. Chairman, that we should do everything possible to get this self-employed protection enacted into law. Because I know you share my concerns for the self-employed, I am confident that we can do just that. Thank you, Mr. Chairman.

The Chairman. Senator Pryor, Marina and the staff have indeed advised me of your hard work on this important matter. As you know, I share your commitment to addressing this self-employed issue. I commend you on your work and share your hope to work out any bugs in this amendment before we vote on final passage of this bill. Thank you.

Are there any who have not spoken who desire to speak?

(No response)

The Chairman. If not, we will stand in recess for the caucuses of both parties, and we will return here at 2:30. And all will have spoken, and we will then move on the read-out of the bill.

(Whereupon, at 12: 37 p.m., the meeting was recessed.)

AFTERNOON SESSION

(After Recess, 2:38 p.m.)

The Chairman. If you will please cease talking, we will begin the afternoon session. I will now call on Marina Weiss.

Ms. Weiss. Yes, Mr. Chairman. I will go through the provisions of the mark-up document that you have in front of you, beginning on page one.

There is an increase in the health insurance tax deduction for the self-employed, which will be discussed by Harry Gutman, when he takes up the tax component of the bill.

The bill also includes grants to States for small employer health insurance purchasing programs. Such sums as would be necessary are authorized for fiscal years 1993 through 1995, and an evaluation would be required to be done by the Department of Health and Human Services.

There is a study of the use of Medicare rates by private health insurance plans; the Secretary of HHS to report to the Congress by January 1st of 1993 on the feasibility and desirability of developing prices based on the methodology used in the Medicare program for payment.

Under Title II of the bill, which is intended to provide improvements in health insurance for small employers, there are a number of individual provisions.

Senator Chafee. Marina, could I ask a question at this time?

Ms. Weiss. Yes, sir.

Senator Chafee. How do you want to do this, Mr. Chairman?

The Chairman. Yes, that is fine.

Senator Chafee. Marina, on the deduction for the self-employed --

Ms. Weiss. Yes, sir.

Senator Chafee. -- that solely applies to self-employed. There would be no deduction for the individual who works for a company who is having to pay a portion, or perhaps all of his or her premiums. Is that correct?

Ms. Weiss. I am going to defer to Hank on that issue.

Senator Chafee. All right.

Mr. Gutman. Senator Chafee, that person would not be entitled to a deduction under this section, but would rather be entitled to a deduction only if medical expenses exceeded the threshold.

Senator Chafee. Which is the situation today.

Mr. Gutman. That is right.

Senator Chafee. In other words, there is no change for that group.

Mr. Gutman. Not for that group; that is correct.

Senator Chafee. Thank you very much.

Ms. Weiss. Under Title II, minimum Federal requirements would be established for State laws regarding the sale of health insurance to small employers.

And, for purposes of this section, small employers is defined as employers with between two and 50 employees working at least 30 hours a week. And the changes in this area relate to guaranteed eligibility of coverage; guaranteed renewability of coverage; certain conditions on the use of pre-existing exclusions.

There are rating requirements that also would pertain and would tighten over time, going from a 20 percent variation around the average premium for a period of three years, and then on to a 15 percent variation for the next two years.

The rating bands would not apply to differences in premiums that are due to age, sex, and geography. Adjustments to the premiums based on these factors would have to be applied consistently across small employers.

We will include report language at the request of several members indicating that it is Congressional intent that the industry work within existing ranges of variation with respect to these factors: age, sex, and geography.

The GAO would monitor and report to the Congress on the issue of moving more quickly, and ultimately toward community rating the impact of doing so on the price of insurance sold to small employers.

GAO would also make recommendations for purposes of adjusting the minimum rating requirements to eliminate experience rating altogether, based on health status and claims experience, and to eliminate variations in the premiums associated with age, sex, and other demographic factors.

Annual rate increases would be addressed. Small employers could increase by no more than five percent above the underlying trend in health care costs.

The benefit packages would be two. In other words, an insurance company offering coverage in this particular area of business--that is to say, employers of two to 50 employees--would be required, at a minimum, to offer two benefit packages.

The first would follow a defined set of benefits that appear in the law; definitions relating to in-patient and out-patient coverage; physician services; diagnostic tests; preventive services, and so on.

The first is a standard benefit package. The second is what we term a basic benefit package, and that is defined in the statutory language only by category.

It would require that the benefit package offered include in-patient and out-patient hospital care; emergency services; physician services; preventive services.

Again, at the request of several members, we have stipulated in the statutory language that nothing in the Federal requirements prohibits the inclusion of mental health benefits in the basic benefit package. A limit on out-of-pocket spending would be required.

There would be a guaranteed availability of coverage; insurance coverage would be made available to every small employer within a State.

The State could choose from any of the four models developed by the National Association of Insurance Commissioners, or, they could apply to the Secretary for a waiver so that they could add a fifth option for their consideration.

The General Accounting Office study referenced earlier would also measure the impact of the standards for small group insurance on the availability and the price of the insurance offered to small employers, and the differences in State laws and regulations across the country.

There would be a requirement that the Secretary of Health and Human Services ask the National Association of Insurance Commissioners to develop State standards for implementation of these statutory requirements by September 30th of 1992.

If the NAIC fails to act in time, the default mechanism is that the Secretary shall develop standards by December 31st of 1992. And States would be required to establish a regulatory program for the adoption and enforcement of these standards, subject to the approval of the Secretary of HHS.

States could enact more stringent standards, and the Secretary of HHS would be authorized to provide waivers for rating band requirements. In the case when a State has equally stringent, but not identical standards--there was a question about Oregon--I believe we have addressed it there.

The enforcement of standards. Insurers violating the standards would be subject to a Federal excise tax equal to 25 percent of the premiums received on all policies sold to small employers. Insurers in States having a regulatory program approved by the Secretary, however, would be exempt from the tax.

The effective date for the health insurance requirements take effect for the health insurance plans offered, issued, or renewed on or after January 1st of 1994, except in those States where there is a biennial legislation session, in which case, it would follow the next regular session of the legislature.

Title III of the bill addresses the issue of improvements in the portability of private health insurance.

All group health insurance and self-insured employer group health plans would be prohibited from denying or limiting coverage on the basis of medical history or health status, except for a limited pre-existing condition exclusions, could apply to individuals with respect to services for which they had not previously had health care coverage.

The exclusion of coverage could not exceed six months. And pre-existing conditions are defined as those that were diagnosed or treated during the three months prior to enrollment.

Insurers, or the self-insured employer group health plans not in compliance with these requirements would be required to retroactively cover any illegally excluded services, and pay a tax penalty of $100 a day for each violation.

Title IV of the bill involves the creation of a Health Care Cost Commission. The commission would be established to advise the Congress and the President of the United States on strategies for reducing the cost of health care.

The commission consists of 11 members who would be appointed by the President and confirmed by the Senate. The terms would be staggered, and the term of the Chairman would be coincident with the term of the President.

In appointing the members, the President would be required to assure representation of consumers, large and small employers, State and local governments, labor organizations, health care providers, insurers, and experts on the development of medical technology.

By March 30th each year, the commission would be required to report on trends in health care spending, the cost of private health insurance, and so on.

In its first annual report, the commission would be, by statute, directed to consult with the Secretary of Health and Human Services and recommend a national model uniform claims form and uniform standards for the collection of medical and billing records for the use of insurers and providers of care.

The commission would recommend a strategy and a schedule for implementing the national use of these forms and standards.

The commission would also make

recommendations to the Secretary with respect to the development and ongoing review of standards for managed care plans and utilization review programs.

Federal certification of managed care plans and utilization review programs would also be addressed in the legislation. The Secretary of Health and Human Services would be directed to establish a voluntary certification program for managed care plans and UR programs.

Certain State laws would not apply with respect to the qualified managed care plans and qualified utilization review programs. These include laws that prohibit, for example, qualified managed care plans from including financial incentives for enrollees to use in the services of participating providers.

We would increase the authorization level for outcomes research. It would be increased to $175 million in 1992; $225 million in 1993; $275 million in 1994, and $300 in fiscal year 1995.

The bill also includes a series of preventive health care benefits that would be added to the package of benefits under the Medicare program.

Initially, it had been the intention of the

Chairman and others to include a fairly broad package of preventive health care benefits. It is my understanding that the financial constraints are such that that package is going to have to be pared down.

It is also my understanding that coverage at this point would be directed at influenza immunization; tetanus vaccine; well-baby care and immunizations for the 300 children who are ESRD-eligible under the Medicare program.

And the financing for that portion of that bill will be handled in the traditional way. That is to say, 25 percent attributable to the beneficiary; 75 percent to general funds.

And that concludes what I have to say.

Senator Moynihan. Mr. Chairman?

The Chairman. Yes.

Senator Moynihan. May I just express our appreciation and that of so many people that on this provision for influenza vaccinations. This is good health care.

The Chairman. Thank you. Are there further questions? If not, we will proceed to the tax portion.

Ms. Weiss. I just wanted to ask, Mr.

Chairman, before I close up here, if you would authorize the staff to make the necessary technical and conforming changes to ensure that the bill language and the costs reflect the --

The Chairman. That is right. Of course we will. Standard procedure. Mr. Gutman, if you would proceed on that.

Mr. Gutman. Mr. Chairman, we now proceed to the tax portions. You all have in front of you a revenue table entitled, "Estimated Revenue Effects of the Chairman's Mark." That is JCX-9-92.

I thought what I would do is work from that revenue table and go through the provisions in the order in which they are set out in that revenue table, going through them in outline form.

The Chairman. Let me be sure I understand which one we are talking about. Would you show it to us?

Mr. Gutman. Certainly. It is this revenue table, Mr. Chairman.

The Chairman. All right. Thank you. All right. Do we all have one? All right. If you would proceed.

Mr. Gutman. Certainly. The first item on the revenue table is the provision of a $300 income tax credit for every qualifying child of a taxpayer.

A qualifying child is defined as a child under the age of 16 who resides with the taxpayer for more than six months during the taxable year. This credit is not refundable, and the credit amount would be indexed for inflation.

The second item in this category has to do with a number of changes to the earned income tax credit. There are two principle features here.

The first feature would repeal the existing young child credit, which is a credit that is available to taxpayers with qualifying children under the age of one year. That is a rate of five percent of the qualifying amount; that is earned income up to $7,520.

The young child credit would be repealed, but the earned income tax credit itself would be both expanded and simplified. The proposal would increase the basic earned income tax credit rate for taxpayers with two or more qualifying children by 1.75 percentage points.

The proposal would also simplify the operation of the current earned income tax credit by eliminating interactions that occur between the health insurance portion of the earned income tax credit and the medical expense deduction.

The third portion of the first part of the bill extends the current targeted jobs tax credit for an 18-month period.

Now we move into the second portion of the mark entitled, "Promote Long-Term Economic Growth." The first portion of that, a description of which appears at page six of your mark-up document--and, by the way, I will try to refer to the appropriate pages in the mark-up document--which is JCX-7.

JCX-7, entitled, "Description of Chairman's Mark." At page six of that document is a description of all of the individual retirement arrangement changes that are set out in the Chairman's mark.

In particular, under this portion of the bill, we emphasize the restoration of the deductibility of IRA contributions for all taxpayers, and that the limitations would be indexed for inflation.

In addition, the Chairman's mark would permit non-deductible contributions to a new special IRA --

Senator Packwood. May I ask a question on that?

Mr. Gutman. Yes, sir.

Senator Packwood. I know you must have done it somehow, but how did you get the loss on this down to $5 billion down to the original $25 billion?

Mr. Gutman. Well, first, Senator Packwood, there is, in some of the other provisions -- rather, line one here contains not all of the IRA provisions; they are distributed throughout the proposal, so that there are a number of IRA-related issues that are elsewhere in this revenue table. The second, I believe, is the number that you cited was a six-year number.

Mr. Hardock is going to explain the balance of that, Senator.

Mr. Hardock. Senator, as Hank Gutman just pointed out, the effective date of this proposal is 1/1/93. Because we are already into this calendar year, the IRA would not be brought into effect of January 1 of next year.

Another change that Hank pointed out was that the home ownership withdrawal provisions, the education withdrawal provisions, and the medical withdrawal provisions have been broken out and appear elsewhere on the table. Those result in significant revenue lost.

Senator Packwood. And then we have part of it outside the five-year window, if you are starting in 1993.

Mr. Hardock. Obviously, the proposal has always been permanent, Senator. And, yes, the losses would continue outside the window, as they would have before.

Senator Packwood. But the losses are five-year losses.

Mr. Hardock. Right. Another change, Senator, is that this proposal, unlike the $25 billion estimate that I think is now about two years old, but would integrate the cap on IRA contributions with a cap on 401(k) contributions.

Currently, you can only contribute about $9,000 to 401(k) plans. This proposal would say that your total IRA, plus 401(k) can exceed $9,000. That would make it a little less attractive to some people at the higher end.

Senator Packwood. Thank you, Mr. Chairman.

Mr. Gutman. The provision then involves, as I said, restoration of the deductibility of IRA contributions.

Second, the creation of a new, non-deductible Special IRA, withdrawals from which would not be includable in income, so long as they were attributable to contributions that had been held by the Special IRA for at least five years.

And another feature of the proposals is the permissibility of the transfer from a deductible IRA to a Special IRA, without the imposition of the ten percent tax on early withdrawals.

However, if a taxpayer does withdraw money from a deductible IRA and then places it into a Special IRA, the amount that is transferred would be includable in income with a special transition rule for amounts that are transferred before January 1st of 1994.

The other provisions involving withdrawals for housing, education, and medical expenses I will cover when we get to those parts of the mark.

Item #2 in this category involves a number of proposals that relate to education. The first, which is described beginning at page nine of the document, is the self-reliance loan proposal.

The proposal would create a program of direct loans for higher education expenses. The

Secretary of Education would make payments to participating institutions and eligible students would have an account established with the Secretary of Education to record interest on and repayment of their self-reliance loans.

The borrowers would make income-dependent repayments in the future through the income tax system by means of a specially-computed addition to the tax that represents both principal and interest on the loan.

The details of the self-reliance loan proposal are contained through page 16 of the mark-up document.

The second education feature in the mark involves a provision that would permit individuals who have paid interest on qualified education loans to choose either a deduction for such interest, or a non-refundable credit against regular tax liability that would generally be equal to 15 percent of the interest that was paid, subject to a maximum credit of $300.

The third education item that is contained in this portion of the mark is a proposal involving the formation of, and contributions to, tax-exempt youth training organizations. This is at page 19 and page 20 of the document.

Under the proposal, tax-exempt status would be created for certain youth training organizations that are organized for the purpose of administering a training program combining supervised on-the-job training for full-time high school students with academic training.

In addition, the proposal would provide an increased deduction for cash contributions that are made to the tax-exempt youth training organization. The allowable deduction for such a contribution would be 150 percent of the contributed amount.

The fourth item in the education portion of the mark is the availability of penalty-free withdrawals from IRAs for education purposes. The details of this are set forth at page seven of the mark-up document.

The fifth provision extends the current employer-provided educational assistance program for 18 months.

The final provision in this particular section involving the expansion of educational opportunity is an amendment to the current educational savings bond provision.

Under current law, interest income earned on a qualified Series Double EE savings bond is excludable from gross income if the proceeds from the bond, upon redemption, do not exceed qualified higher education expenses that are paid by a taxpayer during the taxable year.

The proposal would expand the definition of qualified higher education expenses to include tuition and fees paid by a taxpayer for the enrollment or attendance of an individual at an eligible educational institution, rather than, as is under current law, simply that for dependents.

And, in addition, the proposal would repeal present law adjusted gross income phase-out limitations and related rules requiring that bonds be issued to individuals who are at least 24 years old.

Item G in the Chairman's mark actually appears at page 64 of your mark-up document, and extends for a six-year period existing disclosure authority, under which tax information supplied to the Internal Revenue Service and the Social Security Administration by third parties--not by individual taxpayers, but by third parties--may be given to the Department of Veteran's Affairs to assist it in determining eligibility for amounts paid under certain of its needs-based programs.

The next category involves Better Access to Affordable Care. The first portion of that is an extension of the current deduction for health insurance premiums of self-employed, which Senator Chafee mentioned earlier.

For this year, the existing provision would be extended from its current expiration date of June 30th through the end of the year at the 25 percent deductibility rate, and then, for the next two years, 100 percent of the premiums paid by self-employed individuals would be deductible.

Mrs. Weiss described items B and C in her description. Item D, at the top of the next page, is dealt with at page seven of your mark-up document, and allows penalty-free IRA withdrawals for serious medical expenses.

Item E, which is described at page 27, involves an increase in the tax rate on ozone-depleting chemicals.

Currently an excise tax is imposed on certain ozone-depleting chemicals. And, under the proposal, it would increase and apply the same tax base to both initially listed chemicals and newly-listed chemicals. Finally, Item F is an 18-month extension of the current orphan drug tax credit.

Item #4 in this category involves investment in real estate. The first provision in this category is an allowance of penalty-free IRA withdrawals for first home purchases. This, too, is described in a paragraph on page seven of the mark-up document.

From pages 29-35, a number of changes to the unrelated business income tax provisions are described. Those provisions are designed to make it easier for pension plans to invest in real estate, and essentially relax some of the rules with respect to debt-financed acquisitions and other rules that will ease pension plan investments in real estate.

Item C, which appears at page 36, is a $5,000 tax credit equal to 10 percent of the purchase price of a residence, or up to a maximum of $5,000 for individuals who are first-time purchasers of a new principal residence.

This provision would be effective if a taxpayer acquires a residence on or after February 1, 1992, and before January 1 of 1994; or enters into a binding contract to acquire the residence before January 1, 1994, and purchases the residence within 90 days of entering into that binding contract.

Item D, at page 37, provides passive loss relief for those who are engaged in the real estate business. It extends passive loss relief to taxpayers who materially participate in real estate development activities.

The taxpayers would be able to use the losses from those activities to offset income from property in which the taxpayer owns more than a diminimus interest and actively participates, plus 80 percent of the taxpayer's taxable income for the year that is attributable to other real estate activities that the taxpayer is involved in.

And the purpose of this provision is to redress the perceived imbalance in the passive loss rules as originally enacted in order to provide relief for those who are engaged in the real estate business.

The next item, Item E, extends the depreciation period for non-residential real estate from 31.5 to 40 years.

The next item, Item F, which is at page 40 of your document, extends the existing low-income housing credit for 18 months, through December 31, 1993, and, in addition, it makes a number of modifications to improve the effectiveness of the program.

And Item G, at page 42 of your document, extends the current mortgage revenue bond and mortgage credit certificate programs for an additional 18 months. Item five --

Senator Breaux. What page are you on?

Mr. Gutman. I am on page two, Senator; Item five, a little below half way down the page. "Other Incentives to Improve Long-Term Investment and Improved Competitiveness."

The first item there is a ten percent investment tax allowance. That is, an additional first-year depreciation deduction that is equal to ten percent of the adjusted basis of -- I am sorry. That is page 43.

An additional first-year depreciation deduction equal to ten percent of the adjusted basis of certain qualified property that is placed in service before July 1, 1993.

Basically, the property that will qualify for this ten percent investment tax allowance is property that is described in Section 1245 of the

Internal Revenue Code, and this credit, the investment tax allowance, would be available both for regular tax, and for AMT purposes.

The operation of the ITA is set forth in a number of examples at the bottom of page 44.

The Chairman. Just a moment.

Senator Baucus. If I might ask a question. Generally, Section 1245 property is --

Mr. Gutman. 1245 property is basically property that is used in a trade or business other than real estate, in general, Senator.

Senator Baucus. Thank you.

Senator Durenberger. Mr. Chairman.

The Chairman. Yes. Senator Durenberger.

Senator Durenberger. May I ask a question? Really, it deals with the placed-in-service date. I mean, I can think of a situation where a project would meet the contract dates; it would meet the ground breaking; it would meet all of that, but it is such a large project that it just cannot be completed within the period of time prescribed here, which I think is the fourth quarter of 1993. Is there any way to get some flexibility for these large-sized projects, or something?

Mr. Gutman. Moving the placed-in-service date back to July 1, 1993, with the provision being effective basically for orders placed in 1992 was intended to try to accommodate that problem.

In other words, the ITA is basically available for property that is ordered prior to January 1 of 1993, during the 11-month period, February through the end of the year. But, then, because of the lag time, the property will still qualify, so long as it is placed in service before July 1st of 1993.

Senator Durenberger. But does it have to be placed in service by July 1?

Mr. Gutman. Yes. Yes.

Senator Durenberger. Well, that is the kind of problem I was contemplating where it is of such a size and such a dimension -- I think, for example, of a paper-making facility. These are huge facilities.

And yet, they are going to provide tremendous, tremendous investment opportunities. Is there any other way to accommodate projects of that size?

Mr. Gutman. Well, Senator, that, I think, is one of the problems that is endemic when you have a --

Senator Durenberger. Placed-in-service date.

Mr. Gutman. -- placed-in-service, or a limited time period within which an investment incentive is available.

Senator Chafee. Mr. Chairman.

The Chairman. Yes. Senator Chafee.

Senator Chafee. Mr. Chairman, I would just like briefly to go back to page 26.

Senator Breaux. Can I ask, Mr. Chairman, on this thing -- I do not want to --

Senator Chafee. No, go ahead. Then I will go ahead. You go ahead.

Senator Breaux. Just on this point, the July 1st date, I would try and make a point, is what, 12 months, and then four months of the next year.

Mr. Gutman. It is another six months thereafter. It is 18 months --

Senator Breaux. So, it is 18 months.

Mr. Gutman. It is a 17-month period from the effective date.

Senator Breaux. It is from the effective date, or July 1st?

Mr. Gutman. Yes. The effective date of the provision would be February 1st of 1992. And so long as the property is placed in service before July 1, 1993, which is 17 months, you would be available for the investment tax allowance.

Senator Breaux. Well, suppose we do not pass this bill for another six months.

Mr. Gutman. Well, unless something happens to change the dates, then some of the period of --

Senator Breaux. Well, I mean, I think that is an important point. We do not know when we are going to finally pass the tax bill, and if locked into a July 1st, 1993 placed-in-service, we may not pass this till June of 1993.

I mean, the point I am trying to make is that it gets closer to the July 1st date of being a shorter and shorter period for that project to be completed.

I can think of ships that may like to take advantage of this, but would take more than, say, five or six months to actually construct. And as the date of passage of this bill gets further and further back, there is no extension of the placed-in-service date. Perhaps there should be some consideration for tying those two together.

The Chairman. Senator, I am sure that you could pick out projects that are going to take substantially longer than that, even if we move out farther in time. The problem is, we have modeled this after the administration's proposal, did we not?

Gutman

Senator Breaux. That is correct, Senator.

The Chairman. And we figured the cost based on that. And the more you extend it out, the more you add cost to it, and we do not have any flexibility left insofar as adding to the cost.

That is our problem. Because I am sure you are quite right, that we could pick project after project that will not get covered in the process.

Senator Chafee. Mr. Chairman.

The Chairman. Yes.

Senator Chafee. Mr. Chairman, I would briefly like to call attention on page 26 to the 100 percent deductibility of health insurance premiums paid by the self-employed. As I read this--and correct me if I am wrong, Mr. Gutman--the 100 percent deductibility does not apply until 1993 and 1994.

Mr. Gutman. That is correct, Senator.

Senator Chafee. Then that ends at the end of 1994. In other words, you get two years out of it.

Mr. Gutman. That is correct.

Senator Chafee. Then, presumably, it drops back to the 25 percent.

Mr. Gutman. No. At that point there is no provision that permits deductibility of these premiums at all, other than the extent to which they constitute medical expenses.

Senator Chafee. All right. That is even worse. My point is that no one in their right mind thinks that once we get that that it will not be continued.

And, therefore, the only way to pay for it will be to take this 36 percent tax rate and either increase it, or apply it to lower incomes.

And I think that is the point that we have been describing here earlier, Mr. Chairman, where we are concerned that we are embarking on a road whereby we are going to be not only locked into these rates, but these rates are either going to increase, or the higher rates are going to apply to lesser amounts.

The Chairman. Well, my concern, if we are talking about something like that, would be--when you made your point that we were not cutting more to the deficit and putting more of it that way, that I look at the other side of it--the CBO estimates that the administration's bill comes in with a $27 billion increase to that deficit, adding to that deficit. That is what we are looking at there.

Senator Chafee. Well, Mr. Chairman, I will conclude this by saying you will not find everybody on this side an enthusiastic supporter of the administration's bill, and certainly the second phase of it. What support you will find from many of us over here is for the first seven items.

The Chairman. Well, let me further state then, Senator Chafee, another reason as far as a limitation on that deductibility, we have all sorts of comments about a major health care reform bill coming about. And by that time, that may well have happened. And I would rather not anticipate the situation.

Mr. Gutman. The next provision in this category appears at page 46 of the mark-up document, and it involves the Alternative Minimum Tax treatment of gifts of appreciated property to charitable organizations.

And, under the proposal, all charitable

contributions of appreciated property, whether real, personal, or intangible, made during 1992 and 1993 would not be treated as a tax preference item for Alternative Minimum Tax purposes.

In addition, the Secretary of the Treasury would be directed to develop and implement a procedure to get an advanced determination for Federal income tax purposes on the value of property transferred to charitable organizations.

Finally, the Secretary would be directed to conduct a study on the tax treatment of corporate sponsorship payments received by charitable and other tax-exempt organizations in connection with athletic and other events.

Senator Moynihan. Mr. Chairman.

The Chairman. Yes, of course. Senator Moynihan.

Senator Moynihan. May I simply say, the advanced determined provision seems to me very good tax practice, and I see Mr. Gutman agreeing.

Mr. Gutman. The next provision deals with the tax treatment of intangible drilling costs of independent producers. It contains three changes to the current treatment for Alternative Minimum Tax purposes of IDCs.

First, it raises the net oil and gas income offset pursuant to which the amount of IDC preferences are determined, from 65-70 percent.

Second, it eliminates the adjusted current earnings adjustment for intangible drilling costs. And, finally, it simplifies the existing special energy deduction by removing the need to identify exploratory, as compared to producing, wells, by providing a mathematical test to accomplish that result.

Senator Packwood. Mr. Chairman.

The Chairman. Yes. Senator Dole.

Senator Packwood. I wonder if I might put in the record at this point a letter from Secretary Brady on this very point, in effect agreeing with the letter I had written about the impact of these rules on independent producers, saying they should be softened. Mr. Goldberg is here. I think he can respond to that. I do not have my sheet here, so I do not know what the cost of this change is.

Mr. Gutman. The cost of this provision is $800 million over five years, Senator.

Mr. Goldberg. Senator Packwood, we have not had a chance to review the proposal, but it is clear to us that the current AMT rules do have an adverse effect on independent producers, and it is an issue that we think should be addressed, and the situation should be remedied. So, I appreciate your support.

Senator Packwood. I would just like to put this in the record, if I might.

The Chairman. No objection.

(The letter appears in the appendix.)

Senator Grassley. Mr. Chairman.

The Chairman. Yes.

Senator Grassley. Could I please go back one step to the ITA?

The Chairman. Yes, of course.

Senator Grassley. My question, Mr. Chairman, and to the staff, is does it apply to single-purpose agricultural buildings? And I use that term the same way that was used prior to the 1986 tax bill.

Mr. Gutman. Yes, it does, Senator.

Senator Grassley. It does. Mr. Chairman, I would raise a point, and this is entirely opposite a position I would have taken ten years ago.

A lot of us on this committee fought very hard for the application of then the ITC--not the ITA--to special-purpose agricultural buildings.

My purpose was more oriented towards the fact that Congress had passed such legislation in 1976, and then, through their own rulings and through applying one court case as opposed to three or four that went against them, to deny certain Congressional policy for single-purpose agricultural structures.

So, we worked then for three or four years to finally get the Treasury Department to do what Congress intended in the first place, but it turned out to be very bad economics for the family farmer.

And I guess I am not going to say anything more now than to just ask the Chairman and the staff to look at whether or not there should be at least some limits put on it, or no application whatsoever of the ITA to special-purpose agricultural buildings. It should apply to the equipment inside, but not to the structure itself.

The Chairman. Thank you, Senator. We will do that. We will take a look at that.

Mr. Gutman. The next provision, Senator, is the repeal of the ACE depreciation adjustment. That is item B-3. With respect to property placed in service after February 1, 1992, the proposal would eliminate the depreciation component of adjusted current earnings for the corporate AMT.

In other words, the same depreciation rate would be used for all purposes in the corporate AMT, rather than having a special depreciation rate for the adjusted current earnings component.

The next provision would extend for 18 months the current research and experimentation tax credit. Item D, which begins at page 53 of the mark-up document, contains two capital gains relief proposals.

The first is a progressive rate structure that would be applied to capital assets other than collectibles that have been held by a taxpayer for two years, or more.

Under the progressive capital gains rate proposal, a tax rate of five percent, 19 percent, 23 percent, or 28 percent, would apply to capital gain, depending upon the individual taxable income.

Mr. Auerbach will, in just a moment, explain the operation of that provision to you with a number of examples.

The second portion of the capital gains proposal involves an exclusion of 50 percent of the gain realized on the sale or exchange of certain small business stock that has been held for more than five years.

The purpose of this provision is to encourage investment in small businesses and entrepreneurial enterprises with a 50 percent exclusion then for the gain on the sale of the stock, so long as the stock has been held for five years.

The types of companies, the stock of which qualifies for this special treatment, are described at pages 55 and 56 of the mark-up document.

In particular, you should notice that the provision is available with respect to investments in corporations, the adjusted basis of the assets of which does not exceed $100 million.

Now, Mr. Auerbach, if you would go through the capital gains proposal, please.

Mr. Auerbach. Yes. You should have in front of you a group of charts and tables, the front of which says, "SFC Capital Gains Proposal Example 1."

This consists of two charts detailing two examples, plus an explanation and further examples. I will just go over the first two charts to show how the proposal works.

The basic idea of the proposal is to apply an alternative rate schedule to capital gain income, continuing to apply the ordinary schedule to other income.

And the rate schedule, as Mr. Gutman said, would be five percent, corresponding to people in the 15 percent bracket. That is an exclusion of 67 percent for gains in that bracket; 19 percent for people who would be in the current 28 percent bracket, which amounts to an exclusion of gain of 34 percent in that bracket; 23 percent for people who would be in the 31 percent bracket; that represents an exclusion of 27 percent; and 28 percent for people above the 31 percent bracket, under the other provision of this proposal, which would raise the top bracket to 36 percent. And that represents an exclusion of 22 percent.

Therefore, it is termed a progressive capital gains proposal because the rate of exclusion declines with the increase in the marginal tax rate on ordinary income.

The examples that you have here -- there are two examples in the graphs to represent two typical taxpayers in their situations and how they would be affected under current law and under the proposal to change the treatment of capital gains tax rates.

The first taxpayer is a taxpayer with $25,000 of ordinary income, and, in addition, $15,000 of net capital gain. And in the graph on the left side is how the taxpayer would be treated under current law. On the right side is how the taxpayer would be treated under the proposal.

This taxpayer's income before taking account of capital gain is entirely in the 15 percent bracket, and all of that taxable income would be taxed at 15 percent.

Under current law, an additional $10,800 of gain income would be taxed at 15 percent, and the remainder of the $15,000 gain--that is, $4,200--would be taxed at 28 percent. So, some of the gain would be taxed at 15 percent; some of it would be taxed at 28 percent.

Under the new proposal, once the taxpayers began counting capital gain income, the first $10,800 would be taxed at five percent, because that corresponds to the 15 percent bracket--the break points are the same--and then passing into the next bracket, which, for capital gains, is 19 percent rather than 28 percent.

The taxpayer would conclude the computation of tax. The result would be a tax on the gain of $960 rather than $2,445.

The second example shows a taxpayer with a larger capital gain and a larger ordinary income, so this is a higher bracket taxpayer. This taxpayer has $60,000 of ordinary income, and, in addition, $200,000 of net capital gain.

Under current law, this taxpayer would otherwise be in the 31 percent bracket under current law, but once the taxpayer hits the 28 percent bracket, current law dictates that this taxpayer will pay no more than 28 percent on capital gains.

There is a ceiling of a 28 percent rate on capital gains. Therefore, this taxpayer's entire capital gain would be taxed at 28 percent.

Under the new proposal, the first part of the taxpayer's capital gain--which would amount to $26,500--would be taxed at 19 percent, because that part of this taxpayer's gain is in the ordinary bracket corresponding to 28 percent, and, hence, the alternative capital gains bracket corresponding to 19 percent.

The next piece of the taxpayer's capital gain--a total of $88,500--would be, under the proposal, in the 31 percent bracket, which corresponds to an alternative capital gains tax rate of 23 percent.

And the final piece of capital gain at the top, which would be, under the proposal, in the new 36 percent bracket, will be taxed at 28 percent, for a change in tax from $56,000 to $49,190.

The remaining sheets attached to this go through several other examples to elucidate the presentation of how the proposal would work.

Senator Danforth. Mr. Chairman.

The Chairman. Yes.

Senator Danforth. I am just trying to figure this out.

Senator Moynihan. Are you having problems?

(Laughter)

Senator Danforth. Is it fair to say that this is more complex than current law?

(Laughter)

Mr. Auerbach. This is simply taking the established principle of applying an alternative rate to capital gains, which we currently do, with a 28-percent maximum, and extends it all the way down to the lower brackets.

At present, a taxpayer who has hit a tax bracket above 28 percent--that is, someone who is now in the 31 percent bracket--faces an alternative tax schedule on capital gains; namely, a top rate of 28 percent. So, we now have an alternative rate schedule at the top, 28 percent corresponding to 31 percent.

This simply establishes alternative rates for the other rates in the tax system, namely, the 28 percent rate, and the 15 percent rate.

Senator Packwood. Only they have to be a tax man to figure this out.

The Chairman. No, you really do not. It is a little hard to follow, I agree with that. But if you have a fellow that is making $100,000, he will figure it out, and it will not take him long.

(Laughter)

Senator Danforth. Mr. Chairman, could I just follow through, if I could, and ask Mr. Goldberg, have you analyzed this proposal?

Mr. Goldberg. Senator Danforth, we saw it about 1:30 this afternoon, so the answer is no. However, I would point out that, looking at it very quickly, as a practical matter, it is likely to afford very little, if any, capital gains relief to one-time sellers of small businesses, one-time sellers of family farms, and similarly situated taxpayers who have a one-time sale of a single asset with a great deal of appreciation and value.

Mr. Foley. Well, that will depend on the taxable income of the individual making the one-time sale. If you have an individual who is currently in the 15 percent bracket, somebody with adjusted gross income of $40,000, but taxable income of only $25,000, this proposal will afford that person who has, let us say, a taxable gain of $50,000, tax relief.

Mr. Goldberg. I believe that in the real world, when the members check with those who own small businesses and those who own family farms that, while this is certainly a step in the right direction, I think you will find, as a practical matter, that it affords very little capital gains relief for those classes of taxpayers, and I would just urge you to investigate that question.

Senator Packwood. Can I ask Dr. Cohen a question?

The Chairman. Yes. Sure.

Senator Packwood. I think I understand this, although I am glad it is not in the simplification section of this mark-up. You do not mean that somebody who makes $25,000--this is their ordinary taxable income, so they are in the bottom category--is going to pay five percent on their capital gains. I do not think that is what you meant to say, is it?

Mr. Foley. Yes. I am saying --

Senator Packwood. Mr. Goldberg is not saying that. You sell your business. You have got $25,000 of taxable income, you sell it for $300,000, and you have got a capital gain of $200,000--your lifetime business.

Mr. Foley. Right.

Senator Packwood. You do not pay five percent on that, do you?

Mr. Foley. No, Senator. What I am saying is that if you are currently in the 15 percent bracket, you will take your capital gain and you will essentially stack your capital gain on top of your ordinary income.

And then the taxation of your capital gain will be -- the amount of the capital gain in the

15 percent bracket will be taxed at five percent. The amount of the capital gain that would, under today's law, fall in the 28 percent bracket, would be taxed at 19 percent. And that is how that would work.

Senator Packwood. Well, Mr. Goldberg is right. For somebody who is making $60,000, $70,000 a year: they have a hardware store, they have ten employees, and they sell it for half a million dollars, they are not going to get much relief under this. If they cash out; they retire.

Mr. Foley. If you have some who has taxable income who is currently in the highest tax bracket, they will not receive any tax relief under this proposal.

The Chairman. Let me see if I can make another point to try to get this in prospective. The administration's capital gain costs about how much, about $14 billion?

Mr. Goldberg. We believe that it will raise $4.5 billion.

The Chairman. Well, I was not asking you, Mr. Goldberg, because I know how you fellows figure capital gains from the OMB side. I can go right back to the day when we were talking about lowering the top rate, and the administration was saying, if we bring the capital gains up from 20 to 28, how much money we would make to be able to bring that top rate down.

Now the administration and the OMB is saying how much money we will make by lowering the capital gains. You just cannot have it both ways. But let us get to this point. The question was $14 billion, approximately.

Mr. Auerbach. Over the budget window through 1996, it would be about $12 billion, because there would be one fewer year added on.

The Chairman. All right. And this one that is proposed will cost us how much?

Mr. Gutman. $7.3 billion.

The Chairman. $7.3 billion. So, if it is $12 billion on the one side and $7 billion on this, we are still talking about a lot of money insofar as what you are going to see in the way of incentives for people to take capital gains. Not as much as the administration, but still a lot. $7 billion as related to $12.

Senator Hatch. Mr. Chairman. Senator Hatch down here.

The Chairman. Yes. Right.

(Laughter)

The Chairman. I never thought that I could overlook you. But go ahead.

Senator Hatch. I appreciate that. I have had some problems in this area, too. Could I ask Mr. Goldberg, I know that you have some scoring difficulties on capital gains, but I keep hearing this $27 billion cost of the deficit as well.

Could you tell us how the administration scores not only capital gains and where you come out there, but also on the $27 billion?

Mr. Goldberg. Yes, Senator Hatch. The non-partisan Treasury Department --

(Laughter)

Mr. Goldberg. -- scores the administration's budget--the seven items, plus the pay-fors--as raising $15 billion, i.e., reducing the deficit by $15 billion over the five-year period.

We should point out that that deficit reduction occurs, not through tax increases, but occurs by reason of good government reforms and reductions in government spending.

The Chairman. Well, I am all for good government.

Senator Breaux. Mr. Chairman, I would just like to ask some factual questions about it. Does it restrict, in any way, the type of assets under this progressive plan that we are talking about being effected about it, or does it affect, in any way, assets that are already held that meeting the holding requirement?

Mr. Gutman. This would apply to existing assets, Senator; and it applies to all assets, with the exception of collectibles.

Senator Breaux. All right. Thank you.

The Chairman. All right.

Mr. Gutman. The next item on the list, which is Item E, fourth from the bottom of the page on page two, is an extension of the current qualified small-issue bond provision for 18 months, through December 31, 1993.

And the next provision is an extension of the current business energy tax credits that are allowed for 10 percent of the cost of qualified solar and geothermal energy property. This is another 18-month extension of a provision that would otherwise expire on June 30th.

The next item involves the classification for tariff purposes of multi-purpose vehicles. This provision conforms the treatment of multi-purpose vehicles, such as mini-vans and sport utility vehicles, by various agencies.

These vehicles have been classified as trucks, for most purposes, such as emission or fuel economy standards, but as cars for tariff purposes. The amendment incorporates language into the tariff schedules to correct that anomaly.

Senator Packwood. Now, correct which anomaly?

Mr. Gutman. The anomaly that these vehicles are treated as trucks for some purposes and as cars for others, and it treats them as trucks for all purposes.

Senator Packwood. Well, what is anomalous about that? As I understand --

Mr. Goldberg. Well, it is inconsistent.

Senator Packwood. Oh. It is inconsistent.

Mr. Gutman. There is an inconsistency. Excuse me, Senator.

Senator Packwood. Oh. Well, in that case, we would not want to do anything inconsistent. Is it not true that both the EPA and the National Highway Traffic Safety, whatever it is, are now starting to classify, for many purposes, these trucks as vans, and vans as trucks, that you are taking an old definition that the other two are using?

Mr. Kyle. There may be some changes. I think the proponents of the measure argue that, for many purposes, they are still being treated as trucks for the items that are being moved into the truck category, and, therefore, it is an attempt to make them consistent in this case.

Senator Packwood. Well, let me make sure I understand what the effect is going to be. The major auto companies in the United States now have about 75 percent of the sport/utility, and about 90 percent of the van business.

For those things that are now coming in at 2.5 percent that, in essence, look like the American van that I drive, they are not going to be taxed at 25 percent, and the consumer is going to pay $2,000 to $3,500 more for them, assuming they still come in. Have I got it roughly right?

Mr. Kyle. It is true that the effect of this provision would be to increase the tariff on the items affected from 2.5 percent to 25 percent.

Senator Packwood. It would probably have the effect of the domestic vans going up roughly $2,000 to $3,500.

Mr. Kyle. Obviously, it would depend on the price of the van.

Senator Dole. But why are we doing it?

Mr. Kyle. The purpose, I think, of the provision, is to correct the anomaly that exists that these trucks that are brought in are treated as trucks under EPA and DOT standards for emission and KFA standards, but they are treated as cars for purposes of the tariff schedules.

Senator Riegle. Mr. Chairman, could I be heard on that?

The Chairman. Yes, of course. Senator Riegle.

Senator Riegle. There is an anomaly in the law, and, in effect, it is a gimmick. The Customs Service, back in 1989, was very clear on saying that the vehicles in this category were trucks, and ought to be treated under the tariff schedule for trucks as opposed to cars. And there was an administrative ruling to set that aside.

It does make a difference, because it lowers the tariff from 25 percent to 2.5 percent, and it costs the Federal Government each year about $220 million. That is the CBO estimate.

So, there is a revenue loss to our government associated with that administrative decision overturning Customs' judgment. But let me give you an idea of how the anomaly works, and I am just going to give you one vehicle type; there are others to which this would apply.

I am going to just take the example of what is called the British Range Rover. This is an imported vehicle which is classified as a car by the Customs Service under this administrative ruling, but it is classified as a truck for safety standards, for emission standards, and for fuel economy standards.

And in all three of those standards, they are less than they are for passenger autos. And, of course, they are under the jurisdiction of the U.S. Government. So, you have got this situation.

The same thing is true with respect to the luxury car tax. They have argued that even though they want it classified as a car in order to pay the lower tariff, then they want to be able to switch over and have the truck designation with respect to avoiding the luxury car tax.

And what it is, it is an illustration of how foreign suppliers--this is one example; I can give you other examples with various Japanese vehicles-

-where they will send the car in under one guise, or the vehicle; it is not a car. They try to have it be seen as a car.

They will send it in, and then they will reconfigure it once it gets here and turn it into a vehicle that is, in fact, a truck, and should come under the truck standards, but then try to play the game both ways.

It is an important anomaly that ought to be corrected. It does pick up $220 million to the U.S. Treasury that should properly be paid. I mean, there has to be consistency along the lines of applying these standards.

And when we allow this zigzag treatment where we allow inconsistent application of which category it is in order to benefit the importer that is sending it in and let that person, in effect, defraud this government.

I mean, that is why the Customs Department blew the whistle on this back in 1989, and we ought to stay with their judgment at that time and that is what this would do. And it picks up, as I say, $220 million.

Senator Symms. Mr. Chairman.

The Chairman. Yes. Senator Symms.

Senator Symms. Can I ask a question? How much per vehicle will it cost more for the consumers? Does anybody have any numbers on that?

Senator Dole. $2,000 to $3,500.

Senator Symms. $2,000?

Mr. Kyle. Obviously, it is going to depend on the price of the vehicle, since it is an ad valorem tariff on the item coming in. But it would raise the tariff on the imported items that are affected by this provision to 25 percent.

Senator Symms. Has anybody got any numbers on what -- you know, in our part of the world, Senator Baucus and mine, a lot of people drive these kinds of vehicles. What has been Detroit's response, if we do put this in? Will they just raise their prices to match the foreign vehicles, or will they --

Mr. Kyle. I do not think it is possible to speculate. I certainly could not speculate as to what the Big Three would do in response to this provision.

Senator Riegle. If I might just say to my friend, if he would yield, there is intense competition in this area. If you go out and look at the vehicle types that are available, there is no shortage of competition, and there is no shortage of price competition.

And you can go, and whether it is on financing arrangements or cost reductions, what have you, this is a very good time to go buy an American vehicle of this kind, and I would encourage you to do so.

(Laughter)

Senator Symms. I hope to be able to afford to do that next year.

The Chairman. Senator Dole.

Senator Dole. Is there enough money raised in the offset to repeal the luxury tax on all automobiles? Is that the reason for this, to get enough money to repeal the luxury tax on all automobiles?

Senator Riegle. I am not sure that is in there. Is that in the Chairman's mark? I am not sure it is.

The Chairman. There is not any correlation. We have worked very hard to get it to pay for airplanes and boats.

Senator Dole. But, I mean, if there is enough money, why do we not just take the luxury tax off automobiles?

Mr. Gutman. There is not enough money there, Senator.

The Chairman. No. We did it to take the tax off of airplanes and boats.

Senator Hatch. Mr. Chairman.

The Chairman. Yes. Senator Hatch.

Senator Hatch. If this provision stays in the bill, we checked with our largest car dealer in Salt Lake City. He said that 40 percent of his sales are derived from vehicles reclassified by this bill.

And typical price increases for Utah consumers, as well as those in most other States, would be just on three. He lists Toyota 4-Runner would be up $4,200; Trevia van up $4,500, and a Land Cruiser would be up $5,900.

Those are tremendous additional costs to American consumers. And, like Steve said, in our part of the country, a lot of these four-wheel models are used all the time. And I just do not see how that benefits consumers or the Tax Code. It is just another form of protectionism.

The Chairman. Thank you. Would you proceed?

Mr. Gutman. The next item which appears at the bottom of page two is a proposal to cap the deduction for executive compensation for corporate officers at $1 million. At the top of page three --

Senator Dole. How does that work? Could you explain that last one? That will not affect members, will it?

(Laughter)

Mr. Gutman. A covered employee is an officer of a corporation, other than an employee-owner of a personal service corporation, Senator.

Senator Danforth. Now, can I ask a question? These are now deductible as ordinary and necessary business expenses, right?

Mr. Gutman. That is correct, Senator.

Senator Danforth. And, as a matter of practice today, how customary is it for us to make distinctions between what we think are appropriate, ordinary, and necessary businesses expenses and what are not?

Mr. Gutman. It is not very common to do that.

Senator Danforth. I remember a few years ago, we had a big debate on first-class air fare, and there was, I think, an amendment offered on the floor that the difference in cost between a first-class ticket and a coach ticket should not be deductible. And I remember Senator Long arguing very strongly on the floor of the Senate that we should not make that kind of distinction.

I know that there has been so much written about excessive executive salaries, and I do not want to indicate any delight or support for the idea that somebody in a failing company is being paid $3 million to $4 million a year, but there is a broader question of tax policy here, I think-- and I would really defer to Treasury and Joint Committee on this issue.

But are we wading into a broader precedent if we say that ordinary and necessary business expenses are only deductible to the extent that we liked what businesses are doing in spending their money? It is very manipulative of a very ancient provision in the tax law. Is this a precedent that is going to come back to haunt us?

Senator Breaux. Mr. Chairman, I have a question.

The Chairman. Yes. Senator Breaux.

Senator Breaux. I would just ask a question of the staff, does the IRS now have the authority, according to your summary of what the present law is, to allow the deduction for what you say is a reasonable allowance for salaries? Does that imply that they cannot allow it if they determine it is unreasonable?

Mr. Gutman. Yes.

Senator Breaux. Well, then we are just saying that Congress should have something to say in what is reasonable and what is not reasonable. Now we are letting bureaucrats determine whether the allowance is reasonable or whether it is unreasonable. If it is unreasonable, the current law says they should not allow it. Is that not right?

Mr. Gutman. Well, the service has the power to disallow the deduction for compensation that is unreasonable.

Senator Breaux. That is right.

Mr. Gutman. Traditionally, that has been used in the area of closely-held businesses to try to distinguish between dividends and what would otherwise be salary. But it is there. The authority is there.

Senator Danforth. I do not think that that is what he is saying current law is. I think what you are saying is that if you cloak a dividend --

what would be the tax purpose of doing that, incidentally? The business cannot deduct --

Mr. Gutman. It cannot deduct a dividend, and it can deduct salary.

Senator Danforth. It can deduct salary. So, if somebody is the sole owner and he is paying himself a huge salary, then they would say that that is a sham, really. Right? That is why you are allowed to deduct it.

But there is no argument in this case that this is a sham, is there?

Mr. Gutman. Well, it is a little more complicated than that, I think, Senator, because salary can, in fact, represent payments for lots of different things.

And the traditional notion of a currently deductible expense is an expense that provides a benefit within the accounting period that we are talking about.

If one could conceive of some of the salary that is paid to an executive as providing benefits beyond simply the current period, in which case, one could say that a portion of that ought not to be currently deductible, but ought to be capitalized and written off over some other period.

Senator Danforth. That, again, has nothing to do with this provision. This is an arbitrary amount, and this is saying that it is now the decision of Congress, after all of these years, that ordinary and necessary business expenses are only expenses up to a certain amount.

I mean, I have read all these stories, too, about these people who have companies that seem to be terribly managed, losing money right and left.

And, somehow, they have their Board of Directors going along with huge compensation packages. And we are all just very angry about it; I am.

Maybe I am wrong. Maybe this has nothing to do with tax policy. But I have been told for so long that it is terrible tax policy for Congress to begin picking and choosing what is ordinary and necessary, and what is not. And is this not a significant precedent, Mr. Goldberg?

Senator Packwood. Let me answer, if I could. It may be inconsistent, which is something that troubles us, but it is not a shattering precedent. We have limited to 80 percent the cost on meals and convention expenses now. And we have said beyond that it is not reasonable, and we cannot take it.

Senator Danforth. Maybe it is fine. I just raise the --

Mr. Goldberg. Senator, if I can begin by commenting on Senator Breaux's observation, the Internal Revenue Service does not have the authority to set reasonable compensation. Reasonable compensation has to affect market-level prices, and the IRS cannot arbitrarily pick it.

The IRS argues what the market-level of compensation is so it is a market-based determination, not an IRS fiat.

Senator Breaux. Let me comment on that, then get to the next point.

Mr. Goldberg. Yes, sir.

Senator Breaux. The IRS determines an allowance, not what it is, but whether it is reasonable or unreasonable. Because the current law requires you not to allow as a deduction a salary allowance that, in fact, is not reasonable.

Mr. Goldberg. But the determination of what is reasonable is by reference to what market conditions justify.

Senator Breaux. So, currently the IRS, no matter how much somebody is paid, the fact that they are getting paid that much is allowable?

Mr. Goldberg. If that compensation is a function of what the marketplace indicates is what the pricing would be for those particular set of services, that is correct. The Internal Revenue Service cannot disallow that.

Senator Symms. If the Senator would yield, I think where that takes place is like in small, family-held businesses.

And then the IRS will look at the audit every year and say, well, did Aunt Sarah really work, or can we justify that you paid her X thousands of dollars? The company does not pay any dividends. That is where that comes from; is that not right, Fred?

Mr. Goldberg. That is correct. But, again, it is all market-based, and Senator Danforth raises a very important question.

Senator Symms. Well, could I ask one other question, if the Senator does not mind my interrupting? If the Congress is going to do this and start interfering in between the stockholders, say, of Chrysler Corporation, and what they pay the CEO, and have us intervene, are we going to put income averaging back in for the years an executive works for a dollar-a-year, and then he gets a big pay-out once they turn the corner and make a profit, so they can spread that out over a few years?

Or do they just have to pay non-tax deductible income to an executive? Is that not the case in some of these packages? I recall Lee Iacocca worked for a dollar-a-year for several years. Then he did have some very high salaries. But how would that be treated in the future on this amendment?

Mr. Sessions. Senator, there is no provision for averaging here. It is just a year-by-year determination.

The Chairman. I think what you are saying here is a shot across the bow by the Congress, because of the concern of what they have seen in the way of some of the top executive compensation, as related to what we have had in the past and what you are seeing in other countries that are major economic competitors.

The Congress does have, as Senator Packwood said, the right to set some limitations. In this one, they have not denied the right for the corporation to put it just as high as they want to; they just stated that if you go over $1 million, you start losing your deduction for the excess.

Senator Danforth. Mr. Chairman.

The Chairman. Yes.

Senator Danforth. May I just follow through with one further question? I happen to believe that it is a very important concept in containing the cost of health care that we cap the amount that a business can deduct in providing very high-cost health care, particularly for top executives.

And I just wanted to clarify the precedent here. If we adopt this--which I have questioned--I take it that this would constitute a very solid precedent for the idea of capping the deductibility of health insurance payments. There would be no conceptual difference, would there?

Mr. Gutman. I do not know that there would be a conceptual difference, Senator. I think this is a determination that, as I see it, is one that is being made by the Congress with respect to what is reasonable under these circumstances.

Senator Danforth. But, I mean, if you are going to say that we can have dollar amounts on various types of compensation--cap them for deductibility purposes--if you can do that for one purpose, salary, you can do it for another purpose, namely, the value of health insurance premiums.

Mr. Gutman. You certainly could.

Senator Dole. Mr. Chairman.

The Chairman. Senator Dole.

Senator Dole. I think this is a political point being made in the bill. I read in the letter to Mr. Breadon, who is the Chairman of the SEC, saying, why do we not do it by giving more information to shareholders. They are the ones that are going to lose.

Let the free market forces work and not have government intervention. And steps are being taken by the SEC, because the shareholders are the ones that are going to pay the bill. We ought to make that compensation information available to them, and they ought to make that decision, rather than have the government interfere.

No doubt about it: some of the salaries are excessive. But are we in a position to judge some arbitrary limit what may happen in any corporation? Why not let the shareholders make that judgment at their annual meeting?

Senator Baucus. Would the Senator yield on that point?

Senator Dole. I think the SEC is moving in that direction.

The Chairman. Senator Baucus.

Senator Baucus. I am a little unsure whether the SEC really can solve this. A few years ago I used to work at the SEC. I used to review these proxy statements, particularly proxy battles.

And often the argument was, well, if somebody disagreed with the executive compensation being paid, well, just vote the shares for an alternative plan.

I can tell you, just based on my experience, that just does not work, for a lot of reasons. Number one, disclosure. Now, theoretically, the SEC could change its disclosure requirements.

Senator Dole. But they never do.

Senator Baucus. But, number two, most shares are held by institutional investors. They are not held by the average little stockholder who really is concerned about this. The trouble is, the system just does not allow that kind of remedy.

Senator Daschle. Mr. Chairman.

The Chairman. Yes. Senator Daschle.

Senator Daschle. We have probably talked about this long enough, but I do have a question of Mr. Gutman.

Mr. Gutman. Yes.

Senator Daschle. What amount of revenue does this actually generate?

Mr. Gutman. This is anticipated to bring in $1.5 billion through the five-year period, Senator.

Senator Daschle. $1.5 billion.

Mr. Gutman. Yes.

Senator Daschle. Well, all of these issues, it seems to me, are clearly tax expenditures. And we have to weigh carefully as to what kinds of tax expenditures we want to pay for.

It seems to me we have all given our deficit reduction speeches today, and we continue to give them on the floor. And the question is, can we afford $1.5 billion over the next year in the form of a tax expenditure to businesses paying executives more than $1 million a year?

If we can afford that, we ought to have a vote on it. We ought to discuss it. If we cannot afford it, if there are other priorities we can be spending that money on, we ought to discuss that.

As I understand it, there is no prohibition on anybody taking whatever income they want to. All I think this says, as far as the taxpayers are concerned, is we are not going to subsidize it beyond $1 million.

That does not seem to me like anything radical or anything we should be concerned about. We are saying we cannot afford to subsidize salaries over $1 million a year. I think it is appropriate tax law, and I am glad it is in the bill.

Mr. Gutman. Moving to the top of page three, the next provision is a provision that would expand the current law and the value of transit passes a month to extend that exclusion also to van pooling and certain park-and-ride benefits.

And, at the same time, to limit the exclusion for employer-provided parking, which is currently excludable in full to $160 per month. The next item, which is --

The Chairman. Just a moment. Senator Moynihan, for any comment.

Senator Moynihan. Mr. Chairman, may I just thank you for including this? This is a measure, basically, of transportation policy which we have been pressing for a decade, in legislation, since 1984. And it is very welcome and much appreciated.

The Chairman. Thank you. If you would go ahead.

Mr. Gutman. The next item is the repeal of the luxury tax on boats, airplanes, jewelry, and furs, and the indexation of the threshold for the luxury tax on automobiles, together with the imposition of a diesel excise tax on motorboats that are used for recreational purposes.

Senator Dole. Well, when does the present luxury tax expire on automobiles?

Mr. Gutman. 1999.

Senator Dole. And how much would it cost to have it expire now?

Mr. Gutman. It is about $400 million a year; so it is close to $2 billion through the window.

Senator Dole. And how much is indexing? You are going to index, right?

Mr. Gutman. Just a moment, Senator. $250 million through the window.

Senator Dole. And there is not enough

revenue available to include the repeal of the luxury tax on automobiles in the Democratic proposal. Is that correct?

Mr. Gutman. Not in this proposal, Senator.

Senator Dole. That is another thing we will want to look at the next time around.

The Chairman. All right.

Mr. Gutman. Finally, in this provision, there are three other expiring provisions that are dealt with in the Chairman's mark.

They involve the extension of general fund transfers to the Railroad Retirement Tier-2 Fund; the allocation and apportionment of research expenses between foreign and domestic sources, and the extension of the excise tax for certain vaccines for the Vaccine Injury Compensation Trust Fund.

Senator Packwood. Can I ask a question?

The Chairman. Yes, of course.

Senator Packwood. Mr. Gutman.

Mr. Gutman. Yes. I am sorry, Senator.

Senator Packwood. I want to ask a question.

Mr. Gutman. Yes, sir.

Senator Packwood. Is the only expiring provision not included the employer-provided legal plans?

Mr. Gutman. I believe that is correct.

Senator Packwood. Why is that?

Mr. Gutman. Oh. Also Section 29, Senator Packwood.

Senator Packwood. Section 29 is which, again? Refresh my memory.

Mr. Gutman. Non-conventional fuels.

Senator Packwood. And what is the reason for leaving out the employer-provided legal plan? Just a feeling that they were not worthwhile?

Mr. Gutman. Well, the principal justification for it was that there was not a demonstrated benefit from the existence of the program.

Senator Packwood. It is not a demonstrated benefit.

Mr. Gutman. That is correct.

Senator Packwood. What does that mean, exactly?

Mr. Gutman. Well, what that means --

The Chairman. Let me put it to you another way. There was very little support evidenced for it; very little.

Senator Packwood. Mr. Chairman, I am amazed.

I was advised by the unions--and this is basically a union issue--that were involved in this that any number of people were going to speak up for it.

But, at the moment, Mr. Chairman, I will not pursue it. I simply want to say to those who are pushing this that are listening, I want to say again to them what they have said to me about the support they have promised on the Democratic side on this that does not appear to be materializing.

Mr. Gutman. In the hearings that were held on the expiring provisions on the House side, Senator, there was not much support for this.

Senator Packwood. Nor apparently on this side either, when the mark-up was being made.

Senator Mitchell. Mr. Chairman.

The Chairman. Yes. Senator Mitchell.

Senator Mitchell. Might I ask a couple of questions --

The Chairman. Yes, of course.

Senator Mitchell. -- before we get to the tax provisions, which I assume is next on your list?

The Chairman. Oh. All right.

Senator Dole. We have not left Section 29 yet.

Senator Baucus. Are we still on expiring provisions?

Senator Mitchell. All right. If you have a question, I would yield, if you would like.

Senator Baucus. Do you, on expiring?

Senator Mitchell. No. I wanted to ask a question on payment for these various incentives and the differences in the two plans, if I might.

The Chairman. Certainly.

Senator Mitchell. Mr. Gutman, Mr. Goldberg, and perhaps Dr. Cohen, the tax provisions are included in the Chairman's measure as stated in part to achieve fairness in the Tax Code, and, in part, to pay for the cost of the various incentives through which we have now gone.

The President's priority plan, by contrast, includes seven incentives, all of which are included in some form in the Chairman's bill, but there are no corresponding tax provisions to raise the money to pay for them.

And I wanted to inquire, if I might, as to how that was achieved. As I understand it, there was first a difference in estimating the effects of the capital gains tax rate reductions; that difference being a little more than $17 billion.

The administration estimates that, over the five-year period, the capital gains tax provision will raise approximately $7 billion, and the Joint Tax Committee estimates that the same provision over the same period will lose approximately $10 billion. Is that correct so far?

Mr. Gutman. It is actually $12 billion we think it will lose, Senator.

Senator Mitchell. $12 billion. All right. Now, the other major difference, as I understand it, is with respect to the application of what is called accrual accounting the Pension Benefit Guaranty Corporation's operations.

And it is my understanding that the administration includes a figure of approximately $19 billion during the five-year period for that change, while the Congressional Budget Office and Joint Tax Committee provide zero for that amount.

So, there is a rather large difference in two areas. One is where they both turn out to be approximately $19 billion.

Now, I would like to inquire of you, Dr. Cohen, if you could explain to us how, by changing the accounting mechanism of the Pension Benefit Guaranty Corporation, the government will receive

$19 billion in the next five years.

First, my question is, is that money that the government will actually receive during that period of time?

Dr. Cohen. No, it is not, Senator. I think you have to make the reforms. That is how you get the money. Even with the reforms, Senator.

Senator Dole. That is with the reforms, yes. Now, I have read several statements by Mr. Darman to the effect that accrual accounting was recommended by outside experts concerned about the use of cash accounting in various accounts of the Federal Government.

And my understanding, upon inquiry, is that those recommendations were made as a prudent measure because liabilities were anticipated in future years in that account, and the concern was that we ought to be acting more cautiously than we were with respect to them. Is that correct, Dr. Cohen?

Dr. Cohen. That is correct, Senator. The liabilities would occur way in the future, and the suggestion to move to accrual accounting was based on the notion that we would be better able to see those liabilities if we reported them as part of our current year budget totals.

But the liabilities themselves do not actually occur within the window of the five years that we are considering in this budget period.

Now, what the administration has done, as I understand it, is as follows: they have said that there are liabilities that occur way out in the future, but we are going to show them now in the five-year window.

Then they come along and they have said, in step two, we are going to make some reforms which are going to reduce those future liabilities.

But since they have now transferred the accounting for those future liabilities into the current window, they are going to show those savings in the five-year window.

Then they have come along and spent the savings that they have just gotten from making changes that would affect future liabilities and they would spend it on things that have nothing to do with the PBGC, or any of the other accrual accounting mechanisms.

Senator Mitchell. Well, what will happen when those future liabilities occur?

Dr. Cohen. We will have to pay them. The money that will have ostensibly been raised and spent now will be gone. Any additional money that we have raised now through these reforms, we will have spent in this five-year window, and we will still have the same liabilities out in the future. We will be facing those when we get to that time.

Senator Mitchell. I know this is all very complicated accounting discussion, but let me see if I understand the simple concept.

Do I understand you, Dr. Cohen, to be saying that the government will not, in fact, be receiving $19 billion in cash during this five-year period?

Dr. Cohen. That is exactly correct, Senator.

Senator Mitchell. So, the $19 billion that will be spent during this five-year period to pay for these incentives, where will that come from?

Dr. Cohen. That will be borrowed, Senator.

Senator Mitchell. So, that will be an increase in the deficit.

Dr. Cohen. That is correct.

Senator Mitchell. And, as I understand what you said, Dr. Cohen--and please correct me if I am wrong--the original purpose of moving to accrual accounting was to, as an additionally cautious and prudent measure, prepare for future liabilities.

Dr. Cohen. That is correct, Senator.

Senator Mitchell. The effect of its application in this case is to increase the deficit now, or in this five-year period by that amount, and, when those future liabilities do occur, to then have to meet those liabilities in some other way, since the money, the ostensible savings, will have been used for this purpose now.

Dr. Cohen. That is correct, Senator. Right.

Senator Chafee. Mr. Chairman.

The Chairman. Yes. Senator Chafee.

Senator Chafee. I am mixed up. Is he describing a bill before us?

Senator Mitchell. No, he is not.

Dr. Cohen. No, I am not.

Senator Mitchell. He is describing the President's bill.

Senator Chafee. I thought you might be. Why do we not restrict the discussion to the bill that is before us?

The Chairman. Well, I had not noticed that that had been the case so far, but we had moved from it from time to time. Yes.

Senator Mitchell. Mr. Chairman, might I

respond to that?

The Chairman. Yes, of course. Yes.

Senator Mitchell. I can understand the Senator's reluctance to want to discuss the President's package, but the fact is, there has been a great deal of criticism by our Republican colleagues of the tax increases in here, and there has been a great deal of criticism of any measure that would increase the deficit.

And, so, if there were, in fact, a way to come up with $19 billion in the magical manner in which our colleagues' support has done, then we might want to adopt that.

Senator Chafee. I think you are generous in using the term "your colleagues supporting." Certainly I am not on the President's bill.

Senator Mitchell. Well, that is --

Senator Chafee. And I am not sure all the rest of us are. We have got a bill before us which we think is a very bad bill. If you can purify it in some way and enhance it, go to it.

Senator Mitchell. Well, I had hoped that we could fine $19 billion as painlessly as it appeared. But now it looks like it is not really there. Is that correct, Dr. Cohen?

Dr. Cohen. That is correct.

Senator Mitchell. Yes. So, I wanted to make the point that the tax increases in here are necessary to meet the incentives and the Senator from Rhode Island was sharply critical of the Chairman's bill this morning on the grounds of the deficit. But the Chairman's bill does not increase the deficit; the President's bill does.

So, I think it is important that we understand that. I thank Dr. Cohen. I think I should give Mr. Goldberg an opportunity, if Dr. Cohen has misstated anything with respect to the President's proposal, to rebut or respond to it.

Mr. Goldberg. I am debating over the issue of discretion, Senator. I guess a couple of comments. One, it is gratify, if I construe your remarks properly, that you do support both the change to accrual accounting and the accompanying reforms to the PBGC rules.

Senator Mitchell. You have not construed my remarks correctly if that is your conclusion.

Mr. Goldberg. But if they are so painless, I do not understand. The second point is that, viewed from a broader perspective, the administration's budget does include $90 billion in reduced spending and cuts. It also includes an overall freeze in domestic discretionary spending, and a lot of that is very real. I think as you, and a number of your colleagues pointed out this morning, it is important that we do come to terms with those issues for all of our sakes.

Senator Mitchell. Thank you. I thank you, Mr. Goldberg.

Senator Dole. Mr. Chairman.

The Chairman. All right. Yes. Senator Dole.

Senator Dole. I do not dispute what Dr. Cohen has said, or the Leader, but I want to analyze that further and maybe make a statement later. But there are not any savings whatsoever from changing the accounting, right?

Dr. Cohen. That is correct.

Senator Dole. It is all going to come from programmatic changes; under-funded liabilities and things are going to be done.

Dr. Cohen. The reforms would make changes which might reduce future liabilities, but they will have no savings during the five-year window that we are considering in this bill.

Senator Dole. And the future liabilities have been estimated at about $30-45 billion.

Dr. Cohen. That is correct.

Senator Dole. And you get sort of the rosy scenario if you use cash accounting; correct?

Dr. Cohen. Well, I think some of the experts, Senator Dole, have suggested that you use both sets of accounting.

That is, you continue the Federal budget on a cash basis, but that you provide the information that accrual accounting provides as a supplementary set of information so that you can see exactly where the long-run status of the Pension Benefit Guaranty Corporation is.

We do the same thing with the Social Security system. We look at its effects on a five-year window, but we also, of course, employ the 75-year actuarial estimates from the Social Security actuaries.

So, the two sets of information are complimentary and one is not to be necessarily used exclusive of the other, but to substitute the accrual accounting for cash accounting during the five-year window does create some situations which some analysts have had some concerns about.

Senator Dole. But I imagine there are some who have not have concerns about it. There are always a lot of analysts, right? You get analysts --

Dr. Cohen. Well, the Congressional Budget Office has written a letter in which they said we should not adopt this accrual accounting for the period of the budget window.

Senator Dole. But, I mean, that is a judgment call that OMB might differ with, right? I mean, analysts are analysts. They might have different views.

Dr. Cohen. Well, I assume that OMB has a differing view, since they handled it this way.

Senator Dole. Well, we will get back to this the next time around in a couple of weeks.

(Laughter)

Senator Dole. But I wanted to ask about Section 29, which I thought was a pretty good provision, which expires December 31, 1992, as I understand it.

Has that credit not been extended, is that what I --

Mr. Gutman. That is correct.

The Chairman. That is correct.

Senator Dole. And what would the costs be of extending that credit for one year?

The Chairman. Approximately $1 billion, as I recall.

Mr. Gutman. One year is $1 billion, and permanently it is $3 billion.

The Chairman. Yes.

Senator Dole. $1 billion for one year?

The Chairman. Yes.

Mr. Gutman. Yes.

Senator Dole. So, the point is, it is not extended in the Chairman's mark. Right?

Mr. Gutman. It is not; that is correct.

The Chairman. Will you proceed, Mr. Gutman?

Mr. Gutman. Thank you, Mr. Chairman. I would now like to go through the tax provisions at the bottom of page three quickly.

Senator Packwood. What happened to the simplification?

Mr. Gutman. I was going to go back to that, Senator Packwood. I was going to do simplification and Taxpayer Bill of Rights last.

Senator Packwood. When we get to it, I have a question about airline pilots.

Mr. Gutman. The provisions involving tax increases are at pages 69 and following in the material. Basically, the Chairman's mark provides the addition of a fourth individual income tax bracket at a 36 percent marginal rate to begin at taxable income of $150,000 for single individuals; $162,500 for heads of households; and $175,000 for joint returns.

In addition to that, a ten percent surtax on the tax attributable to taxable income in excess of $1 million is proposed in the mark.

Also, the mark proposed to extend permanently the present law of personal exemption phase-out and itemized deduction limitations.

Senator Moynihan. Mr. Chairman.

The Chairman. Yes. Senator Moynihan.

Senator Moynihan. Could I just ask that we not pass by too quickly this provision three, which extends permanently the personal exemption phase-out and the itemized deduction limitation.

This was adopted a few years ago, at the proposal of Mr. Pease. And it is, in fact, a 1.93 percent increase in the income tax rate, is it not, Mr. Gutman, for the persons in that category?

Mr. Gutman. It is, for the persons who are affected by it. That is correct, Senator.

Senator Moynihan. Yes. We are going through a great deal of attention to the proposal to increase the top bracket to 36 percent, but we have increased for these persons the 30 percent bracket to 31 percent.

Senator Bradley. This is the return of the bubble.

Senator Moynihan. This is the return of the bubble.

Senator Bradley. The return of the bubble.

Senator Moynihan. And you are going to love it when you make it out. It is a ten-step process in the 1991 Tax Code. It was adopted as a two-year provision, was it not, Mr. Gutman?

Mr. Gutman. It was a five-year provision, Senator.

Senator Moynihan. A five-year provision. I am sorry. And now this makes it permanent.

Mr. Gutman. That is what the proposal is.

Senator Moynihan. And the monies that will come in -- this is, of course, moving to limiting the deductibility of State and local taxes. This limits school taxes, charitable deductions. That is right, is it not?

Mr. Gutman. Well, that depends on how you look at it. I think it could be described just as accurately as you did as simply a rate increase.

Senator Moynihan. Well, it is a rate increase that comes about in consequences of the inability to deduct --

Mr. Gutman. Any of the itemized deductions which it covers. That is true as well.

Senator Moynihan. Yes. I wish this were not made permanent, and I do not know why it was made permanent. We had a five-year provision to bring in some revenue, but now, as the Senator from New Jersey says, we have this bubble.

And the income is not that high for two-income families. And the next thing you know, you have your school taxes, and you cannot itemize them. Do you remember the bubble? Not bubbles, bubble.

Senator Bradley. In the 1990 bill we just moved the bubble a bit. It just floated a little bit. It is still there.

Senator Moynihan. I do not think that Mr. Gutman is disposed to expand in any great length on this subject. I do not blame him. But I would call it to our attention that we are making permanent what is, in fact, a new tax rate. I do not ask for you to comment on that, certainly.

The Chairman. All right, sir. If you would proceed, Mr. Gutman.

Mr. Gutman. The next item is a provision that would conform the book and tax accounting for those companies which have securities in their inventories.

Taxpayers who hold securities as inventory would be required to include the value of those securities at their market value for Federal income tax purposes, which is the current treatment that is required of the securities dealers for book purposes.

Senator Moynihan. Mr. Chairman.

The Chairman. Yes, of course.

Senator Moynihan. Could I just say that, as little as I appreciate this appearing in the Tax Code at all, I appreciate your delaying it for a year. How is that?

The Chairman. At the moment I will settle for that.

Mr. Gutman. Item five in this proposal involves making permanent the corporate and individual estimated tax changes that were enacted in the last session and at the beginning of this session involving corporate and individual estimated taxes that were otherwise meant to expire in 1995.

And the final provision involves extending the 45-day processing rule that allows the Internal Revenue Service to process a tax return and give refund checks that is presently applicable to income taxes, to all other taxes, as well.

Mr. Chairman, that completes the principal parts of the mark, with the exception of simplification provisions and Taxpayer Bill of Rights.

The Chairman. Just a moment. Yes. Senator Danforth.

Senator Danforth. Mr. Chairman, I would like to return to the principal item, which is the tax credit, and just make sure I understand the rationale for it, because we did pass over it pretty quickly.

And it is, by far, the largest item in this tax program. It is over half the total cost of the bill, and it is something like four times the next largest item in the bill, and I think we brushed over it pretty quickly at the beginning of the proceedings.

So, let me just see if I understand it. First, this is a credit available per dependent child.

Mr. Gutman. Per child under 16, Senator.

Senator Danforth. Under 16. So that the initial issue is, what is the rationale for it being a credit for children, as opposed to a credit that is available for taxpayers? I mean, there must be a rationale for that.

The Chairman. Let me speak to that one then. The reason for it is this: as we did the study, what we have seen from the economists, those people who have been the hardest hit over the last decade are the middle-income families. Median income in this country is $35,000 for a family.

These people with children had the toughest time of it: the cost of rearing children today; providing for children; the loss of discretionary time--some 40 percent loss over the last 10-15 years--making it more and more difficult; we had a limited amount of resources within the limitations of the Budget Agreement of 1990.

This is where we thought we could get the most impact in trying to help those who had had the most difficult time. Their taxes went up, and their incomes went down.

So, this is an allocation of some $300 tax credit per child. Not an increase in the personal exemption that gives more to that person that has the higher tax rate, but a $300 credit to each of them. If you take an average family of four where they make $35,000 a year, that $600 is a 25 percent tax cut for them. That is meaningful, and that is permanent. That is put into the tax structure.

So, that means that that child, over the next five years, and that family, is going to have about -- how much?

Mr. Sessions. $9,000 over 15 years.

The Chairman. Yes. Is going to have that kind of a credit. And it is a meaningful credit. That is why it was put together. And it does represent approximately a half.

The problem you get when you are dealing with middle income is there are a lot of folks, and it is an expensive process. To say that this is going to give a great impetus to the economy, no, I do not believe that. But I do think it makes a step in the right direction of fairness.

During that same period of time, you have seen people in the top seven-tenths of one percent have a substantial increase in income and a substantial reduction in taxes. So, that is what it is addressing.

Senator Danforth. Well, I am not, for the moment, going to argue the 36 percent on the top. I just wanted to understand the reason for this particular proposal.

As I understand it, it begins phasing out at $50,000.

Mr. Sessions. That is correct, Senator.

Senator Danforth. Is that for an individual, or for a joint return?

Mr. Sessions. It is all returns.

Senator Danforth. For all returns. So, if you had a two-earner family; husband and wife, and between them they made $50,000, then the credit would start phasing out at that point. Right?

Mr. Sessions. That is correct.

Senator Danforth. And it would be gone entirely by the time they are at $70,000.

Mr. Sessions. That is correct.

Senator Danforth. How much of that would be available, say, at $60,000? Would it be about half of it?

Mr. Gutman. Half.

Mr. Sessions. Half.

Senator Danforth. Half of it. So, it is a rateable reduction.

Mr. Sessions. That is correct.

Senator Danforth. Now, for the low-income people, this is not a refundable credit.

Mr. Gutman. That is correct.

Senator Danforth. Approximately what level of income for a two-earner family would it be in a typical case, do you know, where the full $300 credit would be available? For the typical family, how high would their income be before they got the full $300 per child?

Mr. Foley. A family of how many children?

Senator Danforth. Two kids.

Mr. Foley. It would be a little over $15,000 a year.

Senator Danforth. A little over $15,000 before they got the full amount. Now, if they had incomes of under 15, they would get less than that?

Mr. Foley. That is correct.

Senator Danforth. And pretty soon they would be getting nothing at all. Right?

Mr. Foley. That is correct.

The Chairman. Now, if I may respond to that, Senator, because that was a serious consideration of what we are trying to do here. What we did in the last tax bill, we went a long way in trying to address the concerns of the working poor--talking about people under $21,000 a year--and we provided an expansion of the earned income tax credit of $18.3 billion.

In 1990, you had $953 as the maximum amount that a family could receive under the earned income tax credit. Now, with the modifications in the Chairman's mark, the basic credit will be increased to approximately $2,200 in 1994.

Now, that is an increase of 230 percent over five years, and it is directly targeted to the working poor. Now, if they have purchased health insurance, then they are eligible to receive another $525 a year.

Now, you combine those amounts and you have an increase of more than 290 percent over four years. So, we have gone a long way in trying to address your concerns.

But the people we did not take care of was middle income. They are the ones that took the hit. And that is why this one is structured as you see the phase-in of the earned income tax credit, which is not all there yet. But, as that is being phased in, then this is being put in for the middle-income folks.

Now, if you take the quintals and you take the middle quintal, you are talking about something between around $29,000 to $42,000. A median-income family is $35,000. So, that takes care of that quintal.

The next quintal is $42,000 to about $62,000. This starts the phase-out at $50,000. They get it till they get to $50,000, as I understand. And then it starts phasing out up to $70,000.

One of the criticisms, Senator, was that it was going to too many people at higher incomes, so you have limited resources that have been specifically targeted to middle income folks up through the next-to-the-last quintal.

Senator Danforth. Well, now, if it is the $39,000, is that the median?

The Chairman. $35,000.

Senator Danforth. $35,000. What is this worth to a $35,000-family?

The Chairman. To a family of four --

Mr. Gutman. It is worth the same thing.

The Chairman. Right.

Mr. Gutman. It would be worth $300 per child.

The Chairman. The average family of four, with two children, $35,000; that is a 25 percent tax cut.

Senator Danforth. And if it was a two-earner family and one of them lost a job, they would lose the credit.

The Chairman. No.

Mr. Gutman. No, that is not the case, Senator. This is a credit that is based on the number of children the family has.

Senator Danforth. Yes. But if the income goes down, you lose your credit.

Mr. Gutman. Well, if the income is down below the levels where the credit is available, that would be the case. Yes.

Senator Danforth. All right. Now, let me ask you this. Why do you cut it off at age 16?

The Chairman. It is a matter of cost. You do not have enough money to do it more than that. And at the age of 16, some children start to work. But you run out of money in trying to carry it anymore.

Senator Danforth. We do not want to say, do we, that we, in effect, believe that we are going to support people with kids up to the age of 16, and then the kid has to fend for himself. I mean, that is not the policy, is it?

The Chairman. No. But at the age of 16, Senator, some of us started doing summer jobs to supplement income, and that is still being done by lots of folks.

Senator Danforth. So, that is the theory.

The Chairman. That is the theory where we have a limitation in resources and you are trying not to increase the deficit.

Senator Dole. Mr. Chairman.

The Chairman. Yes.

Senator Dole. Can I just ask, how do we phase out the child care credit? Where does it start, how much is that, and where does it stop?

Mr. Sessions. It is not phased out.

Senator Dole. They get that regardless of --

Mr. Foley. But after you reach $30,000, the maximum amount you can get is about $480 for the child care credit.

Senator Dole. The maximum amount who can get?

Mr. Foley. The maximum amount that a family could get.

Senator Dole. What if they had a $100,000 income, would they still get child care credits?

Mr. Foley. They could still get the child care credit.

Senator Dole. Why?

Mr. Foley. You are in a better position to answer that question than I am. That is a policy decision that was made.

Senator Dole. You are going to cut these people off at $70,000, but if you make $200,000, you still get the child care credit. Right?

Mr. Foley. That is correct.

Senator Dole. Or $300,000.

Mr. Foley. That is correct.

Senator Dole. You might find some more money there, Mr. Chairman.

Senator Grassley. Mr. Chairman.

The Chairman. Yes. Senator Grassley.

Senator Grassley. Pretty much related to a discussion that has just been on here with the last two people, I would like to ask your philosophy, or the committee's philosophy, or wherever it came from, the staff, the rationale for doing away with the young child tax credit.

My interest in this is I have had legislation in to expand it. It is a bipartisan deal. Senator Lieberman has legislation in to expand it. A lot of pro-family groups support expansion of it.

It seems to me that, by doing away with this, we are raising taxes on low-income families with children under one year of age. This would be families, primarily, where one spouse wants to stay home and take care of the children, and it only goes to families with incomes under $22,000 a year.

Could I have an explanation on the reason for doing away with that?

The Chairman. I am sorry. I was engaged in conversation, if this is addressed to me.

Mr. Foley. One of the reasons was that, under current law, there is a very small differential between a family with one child and a family with two children. Under current law, that differential is between $40-$60.

So, by eliminating the Wee Tot credit, we were able to put more money into the credit for families with more than one child. And, as a result, we have been able to increase that differential so that it exceeds $200 now.

Senator Grassley. Well, you could not have helped the same families and preserved the philosophy by changing the young child tax credit some other way, rather than doing away with it entirely?

Mr. Foley. I am not quite sure I understand your question.

Senator Grassley. Well, you are telling me you did away with it because there was little difference between families with one child and families with two children.

But, but doing away with it, you are raising the taxes on families with one child, and these are low-income families that are under $22,000-a-year income.

Mr. Foley. Well, one of the things that we are trying to do was, as I mentioned before, was increase the differential for larger families. There is a tax policy rationale for providing a larger subsidy to families with more children, and this is merely one of the ways to accomplish that.

In addition to eliminating the supplemental credit for children, the Chairman's mark also adds an additional $1 billion to the earned income tax credit.

Senator Grassley. I will bring it up later on.

Senator Rockefeller. Mr. Chairman.

The Chairman. Yes. Senator Rockefeller.

Senator Rockefeller. I would like to say something in defense of the Chairman's mark that the Chairman understands very well, and I have expressed this opinion before, that refundability, I think, is a very strong concept.

And it is something that I strongly believe in, but it is not in the Chairman's mark, so that is what we are deciding on. And I think anyone who underestimates the power and the meaning of a tax credit such as in the Chairman's mark is crazy.

You are talking about families now that are working harder; both parents are working. They are making, between them, less money than one of them was making 10-15 years ago. And the idea of a tax credit, even though it is non-refundable, is an enormous help.

I mean, a $300 tax credit, for example, is going to be equal to half the cost of the health care for a child in its first year. And you can start measuring what $300 means to an individual family, or with two or three children, if you start adding that up, it has a tremendous significance.

And in the two-out-of-three families that do not have children in this country, it is also targeted, and, therefore, looks very much at the future of this country.

It is a very direct investment in the future of this country. People do not realize that it takes $6,000, on average, a year, to raise a child--each year; each child.

So, this kind of help is strongly understood by families out there to be what they need. It does not answer all their problems, but it is in the direction of what they need.

The Chairman. All right. Please proceed, Mr. Gutman.

Mr. Gutman. Mr. Chairman, the balance of the mark contains two simplification titles. One, involving employee benefit simplification. The pension simplification provisions that are included in your mark are substantially similar to the provisions that were contained in S. 1364, which was introduced last year by Chairman Bentsen and Senator Pryor.

The effective dates of the provision of the introduced bill have generally been delayed for a year, and, in addition, there are a number of proposed modifications that are detailed in the mark-up document. The mark-up document is JCX 5-92.

The Chairman's mark also contains provisions --

Senator Pryor. Mr. Chairman, may I interrupt there?

The Chairman. Yes. Senator Pryor.

Senator Pryor. I want to thank you, Mr. Chairman, for including this pension simplification in this particular piece of legislation.

This is something that has been long, long awaited; especially by the small business community. I applaud your leadership, I thank you for making it a part of this bill, and I hope it will receive the unanimous support of this committee. Thank you, Mr. Chairman.

The Chairman. Thank you very much.

Senator Boren. Mr. Chairman, I want to join in that, as well. I think this is a very important contribution, because we have had so many people in small businesses that have not had the opportunities to have pension and retirement programs. This will make that possible.

It will also make it possible when they leave some of those businesses for them to roll them over into IRAs and other kinds of saving devices. I think this is a very important contribution, and I want to join with Senator Pryor in saying it is a very important small business initiative.

The Chairman. Thank you, sir.

Senator Packwood. Are you about to explain the whole thing?

Mr. Gutman. No. I have done the explanation that I intended to do, Senator Packwood.

Senator Packwood. Well, then let me ask you about the next-to-the-last one on extending the present law treatment of plans maintained for union pilots to plans maintained for non-union pilots, and what is the reason for that?

Mr. Gutman. I am sorry, Senator. Could you ask me that again? I was distracted.

Senator Packwood. On page 16 of this proposed simplification, JCX 5-92, is a modification that reads as follows: "Extend the present law treatment of plans maintained for union pilots to plans maintained for non-union pilots who are employed by one or more common carriers," and whatnot.

And the reason I ask this, is I want to make sure I understand the law. At the moment, an employer has to offer the same retirement plan to all employees, but there is an exception for collectively bargained plans.

Mr. Gutman. That is correct.

Senator Packwood. And the reason being that the assumption is that the unions are pretty well going to watch out for themselves and they are not going to discriminate among their members, and, therefore, there is no need for that protection.

Mr. Gutman. That is correct.

Senator Packwood. And that is the reason for the exception. But the reason we do not allow it otherwise is because we are afraid that employers might start discriminating among different classes of employees, and, therefore, we give them the protection of non-discrimination.

As I look at it here, it almost looks like a rifle shot, to me, for one company. And that you are going to say to this company may extend to its pilots--not doctors in hospitals; not nurses--can have a pension plan that will discriminate between the pilots and the other employees in that business.

Mr. Hardock. Senator, if you do not mind if I answer, I think you have accurately described the treatment of collective bargain plans under discrimination rules.

This provision really deals with a separate set of rules. The pension rules have a series of exceptions for pilots. The unique nature of that profession has led, over the years, to the adoption of different rules.

They have earlier retirement ages that need to be taken into account. Most of those rules apply to all pilots. There is one rule--this particular coverage rule--that is currently drafted only to apply to union pilots.

All this does is makes the treatment of pilots throughout the pension rules consistent. It is a proposal that was included in Mr. Rostenkowski's simplification bill in June, and is in the House proposal.

Senator Packwood. Well, when you say

uniform, not really. It allows an employer who is a non-union employer to treat its pilots differently than its other employees.

Mr. Hardock. In the same way that that same employer, if he had union pilots, could treat his union pilots differently from his other non-union employees.

Senator Packwood. Well, yes. To the extent that you have different unions, you can bargain with different unions. But that is true of many employers that have half a dozen different unions.

You do not necessarily in that case have to have the same pension plan for every employee, as long as they are collectively bargained.

Mr. Hardock. That is clearly the case. That is accurate. May I also respond, you mentioned that Senator Bentsen has long told staff that rifle shots are inappropriate in legislation he would introduce.

We have explored this, and this would affect a large number of airlines; essentially, indirectly all airlines, because even airlines that have union plans would be affected. But there are a large number of non-union airlines that would be directly affected by this.

Senator Packwood. Is there any money involved in this?

Mr. Gutman. Negligible, Senator.

Senator Packwood. And does it really make the law any more or less simplified?

Mr. Hardock. Certainly for the people directly affected it would simplify the law. They would not have to deal with this one particular rule. To what extent, I think, is a question --

Senator Packwood. My hunch is you would have a hard time making the argument. It simplifies it so much that there was a complexity they could not grasp until this was passed.

I think when we get to the floor, Mr. Chairman, this is one I am going to offer an amendment to simply knock out. There is no money involved, and, frankly, simplification is not the issue.

Senator Chafee. Mr. Chairman.

The Chairman. Yes. Senator Chafee.

Senator Chafee. Mr. Chairman, if I could refer the staff to page ten of this special ERISA section, and Section Six at the bottom, "Treatment of Governmental Plans."

If I understand this correctly, what we are doing is saying, once again, that all the laws that apply to private businesses that we levy on private businesses, we then go on to provide an exception for State and local governments.

And, you can correct me if I am wrong, but, as I understand it, there are very strict limitations on how much a pension can be in private industry in relation to the salary that was paid prior thereto. But, as far as State and local governments go, we, once again, provide an exception.

And I have great difficulty understanding that. I presume that it derives probably from the fact that legislators frequently work at a relatively low salary and then proceed to vote themselves very generous bonuses or pensions.

And they want to be exempt from the ERISA laws that apply to private industry, and throughout the rest of the nation. Am I correct in that?

Mr. Gutman. Well, I am not sure that the characterization would be shared by all, Senator Chafee. We were aware of situations in which State legislators were working for small amounts--you are exactly right--and the States did want to pay them a decent retirement allowance.

Senator Chafee. Or they wanted to pay themselves a decent retirement allowance.

Mr. Gutman. Well, if they are the ones who are voting it, I guess that would certainly be true. And in that situation there was certainly a lot of interest in the House in providing for a pension benefit for these people who had served in the legislatures for long periods of time at amounts that could exceed the smaller amounts that they were receiving while they were in the legislature.

Senator Chafee. Well, Mr. Chairman, I have great difficulty understanding why we proceed this way. In my State, the salaries are set by the constitution and the voters every year turn down any change to that constitution.

So, currently, they receive $5.00 a day for 60 days per year. And they have proceeded to vote themselves generous pensions that are far in excess of these limitations.

And if we apply this law to all private industry, why should we make it different for States? I mean, Mr. Chairman, it seems to me that this is what infuriates the public.

They constantly are receiving that we are levying on industry and private businesses certain requirements, and then we exempt either ourselves, or the rest of those in government from those very requirements. And this is that.

The Chairman. Thank you, Senator.

Senator Chafee. Well, Mr. Chairman, I would like a little explanation. I appreciate being thanked --

(Laughter)

Senator Chafee. -- but I would like a little understanding of why we were doing this.

Mr. Hardock. Senator, I can try, if you do not mind. I think this is a provision that has the strong support of all the major State and local government groups. It is not a provision that particularly helps State Legislatures or anyone else.

As a matter of fact, the most vocal proponents have been policemen and firemen. One of the reasons is that many local government employees do not have to pay F.I.C.A. tax, Social Security tax, and do not get Social Security benefits.

The result is that their pensions tend to be more generous because they do not have Social Security to rely on, and it is much easier for them to get closer to the 100 percent of compensation cap.

At that point, if they get a cost-of-living adjustment, they can conceivably go over the cap. That results in disqualification of the plan under the technical rules of Section 415 and could cause taxation of all benefits of all State and local government employees, no matter what their income level.

This proposal is a proposal that governments have put a great deal of work in. It is in the House bill, and solves the problems without repealing the overall cap on Section 415 that applies to all plans.

There is a maximum amount of tax-qualified pension that can be earned under a defined benefit plan, and that applies to public and private plans. And this proposal does not affect that.

Senator Chafee. Well, does this remove all limitations?

Mr. Hardock. No, it does not.

Senator Chafee. I mean, for this particular group.

Mr. Hardock. No, it does not. It retains the maximum pension cap that is a flat dollar amount of the benefit that can be earned under a qualified plan, and that is the same cap that applies to public and private plans.

As a result, for example, you could not earn, under a private pension plan, a $150,000-a-year pension benefit. You could also not earn $150,000-a-year pension under a public plan.

Senator Chafee. Well, Mr. Chairman, I would look forward to further understanding of it, and I have great trouble proceeding with these exceptions.

The Chairman. All right. Senator Dole.

Senator Dole. I wonder if I might ask Mr. Goldberg, do you have any comments on these last provisions--the simplification provisions.

Mr. Goldberg. Yes, Senator. The administration has historically opposed the provision that Senator Chafee is referring to on the grounds that no case has been made for special treatment of this particular class of employees.

Senator Dole. I know you have not had time to fully analyze the package, but I am wondering if there would be an objection to giving the administration an opportunity to analyze this package and provide for the record any comments they might wish to make.

The Chairman. Senator, we were given a deadline by the President on this of some 50 days.

Senator Dole. It would not hold up the bill.

The Chairman. I would be delighted to have them analyze it, but I want to proceed with the mark-up here in the committee and do our utmost to try to beat the time schedule as set forth by the President.

In the meantime, we will be delighted to have the analysis of the administration for the discussion on the floor. Have we completed your presentation?

Mr. Gutman. There are two more small items, Mr. Chairman. The Chairman's mark also contains provisions that are substantially similar to S. 1394, the simplification bill that was introduced jointly by Chairman Bentsen, Senator Packwood, Chairman Rostenkowski, and Mr. Archer.

Modifications to, and deletions from that introduced bill, as well as a number of additional items, are set forth in JCX 8-92, which you have in front of you. I would particularly call your attention to the simplified payroll deposit regime, which is described at page 58 of that document.

Finally, the Chairman's mark contains 29 provisions that are designed to protect the rights of taxpayers and provide them with procedural safeguards in their dealings with the Internal Revenue Service. These provisions are the Taxpayers' Bill of Rights--the second version of that.

Senator Moynihan. Mr. Chairman, before we go to the Bill of Rights, I believe it is understood, on page 22, item K, that we might have some report language that would ask the Treasury to study the appropriate treatment of repurchase and reverse repurchase transactions. Is that agreeable to you, sirs? I believe it is.

The Chairman. Can I have a comment out of staff on that? We do not have a problem with that, do we?

Mr. Sessions. With regard to a request to a study, there is certainly no objection to that.

The Chairman. We have agreed to that, have we not?

Mr. Sessions. Yes.

Senator Moynihan. Thank you, Mr. Chairman.

The Chairman. All right. Is there further discussion? Are there amendments?

(No response)

The Chairman. If not --

Senator Bradley. Mr. Chairman.

The Chairman. Yes.

Senator Bradley. I would like to offer one amendment.

The Chairman. All right.

Senator Bradley. This is an amendment that deals with the issue of refundability. I do not think that we should move ahead with a bill that does not have refundability in it, or at least make a run at it.

Presently, the child care credit does not cover 25 percent of the children, and I believe that it is important that we at least have a vote to determine whether we want it to be refundable. It is an expensive item. To make it refundable costs about $22.6 billion.

That would cover all children in all families, up to the income level of $70,000. And the Chairman has been explicit in his determination that this be revenue-neutral.

And so, working from within the context of the bill itself, I would propose to pay for the refundability of the children's tax credit by eliminating the provisions that relate to passive losses; eliminating the provisions that relate to the ten percent investment tax allowance; the AMT tax relief that goes to depreciation and intangible drilling costs; the capital gains provision, and the first-time home buyers' credit; and the extenders related to mortgage revenues; small issue manufacturing; business energy credits; and the IRA restoration.

I would also propose that this credit, which is extended to someone to is one welfare, that one-half of the refundable credit be counted as income on the eligibility for welfare.

Mr. Chairman, I know that we have talked about this. I believe it is very important to make at least the effort to make sure that all children are covered, and I would propose to offer this amendment.

The Chairman. All right, Senator. The question has been discussed somewhat before, but let me readdress it. I understand the desire of the Senator.

But what we have done here, once again, is trying to address something that was not addressed in the 1990 tax bill; where we did something very major about earned income tax credits, to get to those below $21,000 worth of earnings a year.

We put in there $18 billion plus--$18.3 billion, as I recall. That is now being phased in. In 1990, you had a $953 maximum credit for a family under the earned income tax credit.

With the modifications in the Chairman's mark, that basic credit will be increased to nearly $2,200 in 1994. That is now being phased in. Now, that is an increase of 230 percent over five years, and it is targeted directly at the working poor.

Now, if they purchase family health insurance in addition to that, that picks up another $525. Now, you put those together and you have had an increase of over 290 percent over four years.

We have not neglected them; we have expanded that program very substantially and gone a long ways to addressing those kinds of concerns. We have made major modifications to the credit to make it easier for individuals to qualify for the EITC.

But we have neglected middle-income. And these surveys show that they are the ones hardest hit; that their taxes went up and their incomes went down; that they are taking extra jobs; that you have more of both parents working than every before in the history of our country; that you have had more people taking a second job than ever before in the history of our country; that you have had them increase their work hours to the extent that it adds up to another full month of work a year. That is what has happened to middle-income folks.

Now, to stay within the confines, the parameters of the budget agreement to see that we do not add to that deficit, we have just so much in resources we can use.

So, we have tried to meld together the working poor with something that now phases in for middle-income people. And I think it is a reasonable package to put together.

Now, as opposed to that, he is talking about withdrawing all of those things that are in the President's package, virtually, insofar as trying to encourage investment and create jobs in the country, and we have put that in here.

I think that would be a very serious mistake, and I would urge the defeat of the amendment.

Senator Rockefeller. Mr. Chairman.

The Chairman. Yes.

Senator Rockefeller. I am going to support the Chairman on this, and I am going to vote against Senator Bradley's amendment, even though I have spent the last two-and-a-half years and have been across the country fighting for an income security policy.

Based upon the refundable tax credit, earned income tax credit, child support enforcement, and minimum assured benefit involving $25 billion in the private economy, which, together with the minimum wage would lift the overwhelming majority of families in this country who are in poverty out of poverty and help every single family in this country immeasurably.

I fought hard for refundability, and I used every occasion that I could. It is not in the Chairman's mark. I am, perhaps, more sensitive than some others as to the Chairman's mark, and I am mindful of that.

Senator Bradley is correct on the merits, but to underestimate what Chairman Bentsen has done in terms of opening up the idea of a tax credit for children--not a blind middle-income tax cut hand-out, but a focused, targeted child tax credit for families that are struggling to make it in this country--I think, is wrong. And for that reason I will support the Chairman.

The Chairman. Thank you. Are there further comments?

Senator Bradley. Mr. Chairman, if I could.

The Chairman. Yes. Senator Bradley.

Senator Bradley. You made reference to the bill in 1990 as taking care of low-income Americans. It is true that the earned income tax credit provides, over five years, $18 billion in tax relief.

But it is also true that a little more than $6 billion of that was needed to offset the regressive taxes that were also put in place.

The tax relief that was provided in 1990 was closer to a net of $12 billion over five years, which is about $2 billion a year. I think that if we do a children's tax credit and do not provide it to the 25 percent of the poorest children in this country, that we will be making a mistake.

The Chairman. All right. The issue is

before us.

Senator Bradley. Mr. Chairman, could I ask for a roll call?

The Chairman. A roll call is asked for. Call the roll.

The Clerk. Mr. Moynihan.

Senator Moynihan. No.

The Clerk. Mr. Baucus.

The Chairman. No, by proxy.

The Clerk. Mr. Boren.

The Chairman. No, by proxy.

The Clerk. Mr. Bradley.

Senator Bradley. Aye.

The Clerk. Mr. Mitchell.

The Chairman. No, by proxy.

The Clerk. Mr. Pryor.

Senator Pryor. No.

The Clerk. Mr. Riegle.

Senator Riegle. No.

The Clerk. Mr. Rockefeller.

Senator Rockefeller. No.

The Clerk. Mr. Daschle.

Senator Daschle. No.

The Clerk. Mr. Breaux.

Senator Breaux. No.

The Clerk. Mr. Packwood.

Senator Packwood. No.

The Clerk. Mr. Dole.

Senator Dole. No.

The Clerk. Mr. Roth.

Senator Roth. No.

The Clerk. Mr. Danforth.

Senator Danforth. No.

The Clerk. Mr. Chafee.

Senator Chafee. No.

The Clerk. Mr. Durenberger.

Senator Durenberger. Aye.

The Clerk. Mr. Symms.

Senator Symms. No.

The Clerk. Mr. Grassley.

Senator Grassley. No.

The Clerk. Mr. Hatch.

Senator Hatch. No.

The Clerk. Mr. Chairman.

The Chairman. No.

The Clerk. The votes are two Senators in favor; 18 opposed.

The Chairman. Are there further amendments?

Senator Rockefeller. Mr. Chairman.

The Chairman. Yes.

Senator Rockefeller. I have an amendment with respect to an effort to stabilize the funding of health care for retired coal miners, their widows, and beneficiaries. The background paper, I think, is being distributed to each of my colleagues.

We have reached a point where the health care benefit which supports the health care for widows and dependents of coal miners that have been working in the mines for 30-40 years is about to run out.

And the fact of the matter is, on March the 13th, or thereabout, they are going to get a letter saying that, on April 13th, their health cards will be jerked.

And these people--who are, on the average, 77 years old; who spent their lives, so many of them, in the most dangerous work that you can do anywhere in America working in the coal mines--will no longer have health care.

The solution that I have is equitable. It is not pleasant, but it is the only way which we can, in a fair manner, return stability to the health fund for these coal miners, their widows, and their beneficiaries.

It affects 120,000 people; average age, 77 years old, who are in the most fragile point of their lives, and who have health problems which exceed most because of the work that so many of them have done. And if we do not correct this problem, on April 13th they will have no health benefits whatsoever.

This is something which has its emotional and moral roots all the way back to Harry S. Truman and John L. Lewis. I will not go into a great deal of further detail, but it is something which is of unbelievable importance to these people.

There is nothing which stands between them and being out on the street, in terms of health care, at the age of 77, other than the action of this committee. And I would move my amendment.

Senator Packwood. Could I ask a question?

The Chairman. Yes, of course. Senator Packwood.

Senator Packwood. In the last paragraph, if the modifications are made to S. 1989 to clarify the definition of coal production subject to the hourly fee, what kind of coal is excluded; what States are excluded? How does it work?

Senator Rockefeller. The types of coal that would be excluded in this definition would be lignite and sub-bituminous.

Senator Packwood. Does that exclude most of the coal dug in Texas?

Senator Rockefeller. It would.

Senator Hatch. Could I ask a question or two?

Senator Rockefeller. I would add, further, however, that lignite has never been counted, for example, in the Black Lung Trust Fund. It has never been counted for over 25 years, so there is nothing enormously unusual about that.

Senator Packwood. And does it change the hourly fee that is now paid by so-called Western coal?

Senator Rockefeller. It changes it from the original proposal that I made when I introduced this bill. It changes it downward.

Senator Packwood. How much?

Senator Rockefeller. From 75 cents to 15 cents on, in terms of Western coal and Eastern coal. Obviously it is substantial.

Senator Packwood. And then how did you make up the difference when you dropped the fees and excluded the lignite and sub-bituminous? Where did you get the rest of the money?

Senator Rockefeller. The rest of the money, clearly, in order to provide the health benefits at their current levels and the needs that these people have would have to be made up by two factors.

One, making the fees for the Eastern bituminous coal sufficient to meet the health requirements; and, secondly, through the application of a very strong managed care program, which would go into effect, were this amendment to be adopted.

Senator Dole. Mr. Chairman, I understand that the Government Accounting Office has been asked to do a study to determine if the Federal Government would be exposed to any financial risk, and we do not have the answer on that. I do not know what our colleagues' response might be.

Are you suggesting that there will be no cost to the government?

Senator Rockefeller. One of the parts about this which is, I think, important, and why it is so important that we solve this now is that this can be solved within the coal industry.

The coal industry has taken care of its own traditionally. This is part of the emotional and moral heritage that I referred to. There would be no Federal taxes involved in this whatsoever.

Senator Dole. Well, I do not disagree with the problem. I think the question is--and I am certain the Senator has the votes and maybe it is a moot question--but it is a very important amendment and it is a very controversial amendment.

What we are doing is imposing a tax on all imported and domestic-produced coal, set up a new government-operated operation that can raise the coal production taxes it levies. It is going to be a penalty through a tax on all non-union coal companies and non-BCO companies that had nothing to do with this problem.

And it is unfortunate, but they are going to help pay for it. But that is what some of the coal-producing people are prepared to do in the Western States. They are not party to the collective bargaining agreement.

They did not promise the lifetime benefits, and now we have got a problem. And it is a serious problem, as the Senator from West Virginia points out.

So, I think it is certainly unfair to those who had nothing to do with creating the problem, but they are going to be asked to pay for it, or pay for part of it. And, to me, that is not the right philosophy to approach. But I would guess that it would not be offered if you did not have the votes.

Senator Chafee. Mr. Chairman.

The Chairman. Yes. Senator Chafee.

Senator Chafee. Mr. Chairman, I would like to ask Senator Rockefeller a couple of questions.

In the hand-out that you passed around, Senator, you pointed out in the next-to-the-last paragraph, the last sentence, "The benefits are subject to cost containment." And I think in your presentation you mentioned something about managed care.

It was my understanding--and perhaps this has been changed from when you originally presented this--that these plans provide for first-dollar coverage with no co-payments. Am I correct in that?

Senator Rockefeller. In fact, there is a very small co-payment. The Senator is essentially correct in that the Senator needs to understand, as those of us who come from coal mining States do, that people who have been through 40 years of coal mining do not come out of that experience in the kind of physical condition that most other folks do from their lifetimes.

So that the benefits are strong, as they need to be. Coal miners have always placed more emphasis on health benefits than they have on pension benefits, and that is because they have to face these things every day.

The managed care portion, I say in great seriousness, because that is part of the agreement on this. There has to be managed care. I do not dispute that the benefits are strong, in terms of health, because the need is very, very strong on the part of these very elderly people.

Senator Chafee. Well, I am a bit confused. The Senator from West Virginia has spent a lot of time on health care and certainly the terms "first-dollar coverage" in managed care are antithetical.

First-dollar coverage is, as I say, the opposite, the antithesis of managed care. Is there first-dollar coverage under this plan?

Senator Rockefeller. In literal terms, there is not, and there is a very tiny co-payment. But the effect--I am not trying to argue with the Senator from Rhode Island--of this is in that direction. And whether or not managed care is antithetical or not to the proposition, I cannot argue. Managed care, when applied very seriously, does have very substantial benefits.

The Chairman. Further questions?

Senator Symms. Mr. Chairman.

The Chairman. Senator Symms.

Senator Symms. Mr. Chairman, I just want to be sure that I understand exactly what is going on here, and I have to say to my colleague from West Virginia that I have to congratulate him for his tenacity on this issue.

It is not a popular issue here in this committee to have to deal with it, and it is not a popular issue for any of us to have to oppose it. But I would like to have a look at what the facts are here now.

Do I understand this correctly, that the three biggest coal companies have under-funded the funding formula to reduce their contribution to the 1974 Trust Fund, and, as a result, other companies have left the agreement. Is that correct?

Senator Rockefeller. No. The Senator has to understand that the Bituminous Coal Operator Association of America is now paying $1 for the health benefits for their own retirees and $3 for everybody else's, including any that might be in the Senator's own State.

The BCOA used to be an enormous organization. There were 2,000 companies that belonged to it. Now it is down to about 300, and it is a very small organization. So that the base for paying for all of this is a very small base. Therein lies our problem.

Senator Symms. Well, if I could just pursue that further with my colleague. I personally do not have a dog in this fight. We do not have any coal in my State. But what I am trying to point out --

Senator Rockefeller. But you do have retired coal miners, Senator.

Senator Symms. Yes, we have some. But the point is --

Senator Rockefeller. And their health is being taken care of.

Senator Symms. What we are trying to do here with this amendment would be to get the Federal Government to impose a levy on all other coal companies to make up for what has failed to have been paid in, and they had no obligation to pay into the fund. Is that not correct?

Senator Rockefeller. The Senator raises, I guess, the moral dilemma that faces each Senator who votes on this. One could say that the BCOA--the Bituminous Coal Operators of America--should pay it all.

And right now, that is what they are doing. As of next January, they stop doing that, because that is when the contract runs out.

So, I guess essentially what people have to say is, are we interested in preserving health benefits which 120,000 coal miners and their beneficiaries have had all of their lives, or are we not?

Senator Symms. Well, it was my understanding that the companies that created the problem have enough resources of their own to solve the problem, and it seems to me like it is wrong to then have the government try to force other people who have no legal, moral, or financial responsibility in the matter to pay it. That is basically what we are doing. Is that not correct?

Senator Rockefeller. Senator, it depends on where you are coming from.

Senator Symms. I know it is a heart-wringing, hand-wringing subject, and it is very difficult, and I am sympathetic with that. But I just want to understand what it is we are doing.

Did the biggest three coal companies not create the problem, and they have a lot of resources and they do not want to pay for it?

Senator Rockefeller. No. I do not think that is an accurate characterization at all. I do not know that the three biggest coal companies have created the situation.

What I do know is that the relatively few coal companies who are in the BCOA right now are paying for the health benefits for the retired miners, their widows, and beneficiaries of every single coal miner in this country--all 120,000--even though they are only responsible for 25 percent of them.

Senator Symms. But the BCOA, in 1974, under-funded this program. Is that not correct?

Senator Rockefeller. That is not correct, sir.

The Chairman. Are there further questions?

Senator Boren. Mr. Chairman.

The Chairman. Yes. Senator Boren.

Senator Boren. Mr. Chairman, I must say that I have very strong feelings about this amendment. I think we are setting here a terrible precedent.

In essence, what we are saying is that one person, or one set of companies can enter into a contract and enter into a contract, perhaps, knowing that they are entering into provisions that they are not going to be able to fund that they will walk away from later, and then put the responsibility on other people to pay for it.

It would be like if one of us entered into a contract and bound another one of us sitting at this table who was not a party to the agreement or the negotiations.

In other words, the store was given away, to some degree, for other people who were not even there at the bargaining table. Now, I think we are all very sympathetic to the need for all of those individuals that are covered to be taken care of to have their health benefits paid.

But to ask people who were not parties to those negotiations, and all of these have been left behind were companies--some of them have since gone out of business, but originally all the people that were involved and covered--were covered by the contract negotiations.

So, we are setting here a very, very dangerous precedent. We all sympathetically want to take care of those in need.

I have made a proposal that the pension funds should be transferred over from these same companies who were a party to the agreement and help take care of those in need; that we have a reach-back provision with a diminimus provision to take care of those companies that produce very little to take care of it.

This would take care of the emergency problem and carry us through, perhaps, for another year, during which time we can try to work out a more permanent solution.

But I do not believe that the other people in the coal industry who were not a party to this agreement in these contract negotiations have any more obligation than any other person on the street who is walking by has an obligation to take care of these benefits.

It is simply a terrible, terrible precedent.

I think it is as wrong as wrong can be. Now, given the situation that we are in -- and I respect all of us on this committee that fight for people in our home States and home regions when we have people that are in hardship.

And I am quite sure that if I were in a similar position as the Senator from West Virginia, I would be wanting to find a solution to take care of my constituents, as well.

I certainly have no lack of respect for the Senator from West Virginia for doing that. He has been tenacious. He has presented his case very forcefully, and I know he is very sincere about it.

So, I have no hard feelings toward him for making his point of view very strongly. I do, just in all sincerity, disagree with him. Now, I am left in this position and when the vote on this amendment is called, I am simply going to vote, present.

Because if I were to vote down this amendment, it is my understanding that it could imperil the entire bill. And there are so many good things in this bill, and we have talked about them earlier; from educational interest deductions on college loans, to beginning to have some incentives for capital formation; and encouraging saving and investment, and a lot of other things that are in this bill.

I think the process is too valuable. I think we should allow the bill to go forward. And, therefore, at this point in time, I am not going to attempt to defeat this amendment.

In conscience, I simply cannot vote for it, because I am not going to put my name down beside a proposition that people who have not entered into a contract should be bound by the terms of that contract.

And I must say I hope between now and the time that this matter comes up on the floor we can find a way to help those in need without violating the principle that people can negotiate, under our legal system, for people that are not a part of contract negotiations.

This is an extraordinary thing. It is wrong. And the only thing that prevents me at this point from trying to defeat this amendment outright is my conviction that the effort we are making to at least go forward at this process, we are trying to come to some deliberation under the President's guideline, and this bill is an improvement over the current law.

So, we are put in the position here, I think, of having to weigh all of those factors. So I am not going to vote, no. In conscience, I simply cannot vote for it. I hope we can find a way around it.

I have to say that in terms of a principle of law, I do not know how in the world they are going to teach this in Introductory Contracts in the contracts law courses of law schools, when they used to say you had to have a meeting of the minds between two people to have a contract. Here we have people being bound who were not even in the room, let alone a meeting of the minds.

Senator Symms. Senator, if my good friend will yield, the way they will teach it is raw power politics. If you have got the votes, you can do it.

Senator Bradley. Well, I hope we can find a way. We are dealing with human need; I do not denigrate that. I do not think any of us want to see people thrown out of nursing homes and thrown out of convalescent facilities. And it is a very terrible situation, and these companies have all undertaken responsibilities which they have not kept, and obviously have not undertaken the right kind of financial planning when they entered into these responsibilities. But that is not the fault of the people that were not parties to the contract.

Senator Packwood. Let me ask you a question.

The Chairman. Senator Packwood.

Senator Packwood. I agree with the philosophy of what you are saying. Why does this bill go down to defeat if this amendment is not in it?

Senator Bradley. I think it might jeopardize the passage of the bill. So I am simply not going to oppose it at this point.

(Laughter)

Senator Hatch. Mr. Chairman?

The Chairman. All right. Are there other comments? Senator Hatch.

Senator Hatch. Mr. Chairman, could I just have a few points of clarification with my friend from West Virginia?

Now, I want to say at the outset that I am dedicated to working out a solution here. Like the Senator from Oklahoma, I do not want to see these people without their health coverage. It may be that we will have to do an overall program of the country, but I am concerned. As I understand it, the old bill was in 1989. You had 75 cents an hour in there. Has that figure changed at all?

Senator Rockefeller. That figure has changed. That figure now is 15 cents.

Senator Hatch. For everybody?

Senator Rockefeller. For those west --

Senator Hatch. No, but the regular BCOA companies were going to pay 75 cents an hour?

Senator Rockefeller. That is correct.

Senator Hatch. Are they going to still do that?

Senator Rockefeller. That is correct.

Senator Hatch. Now, you are saying the Western States, they will pay 15 cents an hour instead of the 75 cents?

Senator Rockefeller. Senator, from the very beginning I have tried to reach out to the West.

Senator Hatch. No, no. I am not finding fault. I just want to know what the facts are.

Senator Rockefeller. The Senator is correct.

Senator Hatch. All right. Now, as I

understand it, in your amendment here today, you are excepting or excluding the lignite producers and the sub-bituminous producers. Is that correct?

Senator Rockefeller. The Senator is correct.

Senator Hatch. So there will be some companies who will have the privilege of not having to pay even 15 cents?

Senator Rockefeller. The Senator is correct.

Senator Hatch. And in what States are those? You have got Texas, and then what are the other States?

Senator Rockefeller. Senator, I am not entirely sure. Staff may be aware of that. In fact, it may be the Senator's own State is one of those.

Senator Hatch. I do not think so.

Senator Rockefeller. In any event, it is all west of the Mississippi.

Senator Hatch. In other words, the sub-bituminous States like Montana and so forth.

Well, the only thing I am pointing out here, is that I certainly agree with the distinguished Senator from Oklahoma, that if there is a way of doing it, we have got to find it. And I am dedicated to helping the distinguished Senator from West Virginia to do that.

But I agree with the Senator from Oklahoma, that this may not be the way to do it. But there has got to be a way and we are working at it now with you.

And I appreciate the efforts that you have made and the intense efforts that you have put in to try and resolve what clearly is an inequity to the people involved, which some will feel will be an inequity to the companies who did not contract to do this, or were not original people agreeing to do it.

But I just want to tell the Senator that I think we can find a way. I just hope it will be acceptable to everybody.

Senator Rockefeller. I appreciate the Senator's concerns.

The Chairman. Are there further comments?

Mr. Chafee. Mr. Chairman, is this levied per ton or per hour work?

Senator Rockefeller. Per hour.

The Chairman. Further comments?

You have presented the amendment. All in favor of the amendment as stated, make it known by saying, aye.

(A chorus of ayes.)

The Chairman. Opposed?

(A chorus of nays.)

The Chairman. You requested roll call. Call the roll.

The Clerk. Senator Moynihan.

Senator Moynihan. Aye.

The Clerk. Mr. Baucus.

Senator Baucus. Aye.

The Clerk. Mr. Boren.

Senator Boren. Present.

The Clerk. Mr. Bradley.

Senator Bradley. Aye.

The Clerk. Mr. Mitchell.

The Chairman. Aye, by proxy.

The Clerk. Mr. Pryor.

Senator Pryor. Aye.

The Clerk. Mr. Riegle.

Senator Riegle. Aye.

The Clerk. Mr. Rockefeller.

Senator Rockefeller. Aye.

The Clerk. Mr. Daschle.

Senator Daschle. Aye.

The Clerk. Mr. Breaux.

Senator Breaux. Aye.

The Clerk. Mr. Packwood.

Senator Packwood. No.

The Clerk. Mr. Dole.

Senator Dole. Present.

The Clerk. Mr. Roth.

Senator Roth. Present.

The Clerk. Mr. Danforth.

Senator Danforth. No.

The Clerk. Mr. Chafee.

Senator Chafee. No.

The Clerk. Mr. Durenberger.

Senator Durenberger. Present.

The Clerk. Mr. Symms.

Senator Symms. No.

The Clerk. Mr. Grassley.

Senator Grassley. No.

The Clerk. Mr. Hatch.

Senator Hatch. Present.

The Clerk. Mr. Chairman.

The Chairman. Aye.

The Clerk. There are 10 Senators in favor; five opposed; five voting present.

The Chairman. The amendment is passed.

Senator Pryor. Mr. Chairman?

The Chairman. All right. Do we have further amendments?

Senator Pryor. Mr. Chairman?

The Chairman. Yes. Senator Pryor.

Senator Pryor. Am I right, is this the stage in the process where I may talk about an amendment?

The Chairman. Yes, of course.

(Laughter)

Senator Pryor. Well, Mr. Chairman, this is a non-controversial amendment. It is relative to the prescription drug prices.

(Laughter)

Senator Pryor. And I think there may be a lot of interest in the room about this particular amendment. I am going to take just a moment, Mr. Chairman and talk about it.

I want to relieve my colleagues here of the notion that I am going to offer this amendment this afternoon; I am not. But I am going to offer this amendment on the floor of the Senate when the bill comes before the Senate.

Mr. Chairman and colleagues, I am going to be very, very brief. I know the hour is late. We are all tired and we have been here all day. I just want to go over if I might, three or four facts that I think might be pertinent to this argument when we reach the Senate floor.

Today, there are 5 million elderly people in America who are today having to decide whether or not to buy their prescription drugs or to provide food.

Three-out-of-every-four elderly in our country today, in a recent poll, said that prescription drugs are the highest out-of-pocket costs that they have. There are 16 million elderly people who have absolutely no drug coverage whatsoever.

The drug companies today--the pharmaceutical manufacturers--my colleagues, they are coming to us and saying, through all of the newspaper advertisements and television, et cetera, that they need higher prices in order to justify the costs that they are expending on research.

Well, the fact is, our answer to the drug companies is very simple. Today, the drug companies are spending $1 billion more on advertising and marketing than they are on research.

And I think that, without question, this is one of the major abuses in our whole health care system, and that is the drug industry and the high cost of pharmaceuticals.

I have attempted to just in a matter of about five charts, very briefly, demonstrate basically where we are in profits. Here, for example, I show to my colleagues the profit basically of 1991 of the Fortune 500 companies; basically, 4.6 percent.

The pharmaceutical companies reaped a profit of about 15.5 percent. We also see that in 1991, that the inflation rate was roughly three percent. The drug inflation rate or the price increase was 9.4 percent. We have just seen January inflation rates, I say to my colleagues.

And we see that the cost of living rate for January was .1 percent. The cost of increases in pharmaceutical drugs are .9 percent. We are continuing to see at least a three-to-four times increase in the cost of prescription drugs over the general inflation rate.

In fact, in the past decade, 46 percent general inflation, I say to my colleagues; 142 percent was in the cost of prescription drugs. We see a $67 billion price tag today for drugs. If the present trend continues, by the year 2000, it will be a $145 billion cost for drugs.

A drug costing, in 1980, $20, in eight years is going to cost $120. These are all statistics from the various departments of government; the Department of Labor, Business Week, AARP.

And this is a nice little chart here, my colleagues. The drug companies say they need all this money. Actually, the elderly household average income today in America is $8,700.

The CEOs are being given a salary by the respective drug companies--the 22 majors--of $1.56 million. That does not include golden parachutes; it does not include stock options; it includes only the salaries themselves.

I have tried to the best of my ability to work out a solution to try to provide a carrot and a stick. The carrot is going to be the 936 tax provision.

The stick is going to be that provision under this new proposal that I am proposing, that anything over the cost of inflation that a drug company increases their drug prices, they will lose that much in percentage of the 936 tax incentive, or tax credit in Puerto Rico.

We see today that in Puerto Rico, a drug company going to that particular place to set up a manufacturing plant, one, they are paying no income taxes on the profits derived from that facility.

But, in addition to that, they get a $71,000 tax credit for every employee that they hire in that particular manufacturing facility.

We think it is time, Mr. Chairman, to deal with cost containment. We know that we have cost containment items, not only in this particular bill, you--and I applaud you for it, Mr. Chairman--have a Commission that you are setting up; an 11 person Commission, I believe appointed by the President, confirmed by the Senate. This is certainly a start.

But I am proposing that we attempt a cost containment as a provision in the program as it specifically relates to the drug pricing.

We are seeing today a double-hit on the American taxpayer. One, we are paying for their research; we are paying through R&D; we are paying through the 935 program.

We are also paying the highest cost of any industrialized country for the cost of prescription drugs in the company.

I would like to applaud one drug company, I might say, and that company is MERCK. MERCK has already come out and publicly stated that they will not increase the cost of their drugs in 1992 over the cost of inflation.

I think that is the type of leadership that we are going to have to have. I am afraid that is the type of leadership that we are not going to get universally throughout the drug industry, unless we have legislation in this field.

Mr. Chairman, in closing, I would like to enclose the list at this point in the record of the 44 very, very splendid and courageous organizations who are endorsing S. 2000. And we look forward to this debate on the Senate floor, and we hope that it will prevail.

Mr. Chairman, thank you, and I thank my colleagues.

(The letter appears in the appendix.)

Senator Hatch. Mr. Chairman?

The Chairman. Yes. Senator Hatch.

Senator Hatch. Mr. Chairman, I do not want to keep us long on this because you are not offering the amendment today. But let me just say this: I understand what the distinguished Senator from Arkansas is saying, and I commend him for trying to find a solution to this problem.

I gave a speech in front of about 2,000 Federal drug lawyers not too long ago. And I suggested to them that there are major P&E companies who are gouging the American public.

It was not just MERCK who agreed. Pfizer automatically started to cut some of their drugs. They said I was right. And frankly, I think something has to be done, but I do not want to go to regulation.

I do not want to go to price controls or rate regulation, because I think this will stifle this one industry that happens to be the best industry in our country right now. We have ruined about every other industry.

Now, we want to turn around and ruin the pharmaceutical industry. And nothing will do it more than rate regulation and playing around with the 936 benefit.

Also, limiting the 936 credit to wages paid will only penalize and undermine the companies primarily responsible for job growth in Puerto Rico. I am concerned about that because it unfairly targets the pharmaceutical industry. And no other industry with Puerto Rico facilities has price restrictions.

So this is a back door approach in my opinion, as much I admire the distinguished Senator from Arkansas, to have price controls in the drug industry.

It is not contingent to Puerto Rico operations, applied if the drug was manufactured in Puerto Rico or the United States, and it is going to hurt U.S. competitiveness by raising costs. And, I might add, few foreign firms have companies in Puerto Rico. So it is a problem.

The credit that we provide for Puerto Rico brings much-needed capital and employment there. Reducing that credit reduces these benefits and hurts the one commonwealth of our country that really, really needs the help.

So you can imagine what the Puerto Rico foundation feels about this: they strongly oppose it. We could argue about it for a long time here today. But I just want to make the point, that I would like to find a resolution to this problem.

I hope that the companies will start to cooperate voluntarily rather than have to go through this type of a problem. And some are willing to do that; very few right now. But I think we can get others to do that. And if that is so, then I think that the distinguished Senator from Arkansas can take a great deal of credit for that.

And I would like to personally compliment him. But boy, I do not want to go to rate regulation.

The Chairman. Gentlemen, this is a very illuminating debate. But I wonder if we could continue it on the floor when the amendment is before us.

Senator Hatch. Sure.

Senator Symms. Mr. Chairman?

The Chairman. Senator Symms, you had been asking for --

Senator Symms. Well, Mr. Chairman, in deference to the Chairman, I will not give my speech. But I would just like to alert my colleagues that I will have an amendment to make a minor modification in the Tax Code which will have a great impact on our transportation, environmental and energy policies.

It makes good economic policy; it makes good transportation policy; it makes good energy policy; good environmental policy; and good tax policy. So if you will keep your powder dry, and I will get to each of you individually and save the Chairman the five minute speech that I was prepared to give now.

The Chairman. Thank you very much.

Senator Bradley. Mr. Chairman, is there any reason that Senator Pryor does not want to offer his amendment now?

Senator Pryor. Yes. The reason that Senator Pryor does not want to offer the amendment right now is I would get beat.

(Laughter)

Senator Pryor. And I do not enjoy getting beat.

Senator Hatch. And rightly so.

(Laughter)

The Chairman. That is refreshing candor.

Senator Pryor. And I might say, Mr. Chairman, and my colleagues, that most of the co-sponsors of S. 2000 are not on this Committee; they are members of the Senate. And they wanted an opportunity to have their record made on this amendment and we are going to have that opportunity on the floor.

I have discussed this with the Chairman and my colleagues this morning, and this will be considered on the floor. We look forward to a very good debate on it.

The Chairman. Thank you. In hearing from both sides, we are about ready for a vote.

Senator Chafee. Mr. Chairman, may I ask a quick question?

The Chairman. Yes.

Senator Chafee. You have 44 organizations that are supporting your amendment. Is the Commonwealth of Puerto Rico one of those?

Senator Pryor. I doubt that they are.

(Laughter)

Senator Pryor. I doubt that, Senator Chafee.

Senator Hatch. I can tell you, they are not.

Senator Pryor. But I might say this, in all due fairness to Puerto Rico, and I have talked to several from that Island: In all fairness, the 936 Provision helps the drug companies much more than it helps Puerto Rico.

And I think that we will make that point on the floor and I hope that I will prove that point. But it is a bonanza for the drug companies.

For example, I am losing two bases. I am losing two military bases. And I can think of nothing better than if the drug companies would come to those two areas of our poor State, and set up some drug manufacturing plants and they could get the same deal in Sebastian County, Arkansas and Mississippi County, Arkansas as they are getting in Puerto Rico.

I think it would be a great tax incentive and an idea for an enterprise zone. And I think we need the same treatment in Arkansas and in other States around the country as we give in Puerto Rico.

Senator Grassley. Mr. Chairman?

The Chairman. Yes.

Senator Grassley. I do not have an amendment to offer. But I do want some time to bring up a problem that asks the Chairman to consider, and maybe help us find a solution for. It is not only my State, but a few other States. The subject is in-home health care for the disabled.

Under a number of State programs, disabled persons are given funds to help with in-home care. In my State, the disabled receive around $4,200 per year for in-home care. Approximately 300 of these recipients turn the money over to a family member to take care of them.

Unfortunately, against the intentions of the State and contrary to what the beneficiaries had been led to believe, the IRS has determined that the funds received by the related care providers, that that is taxable income.

Even worse, the IRS has determined that these family members are self-employed and, therefore, owe FICA tax.

In Iowa, the IRS is also going after back taxes for three or four years. So, the families of disabled people who have sacrificed and do not have much money to begin with are saddled with thousands of dollars of debt to the IRS.

By doing this, we are cutting off our nose to spite our face. I think you can see that. But by substantially reducing these already modest payments through taxes, we are going to force some of these disabled individuals into institutions which then will cost our government many thousands of more dollars.

I want to raise this problem and bring it to your attention, Mr. Chairman, so that hopefully, in the near future, the Committee will be able to help these unfortunate taxpayers. And, I guess, I am asking you if you can maybe help us find a solution to that problem.

The Chairman. Well, I will be happy to work with you and staff and see if we can find something on it, Senator.

Senator Breaux. Mr. Chairman.

The Chairman. Senator Breaux.

Senator Breaux. Mr. Chairman, I have an amendment that I think is small, but significant. I would like to ask the staff to pass out the description to it, and I would like to offer it.

Mr. Chairman, if I am recognized to that purpose, every business in America that has employees that earn part of their wages through tips, have to pay the Social Security tax, not only on the direct wages they pay their employees, but also on the tips that their employees receive--even those tips that are in addition, or over that which can be counted for minimum wage that their employee is entitled to receive.

Now, we all know, Mr. Chairman, that Social Security is supposed to be a payroll tax and it is supposed to be paid on the wages that are paid employees.

Particularly, small businesses like restaurants that have many employees that receive part of their wages in tips are being severely penalized by having to pay the Social Security tax, not only on their wages, but they are paying them also on the tips that their employees receive, and that is not right.

Tips are not planned for; they cannot be put in a small business' budget. It is discriminatory and should be eliminated. Estimates have indicated that this elimination would create as many as 39,000 additional jobs. And it certainly addresses the question of tax fairness for small businesses like restaurants.

Mr. Chairman, the repeal of this tax--the tax credit which I propose--has 10 co-sponsors in this Committee, has 255 co-sponsors in the House; has 45 or 46 co-sponsors in the Senate.

What my amendment would do, would continue the payment by the employer of the Social Security tax so we do not violate the Social Security Trust Fund, but it would give a tax credit at the end of the year for that employer to the extent that he had to pay Social Security tax on the tips that his employees received over and above that which can be counted for the minimum wage.

Mr. Chairman, and members, this cost--and you will see on the thing that we gave out on page four from the Joint Tax--the credit for tips that I am proposing would cost $1.5 billion over five years.

The way we would pay for it is by eliminating the business deduction for membership dues in clubs; clubs like social, athletic, luncheon or sporting clubs.

Now, I would say to my colleagues that members or citizens who belong to these organizations would still be able to deduct their lunches or dinners or social events at those clubs that have a legitimate business expense purpose, and still be able to deduct golfing fees, and certainly would be able to deduct tennis court fees, if, by golly, they are related to the business expense of conducting business, exercising these type of activities.

But they would no longer be able to deduct the membership dues to these clubs. Now, we all know that the average citizen or Joe Sixback, who scrapes up enough money to join a local health club; he cannot deduct that membership.

But wealthy executives in this country, not only deduct the meals and the golf outings and everything else they do at the club, they deduct the membership as well.

And I think that this is a fair exchange, helping hundreds of thousands of small businesses throughout this country, restaurants, in particular.

There are a large number of co-sponsors for this amendment, with a dollar-for-dollar offset, which I think makes sense, is appropriate and proper and it is fair.

The Chairman. Senator Dole.

Senator Dole. Mr. Chairman, is there a limit on the size of the restaurant, on the size of the business?

Senator Breaux. There is not. I would respond, that the way I think it has been drafted is that any restaurant that has tipped employees would be covered by the amendment; small, medium and large.

Senator Dole. The 21 Club in New York would be covered then?

Senator Breaux. Absolutely. As well as Joe's Eatery, if he has tipped employees.

Senator Dole. I would like to help Joe's Eatery, but I am not certain about helping those fat cats in the other areas.

Senator Hatch. Mr. Chairman?

The Chairman. Yes?

Senator Hatch. Mr. Chairman, just a couple of comments. I support the distinguished Senator's amendment. It is a question of fairness and consistency. Employers have to take cash tips into account when paying FICA taxes. But they have to ignore half of those tips when they figure minimum wage calculations, and that is inconsistent.

It is a conflict between the labor and the tax laws and it is forcing employers to pay taxes on income over which they have absolutely no control. So, the restaurant industry, I think we would all admit, is mostly made up of small businesses.

The tax drives up the payroll costs, and, of course, it also costs the businesses from a paperwork standpoint tremendously, and it hinders expansion and job creation in the industry.

So, I would hope our colleagues will support this amendment. I think it is a worthwhile one and it will do a lot of good.

The Chairman. Gentlemen, are we ready to vote on this? The motion is before you. All in favor, make it known by saying, aye.

(A chorus of ayes.)

The Chairman. Opposed?

(No Response)

The Chairman. The motion is unanimous. Carry it. Thank you. I now -- unless there are further amendments.

Senator Bradley. Mr. Chairman?

The Chairman. Yes.

Senator Bradley. Mr. Chairman, I will not offer an amendment here, but the Chairman does not my concern about the issue of living benefits, which is when someone has a life insurance policy and becomes terminally ill and cashes it in, that is now taxable.

I would hope that we can make it non-taxable at some point --

The Chairman. Thank you.

Senator Bradley. -- and perhaps on the floor.

The Chairman. Thank you.

Senator Riegle. Is a motion in order to

report the bill --

The Chairman. Yes, a motion --

Senator Riegle. I make such a motion.

The Chairman. The motion will be to report out the Chairman's mark as an amendment to HR. 4210, contingent on its arrival from the House.

All in favor of the motion as stated --

Senator Dole. Is it open?

The Chairman. If you would like.

Senator Dole. Oh, yes, we want it open.

The Chairman. All right. Fine, good.

Senator Dole. That is why we came.

(Laughter)

The Chairman. A roll call is called for. If you will proceed.

The Clerk. Mr. Moynihan.

Senator Moynihan. Aye.

The Clerk. Mr. Baucus.

Senator Baucus. Aye.

The Clerk. Mr. Boren.

Senator Boren. Aye.

The Clerk. Mr. Bradley.

Senator Bradley. Aye.

The Clerk. Mr. Mitchell.

The Chairman. Aye, by proxy.

The Clerk. Mr. Pryor.
Senator Pryor. Aye.
The Clerk. Mr. Riegle.
Senator Riegle. Aye.
The Clerk. Mr. Rockefeller.
The Chairman. Aye, by proxy.
The Clerk. Mr. Daschle.
Senator Daschle. Aye.
The Clerk. Mr. Breaux.
Senator Breaux. Aye.
The Clerk. Mr. Packwood.
Senator Packwood. No.
The Clerk. Mr. Dole.
Senator Dole. No.
The Clerk. Mr. Roth.
Senator Roth. No.
The Clerk. Mr. Danforth.
Senator Danforth. No.
The Clerk. Mr. Chafee.
Senator Chafee. No.
The Clerk. Mr. Durenberger.
Senator Durenberger. No.
The Clerk. Mr. Symms.
Senator Symms. No.
The Clerk. Mr. Grassley.

Senator Grassley. No.

The Clerk. Mr. Hatch.

Senator Hatch. No.

The Chairman. Mr. Chairman.

The Chairman. Aye.

The Clerk. The votes are 11 in favor; nine, opposed.

The Chairman. Gentlemen, I have one more responsibility here. This is necessary to comply with the requirements of the budget process. I have discussed this with the Ranking Minority Member of the committee and with, I understand, the Minority staff.

In order to confirm Section 9 of the concurrent resolution on the budget for Fiscal Year 1992, regarding reserve fund issues, I would like the committee to report the following items as a separate, original bill:

(1), the earned income tax credit changes; (2), net outlays attributable to the Medicare prevention benefits; (2A), coal miner health benefits legislation; (3), the cap on the deduction for regular tax and AMT purposes for executive compensation; (4), changes to the tax on ozone-depleting chemicals.

I move the adoption of this original bill. All in favor, make it known by saying aye.

Senator Packwood. Mr. Chairman?

The Chairman. Yes? I beg your pardon.

Senator Packwood. Just to clarify this so that everybody understands, you have to do this so that the bill is not subject to a 60-vote point of order on the floor?

The Chairman. That is correct.

All in favor of the motion as stated, make it known by saying, aye.

(A chorus of ayes.)

The Chairman. Opposed?

(No response)

The Chairman. No nays; motion carried. Thank you.

Mr. Sessions. Mr. Chairman?

The Chairman. Yes?

Mr. Sessions. I'd like to ask that the customary drafting, that has already been --

The Chairman. Yes. Without objection, that will be done. Is that it?

Mr. Sessions. That is it.

The Chairman. Thank you very much.

(Whereupon, the meeting was concluded at 5:58

p.m.)

CERTIFICATE

This is to certify that the foregoing proceedings of an Executive Committee Meeting of the Committee on Finance, United States Senate, held on March 3, 1992, were transcribed as herein appears and that this is the original transcript thereof.

William J. Moffitt

WILLIAM J. MOFFITT
Official Court Reporter

My Commission Expires April 14, 1994

STATEMENT OF SENATOR STEVE SYMMS

SENATE FINANCE COMMITTEE

Steve Symms

MARCH 3, 1992

Mr. Chairman: It wasn't so long ago when we would pull together as a Nation during tough economic times. When the President could call the Chairmen of the tax writing committees, they'd agree to work together, and a few weeks later we'd be back on the road to recovery.

It wasn't so long ago when the tax writing committees could put aside their partisanship for a few moments and do what everybody knew to be good for the country. How far we have fallen.

The Chairman of the Ways and Means Committee summed up his tax package in one word: fairness. There are many words I might use to describe what was done in the House, but fairness wouldn't be one of them. Short-sighted comes to mind. Irresponsible would also fit better.

I'm sorry to say that what we have before us today is better, but it's no where near enough. If we have to play these soak the rich games when things are going well, at least we should call time-out when the economy needs some help. I'd of thought we had learned our lesson with 1990's favorite soak the rich taxes -- the luxury taxes. Will we never learn?

Partisan fights are natural, they're important, they're part of what we do in the Senate. But when it comes down to getting the job done, this committee has always found a way to put the public bickering aside and to get the job done on a bi-partisan basis. This time, the Finance Committee failed to get the job done.

This is a ~~low~~ disappointing-point in the history of the Senate Finance Committee, Mr. Chairman. And I know you regret that as much as I do. I don't for a minute think this is what you wanted. But there it is.

Let's finish this charade as quickly as possible, so that those who have led us to this sad moment can score their cheap political points, and so that we can regroup in a few weeks, on a bi-partisan basis, and let's get the job done right so America can get back to work.

Steve Symms

STATEMENT OF SENATOR STEVE SYMMS

SENATE FINANCE COMMITTEE

MARCH 3, 1992

On Health Care

MR. CHAIRMAN: Our health care system has a great many problems. And I would bet most of those problems can be traced to some meddling by the government in the health care market place.

The Finance Committee is at a point where we <u>should</u> be voting on legislation to solve some of the problems that face the health care system. Instead, we're going to vote on a package that, after all the partisan bickering, misses the target completely. There are some provisions in this bill that will help, but the overall result, I fear, will certainly make things worse.

The Health Care Cost Commission, for example. I realize it's an advisory body; however, it will undoubtedly pick up more and more authority as with most commissions established by Congress. What we're really talking about here is the nephew of the 1970's era Council on Wage and Price Controls, only here we restrict it to health and, initially, to health care prices. But will price controls be far behind?

I am also concerned with the tax penalty on insurance companies if they don't comply with the new standards. 25% of gross premiums is fairly steep -- I wonder how the Members of the Finance Committee would handle a 25% cut in their individual budgets? It's a hefty chunk, and if we are out to put insurance companies out of business, this is definitely the way to go.

I hope that's not our goal, but given the underlying agenda of a national health insurance system, maybe putting companies out of the health insurance business is the goal.

The small market reform is another example of how the road to hell is paved with good intentions. I'm sorry to have to be such a pessimist, but you can't violate all the rules of economics with impunity. That's how we got into this mess in the first place.

The result of this small market reform will be that insurance companies will probably leave this market in droves. Maybe that's really the intention. Get the private insurers out of the market to make it easier for national health insurance.

Studying an all-payer system with Medicare rates is just as bad. In my years in the U.S. Senate, Medicare rates are the single issue I can always count on to give me heartburn. No one is satisfied with these rates, and yet, we're eventually going to mandate Medicare rates for all private insurers covering small employers. Is the committee really ready to deal with this?

What we have here, Mr. Chairman, is catastrophic insurance 2 -- the sequel. It's sad we haven't learned much since our last venture into the world of health mandates -- catastrophic 1. I'm only glad when this committee meets in a year or two to repeal this disaster, that I'll be able to watch the turmoil from the peaceful skies of Idaho.

U.S. Senator

Phone: (202) 224-3190

BILL ROTH
NEWS RELEASE

Contact: Verna Hensley or
Ginny Flynn

FOR IMMEDIATE RELEASE:
March 3, 1992

"GET SERIOUS" ABOUT ECONOMIC GROWTH, ROTH SAYS

WASHINGTON -- "As Congress fiddles, the economy burns, and with it, the hopes of real economic growth," Senator William V. Roth Jr., R-DE, said today as the Senate Finance Committee met to consider an economic tax package. Saying the committee should put politics aside and "get serious about passing a viable package which the President would sign into law," Roth criticized the plan put forth by the committee's majority members for failing to address the nation's number one priority: jobs.

"American workers are tired of watching their hopes for jobs, and opportunity being thrown around like a political football, while the Japanese and other foreign competitors do an end run to the international marketplace," Roth said.

"Taxpayers are postponing economic decisions because of Congress' inability to act responsibly, and who can blame them? Each day the Congress refuses to work toward a viable growth package -- one which the President will sign -- more Americans put off economic decisions which could fuel the recovery," he said.

"Unsure about what tax breaks might come to pass, young couples are waiting to buy a house. Companies are putting off buying new equipment in anticipation of a possible investment tax incentive. As long as the possibility of home buyers credits, investment tax incentives, capital gains and passive loss relief are out there, people will wait to make their transactions.

"Every day we delay responsible action, we delay economic recovery," he said.

"The ingredients of a successful, pro-growth economic tax package are well within our grasp," Roth said. "Finance Committee Chairman Bentsen and I have already worked together to push the Bentsen-Roth IRA, a pro-family measure which would boost savings. Even the Democrats in the House of Representatives agree that capital gains taxes must be reduced to stimulate job creating economic activity. An investment tax credit, tax breaks for passive loss in real estate and some form of alternative minimum tax relief are all measures on which this committee should be able to reach agreement -- if everyone is willing to try.

"One thing we all know we cannot agree on is a tax hike. In light of the disastrous results of the 1990 budget summit agreement, I cannot believe we are seriously considering once again raising taxes on American taxpayers," he said. "How many more jobs need to be lost before this Congress learns that raising taxes squelches economic growth and jobs? These tax hikes would deal the death blow to the already weak economy."

"The American people are watching and waiting. They are tired of the statistical games which are used to promote class warfare, pitting taxpayer against taxpayer. This committee has to decide if it is serious about passing a real economic growth plan or merely interested providing the window dressing for political campaigns," Roth said.

STATEMENT OF DAVID L. BOREN

Mr. Chairman, I join with my colleagues in supporting this comprehensive tax legislation. On balance, it provides the middle-income taxpayer with substantial short-term relief, and it represents a first step in our continuing effort to address the long-term economic objectives of our Nation.

First, your proposal provides elements of real relief for middle-income taxpayers. I am particularly supportive of the provision that would allow taxpayers the option of a deduction or a tax credit for interest paid on student loans. This is a proposal that Senator GRASSLEY and I introduced to relieve middle-income Americans of the tremendous burden of paying for a college education for their children.

In addition, I am pleased that the legislation before us today includes an extension of the Targeted Jobs Tax Credit. The groups targeted by this credit comprise an economic underclass, trapped in a vicious cycle of poverty and dependency. These structurally unemployed Americans have great difficulty finding jobs, particularly in these recessionary times. Although I would still urge the Committee to consider making this important provision a permanent one, I understand that concerns about revenue force us to extend this credit for only 18 months.

Not only does the bill address the country's need for short-term economic stimulus, it also begins the process of providing incentives to promote long-term investment and improve our competitiveness in the global marketplace. At the outset, I approve of our acknowledging that the tax code is not economically neutral. It impacts the investment decisions of corporations and of all Americans. We must accept this fact and construct the tax system so that it encourages productive investment and so that it reduces the cost of capital for American businesses.

One aspect of the tax code that has decreased America's ability to compete overseas has been the alternative minimum tax system. While the objective behind the AMT was laudable and while I agree that no corporation that reports profits to its shareholders should entirely avoid paying taxes, the AMT has had unintended economic effects. This legislation addresses some of those effects.

First, the legislation removes gifts of appreciated property from the AMT. Gifts of appreciated property are critical to those sectors of our society that depend heavily on philanthropy for support. For example, eighty percent of the collections in American museums are the result of donations of appreciated assets that are part of our cultural heritage. Land conservation groups depend on gifts of appreciated land to help conserve open space for public enjoyment and protection of important wildlife.

Mr. Chairman, in connection with the extension of the gifts of appreciated property rule, I wish to raise before the Committee an issue which may need our further attention in the future. I'll not press for an amendment today, but I do wish to have expressed, as part of the Committee Report, my views on UBIT and the growing practice of tax-exempt museums developing chains of retail stores.

I am very pleased to see included in this legislation AMT relief for the independent oil and gas industry. In the last few weeks, I have often brought to the attention of this Committee the statistics that dramatically illustrate the plight of this vital industry. They lead to only one conclusion: this industry faces a crisis that will lead to an irreversible decline without decisive action. The provision in the Chairman's bill provides the kind of relief so desperately needed by the independent oil and gas industry. In addition, it simplifies the calculations required by the alternative minimum tax system relating to drilling costs so that independents can actually take advantage of the relief provided them.

I am also pleased that AMT relief is provided generally to corporations wishing to continue a high level of productive investment even in this recessionary climate. Yet I am disappointed that the legislation contains no relief for those corporations that have been paying the AMT for several years and that have not been able to utilize their AMT credits while they still have some value. I am convinced, however, that more far-reaching modifications of the alternative minimum tax system will be considered seriously by this Committee in the next few months.

I am pleased to see the inclusion of one other important provision that is designed to reverse parts of the 1986 Act that went too far. Although we achieved the important goal of eliminating economically-inefficient tax shelters, we also denied to those substantially involved in the real estate industry the ability to deduct passive losses against ordinary income. This legislation ensures that people whose principal occupation is the development of rental real estate will be allowed to offset ordinary income with such losses, thereby stabilizing the real estate market and providing both short- and long-term economic relief.

Finally, Mr. Chairman, I am especially gratified to see the Democratic members of this Committee unite behind a reduction in the capital gains tax rate for currently-held assets, as well as for assets that will be acquired in the future. I have long supported such a proposal because I believe that it decreases the cost of capital in this country and benefits all Americans. The progressive aspect of your proposal ensures that this cannot be characterized as a give-away to the rich. Moreover, the requirement that assets be held at least two years to qualify for capital gains treatment eliminates the possibility that speculative investment will receive this generous treatment.

Certainly, there are parts of this bill that I do not support. I have been very frank with members of this Committee about my dislike of the so-called middle-income tax credit. I believe that Americans do not want the government to provide them with relief that equals only a dollar or less a day. Our constituents are not duped by such proposals -- they know that these provisions do not represent meaningful and lasting relief. Instead, our citizens want us to adopt policies that ensure them and their children a quality education and a productive job. They want us to take serious steps to reduce the deficit before it becomes an insurmountable economic burden on future generations. But I also realize that any bill will contain some provisions that each of us does not support. We must nonetheless unite behind this legislation, which represents a balanced first step to long-term economic progress.

I also ask that our colleagues across the aisle and that the President not dismiss this legislation out-of-hand simply because it contains a fourth tax bracket. The tax rate change proposed by the Chairman is a limited one, affecting only higher-income Americans who have benefitted so greatly from the tax changes of the past several years. It is irresponsible for any of us, whether in the legislative or the executive branch, to refuse to negotiate about any aspect of a responsible tax package, like the one before us today.

I will support this package, Mr. Chairman, and I thank you for your hard work in crafting this package.

FOR IMMEDIATE RELEASE
March 3, 1992

CONTACT: Will Keyser
(202) 224-4373

STATEMENT BY SENATOR MAX BAUCUS
FINANCE COMMITTEE MARK-UP
MARCH 3, 1992

Mr. Chairman, my remarks will be brief because I know that it has been a long night for many and could prove to be a long day for all of us.

First, I want to commend the Chairman for his work in crafting a good, solid package. I am particularly pleased that it responds to the need to encourage long term investment and saving. That is critical to the competitiveness of our economy and our future standard of living.

For example, the capital gains provision is carefully targeted to reward NEW investment in new companies. And the other provisions relating to education, research and development, and tax simplification should help workers and business become more competitive.

I also applaud the chairman for including in the mark his health care proposals, of which I am pleased to be a cosponsor. We all know it is not THE solution to the health care crisis. But they are important steps that will remove some of the burden from small business and those with pre-existing conditions.

And the chairman's child credit also will provide some relief to middle class families, the very group that has lost ground in the past decade.

Again, I want to thank the Chairman for his work on these proposals. We probably all would have done things a little differently, if it had been up to us. But he succeeded in balancing the many competing interests and producing a mark that responds to the needs of the country. I hope it will find bipartisan support on this committee and on the floor.

Thank you.

Senator Dave Durenberger

U.S. Senator for Minnesota

For Immediate Release
March 3, 1992

Contact: Melenie Soucheray
(202) 224-9472

STATEMENT BY SENATOR DAVE DURENBERGER - SENATE FINANCE COMMITTEE - TAX BILL

Mr. Chairman, what we have here is politics, taxes and budget policy bringing out the absolute worst in each other.

Everybody seems to come to this table with an old grudge to settle (including the President): the "fairness" debates of the 1980s, the 1990 budget debacle, the so-called "Pennsylvania message" of last year, and so on. We have all allowed what is "politically urgent" to obscure what is economically important.

The first responsibility of leadership is to define reality. Reality in 1992 is that we need to lower the deficit and raise people's confidence that we are in charge of our future. The process we are engaged in here is almost certain to do the opposite -- on both counts.

We definitely don't need economic lollipops, like 97-cent-a-day tax cuts for the middle class.

We definitely don't need "quick fix" investment incentives financed with debt (reductions in savings). Any economist will tell you that is really giving with one hand and taking away with the other.

And the last thing we need in these uncertain times in our country is a classic display of the same old Washington stuff: noisy, expensive futility.

Too much politics and too little discipline got us to where we are today: a billion-dollar-a-day federal deficit.

How about these for national priorities: we spend ten dollars on interest for every one we spend on education! In fact, we spend more to service the national debt today than we did to run the entire United States government in 1974.

The reality is we need a new way to decide how to spend money, or not spend money, in this government. And we need a new way to decide where to raise the money we need to run it.

-more-

But we are <u>not</u> going to find those new ways -- or the character to enact them -- here, or anywhere this year.

So if we can't do any good, at least let's resolve not to do any further harm.

What good can we do for the economy and the American people? We have in this package two very helpful steps to solve problems people tell us they care about (unlike tax cuts).

First: we should adopt the small group health insurance reforms that are urgently needed and included in the Chairman's package. It's the best substantive thing we can get done this year to improve American health care.

Second: we should adopt the education financing proposals included in the Chairman's package. Senators Simon, Bradley and I have worked hard to find a way to ease the burden of higher education on American families and we think we've found it: the IDEA proposal. It has bipartisan support and we can do it this year.

Then I think we should spend the remainder of the year holding hearings to reexamine this nation's entire approach to taxation. After the political moment has passed in November, we can return next January and markup tax legislation that lays out a path for the future of this country. Not a tax bill for the short term, but a tax code that will set this country on a path toward long-term investment, growth and jobs.

The best thing I can do for this economy and for our future is to vote NO on all the big tax bills. I urge my colleagues, and the administration to open their eyes, lay down their swords, and decide to limit the damage and do the good we can.

-30-

From the office of

SEN. ORRIN HATCH

Washington, D.C. 20510

March 3, 1992 Contact: Paul Smith, 202/224-9854

STATEMENT BY ORRIN G. HATCH

FINANCE COMMITTEE MARKUP

ECONOMIC GROWTH

Thank you Mr. Chairman.

Mr. Chairman, today we have the opportunity to do something good for the American people. They are looking to Congress and this Committee to pass legislation to help lift our economy out of recession and to set the stage for long-term growth in the future.

I had hoped that instead of getting mired in partisan bickering and economic class warfare, we could work together to craft a package to create jobs and long-term economic growth. This is the only way to truly help the American people and give everyone, especially the middle class, economic fairness.

Regrettably, this Committee, as well as the whole Senate, is caught in the middle of a "political theater." While I agree with many of the individual provisions in the Chairman's mark, I cannot support the package as a whole. The majority of the members in the Senate appear intent on following the lead of the House in passing a bill that raises taxes. Increasing individual tax rates is anti-growth and will lose jobs in the long run. This will not serve either the objective of short-term job creation or long-term economic growth.

It is obvious that the President will honor his promise to veto legislation that significantly raises taxes, and that is just what this bill does. Unfortunately, whether vetoed or not, a bill that raises taxes leaves the American people with nothing; no economic stimulus, and no job-creating programs.

Mr. Chairman, time is of the essence here. If we are going to get caught up in the election year political fray, let us go through the motions quickly so we can come back and start to legislate in earnest. We are not that far off from a bipartisan bill. The President's seven points, in some form, are obviously popular on both sides of the aisle. Let us use them to form the basis for compromise and rise above this confrontation. But let us not create disincentives in one group in order to give benefits to another group. That does not make economic sense.

We have the opportunity to create incentives that will make a significant difference in economic behavior by focusing on a narrow bill bold enough to stimulate the lagging economy. Passing a measure that does not provide incentives for taxpayers to increase production, investment, and savings, will merely shift dollars around the economy. Passing a measure that raises taxes will create disincentives for economic growth. We must work together and do something more. A sincere bipartisan effort right now can result in bold legislation that will promote job creation in the short run and sustain long-term growth as well.

Such a package would give the economy a strong push and speed its recovery. More important, it will ease the anxiety that many Americans are feeling today. Mr. Chairman, I strongly believe that we on this Committee can do that and I urge my colleagues to join together in crafting such a plan.

Thank you Mr. Chairman.

UNITED STATES SENATE
COMMITTEE ON FINANCE

Executive Session

Tuesday, March 3, 1992 - 10:00 AM
SD-215 Dirksen Senate Office Building

A G E N D A

To mark up health care and tax legislation.

United States Senate

COMMITTEE ON FINANCE
WASHINGTON, DC 20510-6200

March 3, 1992

The Honorable Lloyd Bentsen
Chairman
Committee on Finance
United States Senate
Washington, D.C. 20510-6200

Dear Mr. Chairman:

It is with the utmost respect for your leadership and vision that we are compelled to send you this letter. Although we may not always see eye-to-eye on every issue, we know you share our commitment to a strong and prosperous America. As a highly regarded member of the Senate and Chairman of the Committee on Finance, we are calling on you to put the good of our great country ahead of politics.

Throughout the country, people from all walks of life are counting on their elected officials to guide them through these tough economic times. Americans rightfully expect us to refrain from pursuing a short-sighted strategy to score points in the next election. Instead, they want us to shed partisan differences and work together to develop a bold long-term strategy to strengthen our economy and propel America into the next century.

Over the last six months, many economists have appeared before Congress and advised us to proceed with great care this year. They cautioned against a short-term fix which will be counterproductive over the long-term. There was a clear consensus that a significant tax increase at a time when the economy is struggling to get back on its feet will not stimulate economic growth and jobs creation.

Regretfully, the majority in the Senate -- like the majority in the House -- appear intent on advancing legislation that will significantly raise taxes while doing little to rebuild the competitive position of America. This approach will not stimulate investment in productive endeavors so that Americans can look forward to securing a good family wage, owning a home, raising a family, and enjoying a prosperous retirement.

Even the Chairman of the House Ways and Means Committee acknowledged that the House bill is essentially a political document, when he said last week: "I really don't want a bill if I can avoid doing it. But the political climate insists we have something." [The New York Times, February 24, 1992]

Clearly, as long as the bill contains significant tax increases, it will be vetoed by the President and the veto will be sustained. If the majority insists on following this course, we urge that it be done expeditiously. Vote the bill out of the Finance Committee today, waive the two-day layover rule, take the bill to Senate floor immediately for final passage, conference quickly with the House, and be done with it.

However, we sincerely hope this futile course will not be pursued. We urge the Committee to lay this bill aside, and begin working together immediately to draft a plan to reinvigorate our economy and provide a blueprint for our future.

This is no time for the Senate to succumb to political expediency. This bill is not a solution to the economic problems facing this country, and we all know it. We have the opportunity to rise above the fray and do something for the good of America. We should seize this opportunity now.

Sincerely,

Bob Packwood | Bob Dole
Bill Roth | Jack Danforth
John Chafee | Dave Durenberger
Chuck Grassley | Steve Symms
Orrin Hatch

MARKUP DOCUMENT FOR S.1872
THE BETTER ACCESS TO AFFORDABLE HEALTH CARE ACT
March 3, 1992

TITLE I: IMPROVEMENTS IN HEALTH INSURANCE AFFORDABILITY FOR SMALL EMPLOYERS

1. INCREASE IN HEATH INSURANCE TAX DEDUCTION FOR THE SELF-EMPLOYED (See tax table.)

2. GRANTS TO STATES FOR SMALL EMPLOYER HEALTH INSURANCE PURCHASING PROGRAMS

PRESENT LAW: Currently there is no Federal grant program to finance group purchasing arrangements to assist small employers in purchasing health insurance. Several states have undertaken related initiatives.

PROPOSAL: A grant program would be established to assist states in developing small employer health insurance group purchasing arrangements. Funds could be expended for administrative costs including marketing and outreach efforts, negotiations with insurers, and performance of administrative functions such as eligibility screening, claims administration and customer service. In awarding grants to states, the Secretary would be required to fund qualified applications employing a variety of approaches to group purchasing.

Such sums as necessary would be authorized for fiscal years 1993 through 1995 for the purpose of funding grant applications.

The Secretary of HHS would by required to conduct an evaluation and report to the Congress by January 1, 1995 on the impact of these programs on the number of uninsured and the price of insurance available to small employers.

3. STUDY OF USE OF MEDICARE RATES BY PRIVATE HEALTH INSURANCE PLANS

PRESENT LAW: In general, prices paid for health care services are arranged privately between insurers and health care providers. No Federal law directs these prices. Some states have laws regulating payments to hospitals by private insurers.

PROPOSAL: The Secretary of Health and Human Services would be directed to study and report to the Congress by January 1, 1993 on the feasibility and desirability of developing prices based on Medicare payment methodologies for use by private health insurance.

The study would include an evaluation of 1) the adjustments needed to apply Medicare payment rules to services provided to the general population; 2) the potential impact of the availability of such prices by all insurers on health insurance premiums and national health care spending; and 3) the potential impact of the use of such prices if they were available only with respect to insurance sold to small employers.

The Secretary would be required to take into account the findings and views of the Prospective Payment Assessment Commission and the Physician Payment Review Commission with respect to these issues.

TITLE II: IMPROVEMENTS IN HEALTH INSURANCE FOR SMALL EMPLOYERS

PRESENT LAW: There is no Federal law regulating the terms of sale of private health insurance sold to small employers. The National Association of Insurance Commissioners (NAIC) has adopted model legislation for state laws governing premium rates and renewability of coverage for health insurance sold to small employers, and guaranteeing availability of health insurance sold to small employers. Fourteen states have enacted legislation similar to the NAIC model on rating and renewability of coverage. Another four states have enacted additional legislation to guarantee the availability of health insurance sold to small employers.

PROPOSAL: Minimum Federal requirements would be established for State laws regarding the sale of health insurance to small employers. The requirements would apply to insurance sold to employers with between 2 and 50 employees working at least 30 hours a week.

The standards would apply to all entities subject to state insurance laws and regulation, including multiple employer welfare arrangements. In the case of a multiple employer welfare arrangement that is fully insured, the standards would apply to the insurer of the arrangement. Self-funded multiple employer welfare arrangements would be subject to state regulation in the same way as under current law. Nothing in the Federal requirements is intended to interfere with a state's ability to regulate licensure or financial solvency of insurers.

Guaranteed Eligibility.- Eligible employees or their dependents could not be excluded from coverage under a small group health insurance plan.

Guaranteed Renewability.- Insurance sold to small employers could not be canceled due to claims experience or health conditions.

Pre-existing condition exclusions.- Newly covered employees and dependents with previous health insurance coverage would generally be protected against pre-existing condition exclusions. In the case of an individual without coverage for a particular service within the 90 day period prior to beginning employment, insurers could exclude coverage for that service for a one-time period of up to 6 months for any pre-existing condition. A pre-existing condition would be defined as one that was diagnosed or treated within 3 months of the beginning of coverage. Individuals with previous health insurance coverage would be given credit for each month of coverage toward the preexisting condition exclusion period. Preexisting condition exclusions could not be applied to services furnished to newborns.

Rating requirements.- Minimum Federal requirements for rating of small employer premiums would limit variation in premiums for health insurance sold to small employers on account of health status, claims experience, duration since issue, industry and occupation.

Rating bands would be established such that the highest premium charged to the lowest premium charged to a small employer with similar demographic characteristics for the same or similar benefits could not exceed 1.5 for the first three years the law is in effect, and 1.35 in subsequent years.

Under limited circumstances, insurers could sort small employers into separate blocks of business, and the rating bands would apply independently to each block of business. Variation in premiums charged between all blocks of business could not exceed 20 percent. Insurers would be allowed to create blocks of business to segregate plans purchased from another insurer, plans provided through an association of small employers, and plans marketed through direct mail or another marketing approach.

These rating bands would not apply to differences in premiums due to age and sex, or geography. Adjustments to premiums based on these factors would have to be applied consistently across small employers. In addition, demographic rating factors would have to be consistent with guidelines developed by the National Association of Insurance Commissioners.

Insurers would disclose to the employer information on rating practices, the impact of rating factors on the employer's premiums, and the potential for future rate changes.

GAO report and Recommendations on Community Rating.- The General Accounting Office would report to the Congress on the impact of the rating requirements on the price of insurance sold to small employers, and would make recommendations for adjusting the minimum rating requirements to eliminate experience rating based on health status and claims experience and to eliminate variation in premiums associated with age and sex and other demographic factors.

Annual Rate Increases- Premiums for a small employer could increase by no more than 5 percent above the underlying trend in health care costs, as measured by the increase in the lowest rate charged by the insurer for the block of business.

Benefit packages.- All insurers offering coverage to small employers must make available at least a standard and a basic benefit package to all small employers in all blocks of business. State laws requiring the coverage of specified items and services would not apply to either benefit package. State laws involving the coverage of newborn children, adopted children or other individuals would continue to govern.

The standard benefit package would provide for the following benefits:

- inpatient and outpatient hospital services, except that mental health services could be limited annually to at least 45 days of inpatient treatment and 20 outpatient visits.

- physician services and diagnostic tests

- preventive services limited to prenatal care, well baby care for children under 1 year, well child care, Pap smears, mammograms and colorectal screening services.

Physician services would be defined to include services lawfully provided by a physician under state medical practice acts, and includes services provided by a dentist, licensed advance-practice nurse, optometrist, podiatrist, or chiropractor acting within the scope of their practices as determined under state law.

Out-of-pocket costs would be limited in several ways. The annual deductible could not exceed $400 for an individual and $700 for a family in 1993. These limits would be indexed to the consumer price index. Coinsurance could not exceed 20 percent, except in the case of outpatient mental health services for which a 50 percent coinsurance rate would apply. An overall annual cap on deductibles and coinsurance would be established at $3,000 for individuals and families in 1993, indexed to the consumer price index thereafter.

The basic benefit package would provide for inpatient and outpatient hospital care, including emergency services; inpatient and outpatient physician services, preventive services which may include prenatal and well-baby care, well child care, mammograms, Pap smears and colorectal screening. Nothing in the Federal requirements prohibits the inclusion of mental health services in the basic benefit package. Deductibles and coinsurance could be imposed. A limit on out-of-pocket spending would be required.

Within the scope of these Federal requirements, a State could choose to define a specific basic benefit package that all insurers must offer, or a State could allow insurers to offer alternative basic benefit packages. The intent of the basic benefit package requirement is to encourage the development of affordable health benefit packages for small employers.

Guaranteed Availability of Coverage.- Insurance coverage would be made available to every small employer within a state. States could choose among alternative approaches to guarantee availability of coverage. These alternatives include 1) mandating that all insurers issue insurance to any small employer, and be required to participate in a reinsurance pool designed to spread risk among insurers, and 2) mandating that all insurers issue insurance to any small employer and allowing voluntary participation in a reinsurance pool, 3) requiring participation in a system for allocating high-risk groups among insurers, and 4) allowing insurers to choose between issuing insurance to any small employer and participating in an allocation system. In addition, a State could apply to the Secretary for approval of a different program guaranteeing the availability of insurance to small employers. Under each approach, states would be required to adopt standards to assure fair marketing of insurance sold to small employers.

General Accounting Office Study.- The General Accounting Office would report to the Congress on (1) the impact of the standards for small group insurance on the availability and price of insurance offered to small employers, differences in available benefit packages, and the number of small employers choosing standard or basic benefit packages; (2) differences in state laws and regulations affecting the price of health insurance plans sold to individuals; and (3) the impact of the standards on the number of small employers offering insurance to employees through a self-funded group health plan.

Development of Standards.- The Secretary of Health and Human Services would request the National Association of Insurance Commissioners (NAIC) to develop standards for State implementation of the statutory requirements by September 30, 1992. If the NAIC fails to act in time, or if the Secretary finds that the NAIC standards do not meet the statutory requirements, the Secretary will develop standards by December 31, 1992. With respect to the alternative guaranteed availability requirements, the NAIC (or the Secretary) would develop standards to implement at least the four alternatives described above.

States would be required to establish a regulatory program for adoption and enforcement of the standards, subject to approval and oversight by the Secretary of Health and Human Services.

The General Accounting Office would conduct periodic reviews to evaluate State compliance.

States could enact more stringent standards. The Secretary of HHS would be authorized to provide waivers for rating band requirements in the case of a state with equally stringent but not identical standards in effect prior to January 1, 1992.

Enforcement of standards: Insurers violating standards would be subject to a Federal excise tax equal to 25 percent of premiums received on all policies sold to small employers. Insurers in states having a regulatory program approved by the Secretary would be exempt from the tax, as would insurers in other States that are individually certified by the Secretary as meeting the Federal standards.

Effective date: The requirements take effect for health insurance plans offered, issued, or renewed to a small employer on or after January 1, 1994, except in states with a legislature that does not meet during 1993. In these states, the requirements would be effective on first day of the first calendar quarter after the close of the first regular legislative session occurring after January 1, 1994.

TITLE III: IMPROVEMENTS IN THE PORTABILITY OF PRIVATE HEALTH INSURANCE

PRESENT LAW: Group health plans often exclude coverage for a period of time for services related to a preexisting medical condition of a newly covered employee or his or her dependents, regardless of previous health insurance coverage. As a result individuals changing jobs may face gaps in insurance coverage for themselves or family members with chronic health conditions, even when both jobs provide similar health benefits.

PROPOSAL: All group health insurance and self-insured employer group health plans would be prohibited from denying or limiting coverage on the basis of medical history or health status, except that a limited preexisting condition exclusion could apply to individuals with respect to services for which they did not previously have health insurance coverage.

Exclusion of coverage for a preexisting condition could not exceed six months. Preexisting conditions would be defined as those that were diagnosed or treated during the three months prior to enrollment.

Individuals would be given credit for previous health insurance coverage. A period of preexisting condition exclusion would be reduced by one month for each month of previous coverage with respect to particular services. Credit would be given for previous coverage ending up to three months prior to the start of coverage under the new health plan.

Insurers or self-insured employer group health plans offering health plans not in compliance with these requirements would be required to retroactively cover any illegally excluded services and pay a tax penalty of $100 a day for each violation.

TITLE IV: HEALTH CARE COST CONTAINMENT

1. HEALTH CARE COST COMMISSION

PRESENT LAW: No provision.

PROPOSAL: A Health Care Cost Commission would be established to advise the Congress and the President on strategies for reducing health care costs.

The Commission would consist of 11 members appointed by the President and confirmed by the Senate. Members would serve for three year terms, except that the terms of initial appointees would be staggered so that the terms of no more than 4 members would expire each year. The term of the Chairman would be coincident with the term of the President.

In appointing members, the President would be required to assure representation of consumers of health services, large and small employers, State and local governments, labor organizations, health care providers, health care insurers, and experts on the development of medical technology.

The Commission would report by March 30th each year on trends in health care spending, the cost of private health insurance, sources of increases in health care costs and comparative trends in other countries. The report would also include the Commission's assessment of public and private strategies for reducing growth in health spending and its recommendations for cost containment efforts.

As part of its first annual report, the Commission would, in consultation with the Secretary of Health and Human Services, recommend a national model uniform claims form and uniform standards for the collection of medical and billing records for use by insurers and providers. The Commission would recommend a strategy and schedule for implementing national use of these forms and standards, taking into account the need for patient confidentiality and special implementation issues, including those of providers in rural areas. The Commission would consider the use of electronic cards or other technology that allows expedited access to medical records and insurance information.

The Commission would also make recommendations to the Secretary of Health and Human Services with respect to the development and ongoing review of standards for managed care plans and utilization review programs. (See item #2).

2. FEDERAL CERTIFICATION OF MANAGED CARE PLANS AND UTILIZATION REVIEW PROGRAMS

PRESENT LAW: Under present law, a health maintenance organization meeting certain standards may apply to the Health Care Financing Administration for certification as a federally qualified health maintenance organization.

PROPOSAL: The Secretary of Health and Human Services would be directed to establish a voluntary certification program for managed care plans and utilization review programs.

Standards for certification of qualified managed care plans would include standards related to the qualification and selection of participating providers, the distribution of providers necessary to assure that plan enrollees have access to needed health services, the provision of benefits for emergency services and the establishment of an ongoing quality assurance program. In order to be certified as a qualified managed care plan, a managed care plan would also have to meet standards identical to those established for designation of qualified utilization review programs.

Standards for certification of qualified utilization review programs include standards related to the qualification of individuals performing utilization review, the utilization review criteria and procedures for evaluating the necessity and appropriateness of health services, the timeliness of UR determinations and procedures for operating an appeals process and standards related to the expenses associated with requests from providers for information needed to conduct UR. The Secretary would be required to periodically review these criteria, taking into account recommendations of the Health Care Cost Commission. (See item 1)

The Secretary could consider a plan or UR program accredited if it meets the requirements of a State licensure program or national accreditation body that the Secretary determines are at least as stringent as the Federal standards.

Certain state laws would not apply with respect to qualified managed care plans and qualified utilization review programs. These include laws that prohibit a qualified managed care plan from including financial incentives for enrollees to use the services of participating providers, laws that prohibit a qualified managed care plan from requiring that services be authorized by a participating primary care physician selected by the enrollee, and laws that prohibit the use of utilization review procedures by a qualified utilization review program or a qualified managed care plan.

3. ADDITIONAL FUNDING FOR OUTCOMES RESEARCH

PRESENT LAW:The Omnibus Budget Reconciliation Act of 1989 authorized funding in the Department of Health and Human Services, through the Agency for Health Care Policy and Research, for research on the outcomes, effectiveness, and appropriateness of health care services and procedures. The law requires evaluations of alternative services and procedures and the development of guidelines for clinical treatments or conditions that account for a significant portion of expenditures under the Medicare program, vary significantly in the type of treatment provided and otherwise meet the priorities of the Medicare program. The law also requires the Secretary to develop standards for uniform collection of data and to provide for the dissemination of research findings and guidelines for the education of health care providers and others. Authorization for appropriations are set at $110 million for fiscal year 1992, two thirds of which is appropriated from the Medicare trust funds; $148 million for 1993, 70 percent of which is appropriated from the Medicare trust funds; and $185 million for 1994, 70 percent of which is appropriated from the Medicare trust funds.

PROPOSAL: Authorization of appropriations would be increased to $175 million in fiscal year 1992, $225 million in fiscal year 1993, $275 million in fiscal year 1994, and $300 million in fiscal year 1995. The amount contributed from the Medicare trust funds in fiscal years 1993 and 1994 would be reduced to 50 percent of the total appropriation.

V. MEDICARE PREVENTION BENEFITS

1. COVERAGE OF CERTAIN IMMUNIZATIONS

Present law.--Medicare generally covers only those health care services that are reasonable and necessary "for the diagnosis and treatment of illness or injury." Thus, Medicare will not pay for services, such as immunizations, that avert (rather than treat) an illness, unless the patient has been directly exposed to the illness. While there are exceptions to this rule, most of them are the result of legislation extending Medicare coverage to a particular item or service, such as the hepatitis B and pneumococcal vaccines.

A Medicare demonstration project under which participants receive annual influenza vaccinations expires September 30, 1992. Under the project, there are State-wide sites in Tennessee, Virginia, Indiana, and Louisiana, as well as smaller sites in Arizona, Massachusetts, Michigan, New York, North Carolina, Ohio, Oklahoma, Pennsylvania, and Texas.

Proposal.--The bill would provide for coverage of annual influenza vaccinations and for tetanus-diphtheria vaccinations every 10 years. Effective for influenza vaccinations furnished on or after October 1, 1992, and for tetanus-diphtheria vaccinations furnished on or after January 1, 1993.

2. COVERAGE OF WELL-CHILD CARE

Present law.--Medicare generally does not cover preventive services. For more information, see the descriptions of current law accompanying the two preceding items.

Proposal.--The bill would provide for coverage of pediatric well-child care, including appropriate immunizations, for children entitled to Medicare who have not attained 7 years of age. This would benefit the approximately 300 children who are entitled to Medicare because of end-stage renal disease. Effective for services furnished on or after January 1, 1993.

3. DEMONSTRATION PROJECTS FOR COVERAGE OF OTHER PREVENTIVE SERVICES

Present law.--Section 9314 of the Consolidated Omnibus Budget Reconciliation Act of 1985 (COBRA) required the Secretary to establish at least five demonstration projects to measure the costs and benefits of providing preventive services to Medicare beneficiaries. These demonstrations, which began in May of 1989, are to continue for four years. The sites are located in North Carolina, Washington State, California (two), Maryland, and Pennsylvania.

Proposal.--The bill would provide for the establishment of an on-going series of demonstrations to evaluate the appropriateness of covering additional preventive services under Medicare. A different service would be provided at each site, so that the effect of that service on Medicare costs could be isolated. The Secretary would be required to evaluate specific services but could extend the demonstrations to include other services as well. Services that the Secretary would be required to evaluate include: glaucoma screening; cholesterol screening and cholesterol reducing drug therapies; screening and treatment for osteoporosis, including tests for bone-marrow density and hormone replacement therapy; screening services for pregnant women, including ultrasound and clamydial testing and maternal serum alfa-protein; one-time comprehensive assessment for individuals beginning at age 65 or 75; and prostate-specific antigen (PSA) testing. While the Secretary would be required to use the sites at which the COBRA demonstrations are currently being conducted, he could designate other sites as well.

4. OTA STUDY OF PROCESS FOR REVIEW OF MEDICARE COVERAGE OF PREVENTIVE SERVICES

Present law.--There is an established process by which Medicare decides whether to cover new medical procedures and technologies.

Proposal.--Subject to the approval of the Technology Assessment Board, the bill would require an Office of Technology Assessment study of the process by which Medicare should decide whether to cover new preventive services in the event that the current statutory exclusion of preventive services from Medicare coverage is repealed.

DESCRIPTION OF S. 1364

(EMPLOYEE BENEFITS SIMPLIFICATION AND EXPANSION ACT OF 1991)

AND PROPOSED MODIFICATIONS

Scheduled for Markup

by the

SENATE COMMITTEE ON FINANCE

on March 3, 1992

Prepared by the Staff

of the

JOINT COMMITTEE ON TAXATION

March 3, 1992

JCX-5-92

SUMMARY CONTENTS

INTRODUCTION

This document,[1] prepared by the staff of the Joint Committee on Taxation, provides a brief description of the provisions of S. 1364 ("Employee Benefits Simplification and Expansion Act of 1991") and proposed modifications. These provisions are scheduled for markup by the Senate Committee on Finance on March 3, 1992.

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[1] This document may be cited as follows: Joint Committee on Taxation, Description of S. 1364 (Employee Benefits Simplification and Expansion Act of 1991) and Proposed Modifications (JCX-5-92), March 3, 1992.

DESCRIPTION OF S. 1364 AND PROPOSED MODIFICATIONS
(Employee Benefits Simplification and Expansion Act of 1991)

A. Nondiscrimination Provisions

1. Definition of highly compensated employee (sec. 101 of the bill)

Description of Bill

The bill provides that an employee is highly compensated if (1) at any time during the preceding year, the employee was a 5-percent owner; or (2) during the current year, the employee is (i) a 5-percent owner or (ii) earns more than $50,000 (indexed; $62,345 in 1992). If no employee is treated as highly compensated under this rule, the highest paid officer is treated as highly compensated except (1) for purposes of applying the nondiscrimination requirements applicable to qualified cash or deferred arrangements (sec. 401(k)) and employer matching and after-tax employee contributions (sec. 401(m)), and (2) for plans maintained by State and local governments and tax-exempt organizations.

The bill modifies the family aggregation rules to provide that if an employee is a family member of a 5-percent owner, the employee and the family member are treated as one highly compensated employee.

Effective date.--Years beginning after December 31, 1992. An employer may elect not to have the amendments made by this provision apply to years beginning in 1993.[2]

Proposed Modifications

Clarify that the determination of whether an employee earns in excess of $50,000 (indexed) would be made based on the preceding, rather than the current, year's compensation. Similarly, the applicable dollar limit for determining if an employee is highly compensated is the prior year's limit.

Repeal the present-law rule that provides that certain family members are aggregated and treated as a single highly compensated employee.

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2 In the description of the bill, all effective dates that were originally years beginning after December 31, 1991, have been changed to years beginning after December 31, 1992, except as otherwise indicated.

2. Cost-of-living adjustments (sec. 102 of the bill)

Description of Bill

The bill provides that the adjustments with respect to a year are based on the increase in the applicable index as of the close of the calendar quarter ending September 30 of the preceding year. Thus, adjusted dollar limits will be published before the beginning of the year to which they apply. Also, dollar limits are generally rounded to the nearest $1,000, except that the limits that relate to elective deferrals and elective contributions to a simplified employee pension plan (SEP) are rounded to the nearest $100.

Effective date.--Years beginning after December 31, 1992.

3. Election to treat base pay as compensation (sec. 103 of the bill)

Description of Bill

The bill provides that an employer may elect to define compensation as an employee's base pay. This election must apply to all employees of the employer, and may be revoked only with permission of the Secretary.

Effective date.--Years beginning after December 31, 1992.

4. Modification of additional participation requirements (sec. 104 of the bill)

Description of Bill

The bill provides that the minimum participation rule applies only to defined benefit plans (not defined contribution plans). Under the bill, a plan is not a qualified plan unless the plan, on each day of the plan year, benefits no fewer than the lesser of 25 employees or 40 percent of all employees of the employer. However, a plan maintained by an employer with only 2 employees must cover both.

Effective date.--Years beginning after December 31, 1991. An employer may elect to apply the provision modifying the minimum participation rule as if included in the Tax Reform Act of 1986.

Proposed Modification

Adopt provision of the bill, but also provide that, for purposes of the rule that permits the minimum participation requirement to be satisfied separately with respect to each line of business of an employer, an employer could demonstrate that a separate line of business exists even if that line of business employs less than 50 employees.

5. **Nondiscrimination rules relating to qualified cash or deferred arrangements, matching contributions, and after-tax employee contributions (sec. 105 of the bill)**

Description of Bill

a. Qualified cash or deferred arrangements

The bill adds an alternative safe harbor method of satisfying the special nondiscrimination test for qualified cash or deferred arrangements. Under the bill, the nondiscrimination test is deemed to be satisfied if the employer either (1) makes a matching contribution on behalf of each nonhighly compensated employee of at least (a) 100 percent of the employee's elective contributions up to 3 percent of compensation and (b) 50 percent of the employee's elective contributions up to 6 percent of compensation, or (2) makes a nonelective contribution to a defined contribution plan of at least 3 percent of each nonhighly compensated employee's compensation, without regard to whether the employee elects to contribute to the cash or deferred arrangement.

The matching contributions and the nonelective contributions must be 100-percent vested. In addition, the employer is required to notify employees of the employees' rights and obligations under the arrangement.

The bill also modifies the method of determining excess contributions under the present-law nondiscrimination test. Under the bill, excess contributions are allocated among highly compensated employees beginning with the employees with the highest dollar amount of contributions.

b. Employer matching contributions

Under the bill, the special nondiscrimination test for employer matching contributions (but not for after-tax employee contributions) is deemed satisfied if (1) the plan meets the nonelective contribution or matching contribution requirements applicable to the cash or deferred arrangement safe harbor, (2) employees are notified of the plan, and (3) matching contributions are not made with respect to employee contributions of elective deferrals in excess of 6 percent of compensation.

Effective date.--Plan years beginning after December 31, 1992.

Proposed Modification

Adopt provision of the bill, but also provide that, in applying the present-law nondiscrimination test, the amount that highly compensated employees can defer in a year is based on the previous year's average deferral percentage (ADP) for nonhighly compensated employees. A special rule would apply in the first year a cash or deferred arrangement is maintained. A corresponding change would be made to the nondiscrimination test applicable to employer matching and after-tax employee contributions.

B. Distributions

1. Rollovers of qualified plan distributions (sec. 201 of the bill)

Description of Bill

The bill allows an employee or surviving spouse to roll over any portion of a qualified plan distribution, other than (1) a minimum required distribution or (2) a distribution attributable to after-tax employee contributions. If any portion of a lump-sum distribution is rolled over, averaging is not available with respect to the rest of the distribution.

Effective date.--Distributions after December 31, 1991.

Proposed Modification

Modify the bill to provide that an employee or surviving spouse of an employee would be permitted to roll over any portion of a qualified plan distribution received, other than a distribution that is (1) a minimum required distribution, (2) attributable to after-tax employee contributions, or (3) part of a stream of periodic payments payable over a period of 10 years or more, or over the life (or life expectancy) of the employee or the joint lives (or joint life expectancies) of the employee and his or her beneficiary.

Effective date.--Distributions after date of enactment.

2. Rules relating to lump-sum distributions (sec. 201 of the bill)

Description of Bill

Income averaging

The bill repeals 5-year forward income averaging for lump-sum distributions. The bill retains the special grandfather rules under the Tax Reform Act of 1986 for individuals who had attained age 50 by January 1, 1986.

Excise tax on excess distributions

The bill technically repeals the special higher ceiling (i.e., $750,000) applicable to lump-sum distributions for purposes of determining whether an individual receives excess distributions during any calendar year.

Effective date.--Distributions after December 31, 1992.

Proposed Modifications

Excise tax on excess distributions

Provide that a taxpayer may elect to determine whether he or she receives excess distributions during any calendar year by applying the special higher ceiling (i.e., $750,000 in 1992) that applies to lump-sum distributions under present law. Not more than one such election may be made with respect to any taxpayer. A taxpayer that has applied the $750,000 limit under present law may not elect to have this provision apply. The provision would be effective for distributions after December 31, 1992.

$5,000 death benefit exclusion

Repeal the exclusion from gross income of up to $5,000 of employer-provided death benefits effective for distributions after December 31, 1992.

Recovery of basis

Provide that the portion of an annuity distribution from a qualified retirement plan that represents nontaxable return of basis generally is determined under a method similar to the present-law simplified alternative method provided by the Internal Revenue Service (IRS Notice 88-118). However, the simplified method would not apply if the primary annuitant has attained age 75 on the annuity starting date unless there are at least 5 years of guaranteed payments under the annuity. The provision would be effective for annuity starting dates after December 31, 1992.

3. Trustee-to-trustee transfers (sec. 202 of the bill)

Description of Bill

The bill generally requires that distributions in excess of $500 be transferred directly to an IRA or to a qualified defined contribution plan that provides for the acceptance of the transfer. Annuity distributions, distributions after age 55, distributions on account of the death of the employee (other than distributions to the surviving spouse), and hardship distributions are not subject to the transfer requirement.

Effective date.--Distributions in plan years beginning after December 31, 1993.[3]

3 This provision of the bill was originally effective for distributions in plan years beginning after December 31, 1992.

4. Minimum required distributions (sec. 203 of the bill)

Description of Bill

The bill provides that, except in the case of 5-percent owners of an employer and IRA owners, distributions are required to begin by the April 1 of the calendar year following the later of the calendar year in which (1) the employee attains age 70-1/2[4] or (2) the employee retires. As under present law, distributions to 5-percent owners and IRA owners are required to begin by the April 1 following the year in which the individual attains age 70-1/2.

The benefits of participants who continue to work for an employer after attaining age 70-1/2 are required to be actuarially increased to take into account the period after age 70-1/2 during which the employee receives no benefits under the plan.

Effective date.--Years beginning after December 31, 1992.

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4 Age 70-1/2 would be changed to age 70 under another provision of the bill, described below.

C. Miscellaneous Provisions

1. Modification to definition of leased employee (sec. 301 of the bill)

Description of Bill

The bill replaces the "historically performed" test with a new rule defining who must be considered a leased employee. Under the bill, an individual is not considered a leased employee unless the services are performed under the control of the service recipient.

Effective date.--Years beginning after December 31, 1983.

Proposed Modification

Clarify that the provision is not intended to expand the scope of the leased employee rule.

2. Half-year requirements (sec. 302 of the bill)

Description of Bill

The bill changes age 70-1/2 to age 70, and age 59-1/2 to age 59 for purposes of the qualified plan rules.

Effective date.--Years beginning after December 31, 1992.

3. Plans for self-employed individuals (sec. 303 of the bill)

Description of Bill

The bill eliminates the special aggregation rule for plans maintained by self-employed individuals.

Effective date.--Years beginning after December 31, 1992.

4. Full-funding limitation of multiemployer plans (sec. 304 of the bill)

Description of Bill

The bill provides that multiemployer plans are not subject to the 150 percent of current liability full funding limitation and that an actuarial valuation need only be performed every 3 years in the case of a multiemployer plan.

Effective date.--Years beginning after December 31, 1991.

Proposed Modification

Modify the multiemployer full funding limit in the Internal Revenue Code.

5. Affiliation requirements for employers jointly maintaining a voluntary employees' beneficiary association (VEBAs) (sec. 305 of the bill)

Description of Bill

The bill provides that employers are affiliated for purposes of the VEBA requirements under the regulations if (1) the employers are in the same line of business, (2) the employers act jointly to perform tasks that are integral to the activities of each of the employers, and (3) these joint activities are sufficiently extensive that maintenance of a common VEBA is not a major part of such joint activity. This clarification of present law applies retroactively.

Effective date.--Years beginning before, on, or after the date of enactment.

Proposed Modification

In addition to the requirements that must be satisfied under the bill, add the requirement that a substantial number of the employers who contribute to the VEBA are exempt from tax under the Internal Revenue Code.

Effective date.--Clarify that the provision is intended to be a clarification of present law.

6. Treatment of governmental plans (sec. 306 of the bill)

Description of Bill

The bill makes a number of modifications to the limits on contributions and benefits as applied to plans maintained by State and local governments. The bill exempts participants of State and local government defined benefit plans from the 100 percent of high 3-year average compensation limitation. Also, benefits provided under a "qualified excess benefit arrangement" (which is treated as a nonqualified deferred compensation plan for tax purposes) are not taken into account for purposes of applying the limits on contributions and benefits. Survivor and disability benefits provided under State and local government plans are also exempt from the limits on contributions and benefits.

The bill also provides that the compensation of participants in such plans includes, in addition to the usual amounts, amounts contributed pursuant to a salary reduction agreement that are not includible in the participant's income.

Under the bill, governmental plans are treated as satisfying the limits on contributions and benefits for all taxable years beginning before the date of enactment.

Effective date.--Taxable years beginning after date of enactment.

7. Simplified employee pensions (SEPs) (sec. 307 of the bill)

Description of Bill

a. Salary reduction SEPs

The bill provides that employers with 100 or fewer employees may maintain salary reduction SEPs and repeals the 50-percent participation requirement for such SEPs. The bill also provides that the safe harbors available to qualified cash or deferred arrangements under the bill apply to salary reduction SEPs if employees are notified of the provisions of the SEP.

b. Eligibility requirements

The bill replaces the 3-out-of-5 years service requirement under present law with a requirement that employees who have at least 1 year of service must be eligible to participate.

Effective date.--Years beginning after December 31, 1992.

8. Contributions on behalf of disabled employees (sec. 308 of the bill)

Description of Bill

Under present law, an employer may elect to continue making contributions on behalf of employees other than highly compensated employees who become disabled. The bill extends present-law treatment to disabled highly compensated employees if continuing contributions to the plan are available to all disabled participants. The employer need not make an election to have the special rule apply.

Effective date.--Years beginning after December 31, 1992.

9. **In-service distributions from rural cooperative plans (sec. 309 of the bill)**

Description of Bill

The bill conforms the rules for distributions from cash or deferred arrangements maintained by rural cooperatives to the rules applicable to other cash or deferred arrangements by permitting distributions after the attainment of age 59-1/2.[5]

Effective date.--Effective as if included in section 1011(k)(9) of the Technical and Miscellaneous Revenue Act of 1988.

10. **Reports of pension and annuity payments (sec. 310 of the bill)[6]**

Description of Bill

The bill incorporates into the general penalty structure the penalties for failure to provide information reports to the IRS and to participants relating to pension payments. Generally, the penalty is $50 for each return with respect to which a failure occurs, up to a maximum of $250,000 per year. The bill does not require reports of pension and annuity payments of less than $10.

Effective date.--Returns and statements required to be filed after December 31, 1992.

11. **Repeal of limitation on ability of tax-exempt employers to maintain cash or deferred arrangements (sec. 311 of the bill)**

Description of Bill

The bill permits nongovernmental tax-exempt organizations to maintain qualified cash or deferred arrangements.

Effective date.--Years beginning after December 31, 1989.

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[5] Age 59-1/2 would be changed to age 59 under another provision of the bill, described above.

[6] This provision is also included in section 702 of S. 1394, the Tax Simplification Act of 1991.

Proposed Modification

Effective date.--Years beginning after December 31, 1992.

12. Date for adoption of plan amendments (sec. 312 of the bill)

Description of Bill

The bill provides that if any provision of the bill requires a plan amendment, the amendment is not required to be made before the first plan year beginning on or after January 1, 1993, if (1) during the period after the provision takes effect, the plan is operated in accordance with the requirements of the provision, and (2) the plan amendment applies retroactively to the provision's effective date.

Effective date.--Date of enactment.

D. Additional Provisions

1. Alternative full funding limitation

<u>Description of Bill</u>

No provision.

<u>Proposed Modification</u>

Provide that an employer may elect to disregard the 150 percent of current liability full funding limitation if each plan in the employer's controlled group is not top heavy and the average accrued liability of active participants is at least 80 percent of the plan's total accrued liability (the "alternative full funding limitation"). The Secretary would be required to adjust the 150 percent of current liability full funding limitation (but not below 140 percent) for employers that do not use the alternative full funding limit to ensure that the election by employers to disregard the 150-percent limit does not result in a substantial reduction in Federal revenues for any fiscal year.

<u>Effective date</u>.--Date of enactment.

2. Duties of master and prototype plan sponsors

<u>Description of Bill</u>

No provision.

<u>Proposed Modification</u>

Authorize the IRS to define the duties of organizations that sponsor master and prototype, regional prototype, and other preapproved plans. Also provide that the Secretary could relax the rules prohibiting cutbacks in accrued benefits when an employer replaces an individually designed plan with a preapproved plan.

<u>Effective date</u>.--January 1, 1993.

3. Disaggregation of union plans

<u>Description of Bill</u>

No provision.

<u>Proposed Modification</u>

Provide that employers may elect to take employees covered by a collective bargaining agreement into account in applying the coverage tests to a nonunion plan (sec. 410(6)), in applying the general nondiscrimination rule to a nonunion plan (sec. 401(a)(4)), and in determining separate lines of business (sec. 414(a)) if the union employees benefit under the same plan on the same terms.

Effective date.--Years beginning after December 31, 1992.

4. Uniform retirement age

Description of Bill

No provision.

Proposed Modification

Provide that, for purposes of the general nondiscrimination rule (sec. 401(a)(4)), the social security retirement age (as defined under sec. 415(b)(8)) is treated as a uniform retirement age, and that subsidized early retirement benefits and joint and survivor annuities that are based on social security retirement age are treated as being available on the same terms.

Effective date.--Years beginning after December 31, 1992.

5. Use of excess assets of black lung benefit trusts for retire health care benefits

Description of Bill

No provision.

Proposed Modification

Allow excess assets in qualified black lung benefit trusts to be used to pay accident and health benefits or premiums for insurance for such benefits (including administrative and other incidental expenses relating to such benefits) for retired coal miners and their spouses and dependents. The amount of assets available for such purpose would be subject to a yearly limit as well as an aggregate limit. The yearly limit would be the amount of assets in excess of 110 percent of the present value of the liability for black lung benefits determined as of the close of the preceding taxable year of the trust. The aggregate limit would be the amount of assets in excess of 110 percent of the present value of the liability for black lung benefits determined as of the close of the taxable year of the trust ending prior to the effective date, plus earnings thereon. Each of these determinations would be required to be made by an independent actuary.

The amounts used to pay retiree accident or health benefits would not be includible in the income of the company, nor would a deduction be allowed for such amounts.

Effective date.--Taxable years beginning after December 31, 1991.

6. Special coverage rule for airline pilots

Description of Bill

No provision.

Proposed Modification

Extend the present-law treatment of plans maintained for union pilots to plans maintained for nonunion pilots who are employed by one or more common carriers or by carriers transporting mail for, or under contract with, the United States Government.

Effective date.--Years beginning after December 31, 1992.

7. Establish commission on retirement income policy

Description of Bill

No provision.

Proposed Modification

Establish a commission to study national retirement income policy. The commission would be directed to submit a report to the Congress by Labor Day 1994, the 20th anniversary of the enactment of the Employee Retirement Income Security Act of 1974.

Joint Committee on Taxation
JCX-6-92
March 3, 1992

DESCRIPTION OF TAXPAYER BILL OF RIGHTS 2 PROVISIONS (Scheduled for Markup by the Senate Committee on Finance on March 3, 1992)

I. Additional Safeguards to Protect Taxpayers' Rights

1. Establishment of Taxpayers' Advocate

Present Law

The IRS Ombudsman assists taxpayers in resolving administrative difficulties with the IRS.

Explanation of Provision

The provision statutorily establishes the position of Taxpayers' Advocate in the IRS as a replacement for the Ombudsman. The Advocate would be appointed by the Commissioner. The provision also requires detailed annual reports to the tax-writing committees, provides that problems resolution officers report to the Taxpayer Advocate, and provides that the Taxpayer Advocate report directly to the IRS Commissioner.

2. Expansion of Authority to Issue Taxpayer Assistance Orders (TAOs)

Present Law

The Ombudsman may issue a Taxpayer Assistance Order, which requires the IRS to cease taking an action (such as a collection action).

Explanation of Provision

The provision permits the issuance of a TAO requiring the IRS to take action (such as issue a refund faster), deletes the requirement of present law that the hardship experienced by the taxpayer be "significant" as a condition for the issuance of a TAO, provides that only the Taxpayer Advocate, the Commissioner of the IRS, or a superior of those two positions, as well as a delegate of the Taxpayer Advocate, may modify or rescind a TAO, and permits the TAO to specify a time period within which the TAO must be followed.

II. Modifications to Installment Agreement Provisions

3. Notification of Reasons for Termination of Installment Agreement

<u>Present Law</u>

The IRS must give prior notice and an explanation before it terminates an installment agreement because the taxpayer's financial condition has changed.

<u>Explanation of Provision</u>

The provision requires that this notice be given before any termination (except in cases of jeopardy).

4. Administrative Review of Denial of Request for Installment Agreement

<u>Present Law</u>

The Code does not require that the IRS provide an administrative review of denials of installment agreements.

<u>Explanation of Provision</u>

The provision requires the IRS to provide written notice of the reasons for denial of an installment agreement. The IRS also must establish procedures for independent administrative review of denials and terminations of installment agreements.

III. Interest

5. Expansion of Authority to Abate Interest

<u>Present Law</u>

IRS may in its discretion abate interest attributable to IRS error or delay in performing a ministerial act.

<u>Explanation of Provision</u>

The provision requires the IRS to abate interest in any case in which the taxpayer establishes that there was an unreasonable and excessive IRS delay and the taxpayer has fully cooperated in resolving outstanding issues. In order to allow the taxpayer to develop the facts, the IRS shall be required, upon written request, to provide the taxpayer within 30 days with all information and relevant records that the IRS has with respect to the history of the taxpayer's case for the time period involved. The IRS shall develop a form for the purpose of such requests.

6. Extension of Interest-Free Period for Payment of Tax After Notice and Demand

Present Law

The Code provides a 10-day interest-free period within which taxpayers may pay after notice and demand is made.

Explanation of Provision

The provision extends from 10 to 21 days the interest-free period within which taxpayers may pay after notice and demand is made, applicable only to amounts of less than $100,000 (amounts of $100,000 and above continue to be subject to a 10 day period).

IV. Joint Returns

7. Requirement of Separate Deficiency Notices in Certain Cases

Present Law

IRS must send duplicate original deficiency notices to both spouses when the IRS has been notified that separate residences have been established.

Explanation of Provision

This rule will apply to all instances in which the spouses did not file a joint return for the most recent taxable year.

8. Disclosure of Collection Activities With Respect to a Joint Return

Present Law

It is unclear whether IRS has authority to disclose to one spouse whether the IRS has attempted to collect a deficiency arising from a joint return from the other spouse.

Explanation of Provision

The provision requires the IRS, upon written request of the spouse, to disclose in writing to the spouse whether the IRS has attempted to collect a deficiency from the other spouse, the general nature of the collection activities, and the amount collected.

9. Joint Return May be Made After Separate Returns Without Full Payment of Tax

Present Law

Married taxpayers who had previously filed separate returns may not file a joint return without first fully paying the tax.

Explanation of Provision

The provision permits married taxpayers who had previously filed separate returns to file joint returns without fully paying the tax.

10. Representation of Absent Divorced or Separated Spouse by Other Spouse

Present Law

A taxpayer who has filed a joint return with a spouse may represent the spouse with respect to a deficiency for any year a joint return was filed. IRS administrative procedures may allow each spouse to appeal separately from the statutory notice of deficiency.

Explanation of Provision

The provision provides that an individual who had filed a joint return with a spouse but who is no longer married to that spouse (or no longer resides in the same household) may not represent the absent spouse at an examination of that return unless the absent spouse permits it in writing.

V. Collection Activities

11. Notice of Proposed Deficiency

Present Law

Although not statutorily required to do so, the IRS often issues a notice of proposed deficiency prior to issuance of a notice of deficiency. Failure to issue a notice of proposed deficiency does not invalidate the notice of deficiency.

Explanation of Provision

The provision requires IRS to issue a notice of proposed deficiency in every instance (except jeopardy). The notice of proposed deficiency must be mailed at least 60 days before any notice of deficiency. Failure to issue a notice of proposed deficiency would invalidate the notice of deficiency. The provision is effective one year from the date of enactment.

12. **Modifications to Lien and Levy Provisions**

<u>Present Law</u>

IRS may withdraw a notice of a lien only if the notice was erroneously filed or if the underlying lien has been paid, bonded, or become unenforceable. IRS may return levied property only when the taxpayer has overpaid its tax liability.

<u>Explanation of Provision</u>

The provision permits the IRS to withdraw a notice of a lien in specified situations. Upon the taxpayer's request, the IRS shall notify credit agencies and financial institutions of the withdrawal. Further, the IRS shall return levied property in parallel specified situations. Finally, the provision increases the dollar value of certain items exempt from levy and indexes those amounts for inflation.

13. **Offers-in-Compromise**

<u>Present Law</u>

The IRS can compromise any assessed tax. An opinion of the Chief Counsel is necessary for any compromise of $500 or more. Information relating to accepted compromises is public.

<u>Explanation of Provision</u>

The provision clarifies that the IRS may make any compromise that would be in the best interests of the United States and raises the threshold above which an opinion of the Chief Counsel of the IRS is necessary from $500 to $50,000. The provision requires that opinions below the $50,000 threshold be subject to continuing quality review.

14. **Notification of Examination**

<u>Present Law</u>

IRS generally notifies a taxpayer in writing before commencing an examination (sometimes it does so by telephone).

<u>Explanation of Provision</u>

IRS must both notify a taxpayer in writing that the taxpayer is under examination and furnish a copy of Publication 1, <u>Your Rights as a Taxpayer</u>, prior to commencing any examination.

15. Recovery of Civil Damages for Unauthorized Collection Action

Present Law

A taxpayer may sue the United States for up to $100,000 of damages caused by an IRS employee who recklessly or intentionally disregards the provisions of the Code or Treasury regulations.

Explanation of Provision

The provision increases the cap to $1 million with respect to reckless or intentional acts. In addition, it permits a taxpayer to sue the United States for damages caused by an IRS employee who negligently disregards the provisions of the Code or regulations, subject to a cap of $100,000 in damages.

16. Designated Summons

Present Law

The period for assessment of additional tax with respect to most tax returns, corporate or otherwise, is three years. The IRS and the taxpayer can together agree to extend the period, either for a specified period of time or indefinitely. The taxpayer may terminate an indefinite agreement to extend the period by providing notice to the IRS on the appropriate form.

During an audit, the IRS may seek information by issuing an administrative summons. Such a summons will not be enforced by judicial process unless the Government (as a practical matter, the Department of Justice) seeks and obtains an order for enforcement in Federal court.

In certain cases the running of the assessment period is suspended during the period (if any) in which the parties are in court for the purpose of obtaining or avoiding judicial enforcement with respect to an administrative summons. Such a suspension is provided with respect to a corporate tax return if a summons is issued at least 60 days before the day on which the limitation period (as extended, if extensions have been made) is scheduled to expire. In this case, suspension is only permitted if the summons clearly states that it is a "designated summons" for this purpose. Only one summons may be treated as a designated summons for purposes of any one tax return. The limitations period is suspended during the judicial enforcement period of the designated summons and of any other summons relating to the same tax return that is issued within 30 days after the designated summons is issued.

Under current internal procedures of the IRS, no designated summons is issued unless first reviewed by the Office of Chief Counsel to the IRS, including review by an IRS Deputy Regional Counsel for the Region in which the audit occurs.

Explanation of Provision

The provision requires that issuance of any designated summons be preceded by review by the Regional Counsel, Office of Chief Counsel to the IRS, for the Region in which the audit occurs.

In addition, the provision requires that the corporation whose return is in issue be promptly notified in writing in any case where the Secretary issues a designated summons (or another summons litigation over which tolls the running of the assessment period under the designated summons procedure) to a third party. The provision applies to summonses issued after date of enactment.

VI. Information Returns

17. Phone Number of Person Providing Payee Statements Required to be Shown on Such Statement

Present Law

Businesses are not required to put their telephone numbers on information returns.

Explanation of Provision

The provision requires businesses to put their telephone numbers and the name of a contact person on information returns (1099 forms).

18. Civil Damages for Fraudulent Filing of Information Returns

Present Law

Present law does not provide for civil damages for fraudulent filing of information returns.

Explanation of Provision

If a person willfully files a false or fraudulent information return with respect to payments purported to be made to another person, the other person may bring a civil action for damages.

19. Requirement to Verify Accuracy of Information Returns

Present Law

Deficiencies determined by the IRS are generally afforded a presumption of correctness.

Explanation of Provision

If a taxpayer asserts a reasonable dispute with respect to any income reported on an information return and has fully cooperated, the IRS shall have the obligation in court to introduce evidence of the deficiency (beyond the Form 1099 itself) in order to prevail.

VII. Modifications to Penalty for Failure to Collect and Pay Over Taxes

20. Trust Fund Taxes

Present Law

A responsible officer is subject to a penalty equal to 100 percent of trust fund taxes (social security and withheld income taxes) that are not paid to the Government on a timely basis. IRS provides for administrative appeals as to whether a person is in fact a responsible officer.

Explanation of Provision

The provision requires IRS to issue a notice to an individual the IRS has determined to be a responsible officer at least 60 days before issuing a notice and demand for the penalty. After exhausting administrative remedies within the IRS, the taxpayer may seek a declaratory judgment in the Tax Court as to whether the taxpayer is in fact a responsible officer.

21. Disclosure of Certain Information Where More Than One Person Is Subject to Responsible Officer Penalty

Present Law

It is unclear whether IRS has authority to disclose to a responsible officer whether the IRS has attempted to collect from other responsible officers.

Explanation of Provision

The IRS shall, upon written request of the responsible officer, disclose in writing to the responsible officer whether the IRS has attempted to collect a deficiency from any other responsible officers, the general nature of collection activities, and the amount collected.

22. Penalties Under Section 6672

<u>Present Law</u>

A responsible officer is subject to a penalty equal to 100 percent of trust fund taxes that are not paid to the Government on a timely basis.

<u>Explanation of Provision</u>

The IRS must print appropriate warnings and issue new publications containing information regarding this penalty. This penalty does not apply to volunteer officers of tax-exempt organizations if they are unpaid and do not participate in the day-to-day or financial activities of the organization. The IRS must provide prompt notification of failures to deposit trust fund taxes.

VIII. Awarding of Costs and Certain Fees

23. Attorney's Fees: Recovery for Costs during IRS Appeals Process

<u>Present Law</u>

Taxpayers may recover reasonable administrative costs under the same conditions that attorney's fees are recoverable, commencing with the earlier of the notice of decision by IRS Appeals or the notice of deficiency.

<u>Explanation of Provision</u>

The provision expands the availability of administrative costs by moving the commencement date to the earlier of the notice of proposed deficiency or the notice of deficiency. Once a taxpayer substantially prevails in litigation and files a written request, the IRS is required to provide within 30 days all information and relevant records of the IRS concerning the history of the taxpayer's case and the substantial justification for the position taken by the IRS. The IRS shall develop a form for this purpose.

24. Increase Limit on Attorney Fees

<u>Present Law</u>

Allowable attorney's fees may not exceed $75 per hour, unless the court determines that the cost of living or another factor justifies a higher rate.

Explanation of Provision

The provision indexes the maximum rate for inflation, effective from the date the $75 rate became effective.

25. Attorney's Fees: Failure to Agree to Extension Not Taken Into Account

Present Law

To be eligible to receive attorney's fees, a taxpayer must have exhausted administrative remedies in the IRS. Under Treasury regulations, failure to agree to extend the statute of limitations is considered to be failure to exhaust administrative remedies. The Tax Court has held this aspect of the regulations to be invalid.

Explanation of Provision

Failure by the taxpayer to agree to an extension of the statute of limitations for assessment is not to be taken into account for purposes of determining whether the taxpayer is entitled to receive attorney's fees.

IX. Other Provisions

26. Required Content of Certain Notices

Present Law

IRS tax deficiency notices must describe the basis for and identify the amounts of tax, interest, and penalties.

Explanation of Provision

IRS notices must contain more detailed information.

27. Relief from Retroactive Application of Treasury Department Regulations

Present Law

Treasury may prescribe the extent (if any) to which regulations shall be applied without retroactive effect.

Explanation of Provision

Any proposed or temporary Treasury regulation shall apply prospectively from the date of publication of the regulation in the Federal Register (unless specifically superseded by subsequent legislation authorizing a retroactive effective date or unless Treasury permits taxpayers to elect to apply the regulations retroactively and the taxpayer so elects). Final regulations may take effect from the date the proposed or temporary regulations are published. For the period from the effective date of the statute until the publication of the proposed or temporary regulations, taxpayers will be governed by the statute and other authorities, as under present law.

28. Required Notice to Taxpayers of Certain Payments

Present Law

The IRS receives payments that it cannot associate with any outstanding tax liability.

Explanation of Provision

The IRS must make reasonable efforts to notify taxpayers who have made payments that IRS cannot associate with any outstanding tax liability.

29. Prohibition of Exchanging Confidential Client Information for Forgiveness of Taxes

Present Law

It is unlawful for any person who prepares a tax return for compensation knowingly or recklessly to disclose tax return information.

Explanation of Provision

It is unlawful for any Federal employee to forgive (or offer to forgive) any taxes due from an attorney, certified public accountant, or enrolled agent in exchange for information about that person's clients.

DESCRIPTION OF CHAIRMAN'S MARK:

TAX PROPOSALS RELATING TO WORKING FAMILIES, LONG-TERM ECONOMIC GROWTH, AND TAX FAIRNESS

Scheduled for Markup

by the

SENATE COMMITTEE ON FINANCE

On March 3, 1992

Prepared by the Staff

of the

JOINT COMMITTEE ON TAXATION

March 3, 1992

JCX-7-92

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INTRODUCTION

This document,[1] prepared by the staff of the Joint Committee on Taxation, provides a description of Chairman Bentsen's Mark on tax proposals relating to working families, long-term economic growth, and tax fairness. The tax proposals are scheduled for markup by the Senate Committee on Finance on March 3, 1992.

(Separate Joint Committee on Taxation staff documents are prepared describing proposals relating to pension simplification, other tax simplification, and Taxpayer Bill of Rights.)

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1 This document may be cited as follows: Joint Committee on Taxation, Description of Chairman's Mark: Tax Proposals Relating to Working Families, Long-Term Economic Growth, and Tax Fairness (JCX-7-92), March 3, 1992.

Description of Proposal

The proposal would provide a $300 income tax credit for each qualifying child of the taxpayer. A "qualifying child" would be defined as a child under age 16 who resided with the taxpayer for more than 6 months during the taxable year. The tax credit would offset regular tax liability and would not be refundable (though through the offset of tax liability, the tax credit could act to increase the amount of refund from the earned income tax credit that a taxpayer might receive). The credit amount would be indexed for inflation. In addition, the credit would be phased out ratably for higher-income taxpayers with adjusted gross income between $50,000 and $70,000.

Effective Date

The proposal would be effective January 1, 1992.

2. Simplification and Expansion of Earned Income Tax Credit

Present Law

Eligible low-income workers are able to claim a refundable earned income tax credit (EITC) of up to 17.6 percent (18.4 percent for taxpayers with more than one qualifying child) of the first $7,520 of earned income for 1992. The maximum amount of credit for 1992 is $1,324 ($1,384 for taxpayers with more than one qualifying child). This maximum credit is reduced by 12.57 percent (13.14 percent for taxpayers with more than one qualifying child) of earned income (or adjusted gross income, if greater) in excess of $11,840. The EITC is totally phased out for workers with earned income (or adjusted gross income, if greater) over $22,370. The maximum amount of earned income on which the EITC may be claimed and the income threshold for the phaseout of the EITC are indexed for inflation. Earned income consists of wages, salaries, other employee compensation, and net self-employment income.

The credit rates for the EITC change over time under present law, as shown in the following table.

	One qualifying child--		Two or more qualifying children--	
Year	Credit rate	Phaseout rate	Credit rate	Phaseout rate
1993	18.5	13.21	19.5	13.93
1994 and after	23.0	16.43	25.0	17.86

A supplemental young child credit is available to taxpayers with qualifying children under the age of one year. This young child credit rate is 5 percent and the phase-out rate is 3.57 percent. It is computed on the same income base as the ordinary EITC. The maximum supplemental young child credit for 1992 is $376. If a taxpayer claims the supplemental young child credit, the child that qualifies the taxpayer for such credit is not a qualifying individual for purposes of the dependent care tax credit (sec. 21).

A supplemental health insurance credit is available to taxpayers who provide health insurance coverage for their qualifying children. This health insurance credit rate is 6 percent and the phase-out rate is 4.285 percent. It is computed on the same income base as the ordinary EITC, but the credit claimed cannot exceed the out-of-pocket cost of the health insurance coverage. In addition, the taxpayer is denied an itemized deduction for medical expenses of qualifying insurance coverage up to the amount of credit claimed. The maximum supplemental health insurance credit for 1992 is $451.

Description of Proposal

The proposal would increase the basic EITC rate for taxpayers with two or more qualifying children as shown in the following table.

	One qualifying child--		Two or more qualifying children--	
Year	Credit rate	Phaseout rate	Credit rate	Phaseout rate
1992	17.6	12.57	20.15	14.39
1993	18.5	13.21	21.25	15.17
1994 and after	23.0	16.43	26.75	19.10

The proposal would permit taxpayers to include all health insurance expenses as medical expenses, subject to the 7.5 percent of adjusted gross income floor on deductible medical expenses, regardless of whether these expenses had been used to claim the health insurance component of the EITC. The proposal would also permit a self-employed taxpayer to claim the allowable deduction for health insurance costs and to use the full amount of these expenses that are related to coverage of dependent children to claim the health insurance component of the EITC.

The proposal would repeal the supplemental young child credit.

Effective Date

The provision would be effective for taxable years beginning after December 31, 1991.

3. Extension of Targeted Jobs Tax Credit

Present Law

Tax credit

The targeted jobs tax credit is available on an elective basis for hiring individuals from several targeted groups. The targeted groups consist of individuals who are either recipients of payments under means-tested transfer programs, economically disadvantaged, or disabled.

The credit generally is equal to 40 percent of up to $6,000 of qualified first-year wages paid to a member of a targeted group. Thus, the maximum credit generally is $2,400 per individual. With respect to economically disadvantaged summer youth employees, however, the credit is equal to 40 percent of up to $3,000 of wages, for a maximum credit of $1,200.

The credit is scheduled to expire for wages paid to individuals who begin work for an employer after June 30, 1992.

Authorization of appropriations

Present law authorizes appropriations for administration and publicity expenses relating to the credit through June 30, 1992. These monies are to be used by the Internal Revenue Service and the Department of Labor to inform employers of the credit program.

Description of Proposal

The proposal would extend the targeted jobs tax credit and the authorization for appropriations for 18 months, through December 31, 1993.

Effective Date

The proposal would be effective on the date of enactment.

B. Provisions for Long-Term Economic Growth

1. Individual Retirement Arrangements (IRAs)

Present Law

Under present law, certain individuals are allowed to deduct contributions (up to the lesser of $2,000 or 100 percent of the individual's compensation or earned income) to an individual retirement arrangement (IRA). The amounts held in an IRA, including earnings on contributions, generally are not included in taxable income until withdrawn.

The $2,000 deduction limit is phased out over certain adjusted gross income (AGI) levels ($25,000 for individuals, $40,000 for joint filers) if the individual or the individual's spouse is an active participant in an employer-sponsored retirement plan. An individual may make nondeductible IRA contributions (up to the $2,000 or 100 percent of compensation limit) to the extent the individual is not permitted to make deductible IRA contributions.

Description of Proposal

The provision would restore the deductibility of IRA contributions for all taxpayers under the rules in effect prior to the Tax Reform Act of 1986 and would provide for the indexing of the limits on contributions to IRAs, in increments of $500.

In addition, the provision would permit nondeductible contributions to new special IRAs. Withdrawals from a special IRA would not be includible in income if attributable to contributions that had been held by the special IRA for at least 5 years. The limits on contributions to deductible IRAs and special IRAs would be coordinated. Furthermore, the limit on contributions to deductible IRAs and special IRAs would be coordinated with the limit on elective deferrals to certain tax-deferred plans (e.g., sec. 401(k) plans). Thus, for example, in no case could the sum of contributions to an IRA, contributions to a special IRA, and elective contributions to a 401(k) plan exceed the limit on elective deferrals ($8,728 in 1992).

The provision would permit transfers from deductible IRAs to special IRAs without imposition of the 10-percent tax on early withdrawals. The amount transferred to a special IRA generally would be includible in income in the year withdrawn. However, in the case of a transfer before January 1, 1994, the transferred amount would be includible in income ratably over a 4-taxable year period.

The provision would allow withdrawals from an IRA and from amounts attributable to elective deferrals under (1) a section 401(k) plan, (2) a tax-sheltered annuity (sec. 403(b) annuity, or (3) a section 501(c)(18) plan without imposition of the 10-percent additional income tax on early withdrawals to the extent the amount withdrawn is used to pay qualified acquisition, construction, or reconstruction costs with respect to a principal residence of a first-time homebuyer who is the taxpayer, the taxpayer's spouse, or the taxpayer's child or grandchild. A first-time homebuyer would be defined as any individual (and if married, such individual's spouse) who had no present interest in a principal residence during the 2-year period prior to the purchase of a home.

The waiver of the 10-percent additional tax on early withdrawals would also apply to the extent distribution did not exceed qualified higher education expenses. Qualified higher educational expenses means tuition, fees, books, supplies, and equipment required for the enrollment of or attendance of the taxpayer, the taxpayer's spouse, or the taxpayer's child or grandchild at a college, university, or post-secondary vocational school. The amount of qualified higher educational expenses for any taxable year would be reduced by any amount excludable from gross income under the provision in the Code pertaining to U.S. education savings bonds.

The provision would extend to IRAs the present-law exception to the 10-percent additional income tax for distributions from qualified retirement plans used to pay deductible medical expenses. For purposes of the medical expense exception (with regard to both IRAs and qualified retirement plans), a child, grandchild, or ancestor of the taxpayer would be treated as a dependent of the taxpayer in determining whether medical expenses are deductible.

Finally, the provision would provide that the present-law rule permitting penalty-free IRA withdrawals after an individual reaches 59-1/2 would not apply in the case of amounts attributable to contributions made during the previous 5 years. Thus, IRA contributions generally would have to remain in the account for at least 5 years to avoid withdrawal penalties. This restriction would only apply to contributions (and earning allocated thereto) that are made after December 31, 1991. Moreover, for purposes of applying the rule, distributions would be treated as having been made first from the earliest contribution (and earnings) remaining in the account, and then from other contributions in the order in which made.

Effective Date

The provision generally would apply to taxable years beginning after December 31, 1992. However, the rule permitting penalty-free withdrawals in certain cases would be effective for taxable years beginning after December 31, 1991. In addition, the rule permitting transfers from deductible IRAs to special IRAs would be effective for taxable years beginning after December 31, 1991. Thus, special IRAs could be established and maintained in taxable years beginning before January 1, 1993, only with funds transferred from a deductible IRA.

2. Income-Dependent Education Assistance: Self-Reliance Loans

Present Law

The Department of Education subsidizes student loans under the Guaranteed Student Loan (GSL) and Parent Loans to Undergraduate Students (PLUS) programs. These loan programs generally are available for certain postsecondary educational expenses, regardless of a student's financial need. The subsidies provided under the GSL and PLUS programs generally take three forms. First, the Department of Education guarantees repayment of qualified student loans made by banks. Second, the Department pays special allowance payments as an interest subsidy on qualifying student loans so that student borrowers are required to pay less interest on the loans. Third, with so-called "Stafford" loans, the Department pays an additional interest subsidy on qualified loans while the student is attending school.[1]

In addition, through the National Direct Student Loan (NDSL) program, the Federal government has made available revolving, direct-loan funds at certain participating educational institutions.[2] Such loans (commonly referred to as "Perkins loans") are available only to low-income students with significant demonstrated financial need. The schools participating in the NDSL program are responsible for collecting amounts due from student borrowers.

Federal agencies are authorized to notify the IRS that a person owes a past-due, legally enforceable debt (such as a delinquent student loan) to that agency. The IRS then is required to reduce the amount of any Federal tax refund due such person by the amount of the debt and pay that amount to the agency. The refund offset program applies with respect to debts of individuals and corporations (sec. 6402(d)).

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1 In the case of Supplemental Loans for Students ("SLS" loans) there is no in-school interest subsidy provided by the Federal government. SLS loans are available only to independent students.

Stafford loans generally are limited to $3,500 for freshmen and sophomores, $5,500 for juniors and seniors, with a total undergraduate cap of $23,000. SLS loans generally are limited to $4,000 for freshmen and sophomores, $5,000 for juniors and seniors, with a total undergraduate cap of $23,000.

2 Currently, a total lending pool of about $850 million is available at over 3300 participating schools.

Description of Proposal

In general

The proposal would create a program ("Income-Dependent Education Assistance") of direct loans ("Self-Reliance Loans") for higher education expenses. The Secretary of Education would make payments to participating institutions on the basis of estimated borrowing needs of the students at such institution. Eligible students who borrow funds under the program would have an account established with the Secretary of Education to record interest on and repayment of the Self-Reliance Loans. Such borrowers would make income-dependent repayments through the income tax system by means of a specially computed addition to tax that represents both principal and interest on the loan.

Eligible students

Eligible students would be United States citizens at least 17 years old, but not yet 51 years old, who are enrolled at a participating institution (which, for fiscal years 1994-1997, are selected by the Secretary of Education). Eligible students would be able to receive Self-Reliance Loans without regard to financial need. Notwithstanding any other provision of law, an eligible student would not receive a Self-Reliance Loan in any fiscal year unless such student's eligibility for assistance under section 428 and subpart 1 of part A of the Higher Education Act had been assessed.

Limits on amounts borrowed

In general

The maximum amount of Self-Reliance Loans that could be borrowed by a student in his or her lifetime would be $30,000, with no more than $25,000 of that amount for undergraduate education. A student could receive a Self-Reliance Loan in the amount of no more than $5,000 per fiscal year in the case of an undergraduate student and no more than $15,000 per fiscal year in the case of a graduate student.

Coordination with other Federal loan programs

The combined maximum amount of loans a student could borrow under the Income-Dependent Education Assistance program, Part B (Stafford and Perkins loans), and Part E (Supplemental Loans for Students) of the Higher Education Act of 1965 could not exceed $52,000 for a dependent undergraduate, $62,000 for an independent undergraduate[3] who borrows at least $10,000 in Self-Reliance Loans, and $115,000 for a graduate student.

Limit by cost of attendance

In any fiscal year, a student could not receive Self-Reliance Loans in an amount greater than such student's qualified education expenses (tuition, fees, books, supplies, and reasonable living expenses away from home) to attend a postsecondary school (as defined in section 481(a) of the Higher Education Act of 1965) less any other Federal educational financial assistance received by such student.

Interest rate on loans

The interest rate on a Self-Reliance Loan would be established at the time of issuance and would be equal to the average of the interest rates on the 10-year and 30-year Treasury bonds. The Secretary of Education would establish the interest rate on Self-Reliance Loans at the same time (and with the same frequency) as is done for the Supplemental Loans for Students program.

Repayment procedure

In general

Repayment on an individual's Self-Reliance Loan obligations would be collected through the individual income tax. For a taxpayer in repayment status, the taxpayer's income tax liability generally would be increased by the applicable Self-Reliance Loan repayment rate multiplied by the taxpayer's adjusted gross income (AGI).[4] This repayment would be treated as a tax imposed by section 1 of the Code except for purposes of determining the amount of any tax credit or the amount of minimum tax.

The applicable repayment rate would be fixed at the time the taxpayer first enters repayment status and would depend upon the taxpayer's amount of outstanding Self-Reliance Loan

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3 As determined in section 428A of the Higher Education Act of 1965.

4 In the case of a married individual whose spouse has not received a Self-Reliance Loan and who files a joint return, the income tax liability on the joint return would be increased by the individual's repayment rate multiplied by the AGI on the joint return. In the case of a married individual whose spouse has not received a Self-Reliance Loan and who files a separate return, such individual's income tax liability would increased by the individual's repayment rate multiplied by the sum of the AGI of that individual and the AGI of the individual's spouse (from the spouse's separate return).

indebtedness. Students with "high" indebtedness (as determined by the Secretary of Education) would have a repayment rate of 7 percent. Students with "moderate" indebtedness would choose between a repayment rate of 5 percent or 7 percent. Students with "low" indebtedness would choose among a repayment rate of 3 percent, 5 percent, or 7 percent. The Secretary of Education would make the determination of "low" and "moderate" indebtedness ranges so that the average borrower in each indebtedness status would be projected to repay the Self-Reliance Loan over a similar number of years as the average borrower with "high" indebtedness status.

A borrower would be in repayment status through the taxable year during which the loan obligation is repaid or, if earlier, 25 taxable years after the borrower was last enrolled in an institution of higher education on at least a half-time basis.

A borrower would be able to prepay all or part of a Self-Reliance Loan without penalty.

Repayment tax payments received on or before the due date (without regard to any extension) for filing of the income tax return for a given taxable year would be credited to the taxpayer's Self-Reliance Loan account as if received on the last day of the previous taxable year. Repayment tax payments received after the due date (without regard to any extension) for filing of the income tax return for a given taxable year would be credited to the taxpayer's Self-Reliance Loan account as if received on the last day of the following taxable year.

Exceptions for at least half-time students

A borrower would not be in repayment status for any taxable year during which either (1) the borrower was enrolled as at least a half-time student in an institution of higher education for 7 months of such taxable year or (2) the borrower was enrolled as at least a half-time student in an institution of higher education for final 3 months of such taxable year and such taxable year was the first in which the borrower was such a student (e.g., the borrower was a freshman).

A borrower would be able to defer payment of interest on a Self-Reliance Loan while he or she attends an institution of higher education on at least a half-time basis.

Exception for borrowers not required to file a tax return

No repayment of a Self-Reliance Loan would be required in any year in which the borrower is not required to file an income tax return.

Discharge of liability of the borrower

In general.--The Secretary of Education would discharge the liability to repay a Self-Reliance Loan in the event of the death or total permanent disability of a borrower. If a loan were discharged because of death or disability of the borrower or because of expiration of the 25-year repayment status period, the borrower (or his or her estate) would not be considered to have discharge of indebtedness income (under Code section 108(f)).

Bankruptcy.--A Self-Reliance Loan would not be dischargeable in bankruptcy. The Secretary of Treasury, however, could postpone payment on past-due amounts owed by bankrupt individuals.

Delinquent taxpayers

Borrowers who are delinquent in repaying their Self-Reliance Loan and who subsequently make interest payments to the Secretary of the Treasury on their underpayment would be entitled to have interest that is properly allocable to such loans credited by the Secretary of Education to their Self-Reliance Loan repayment.

Administration of the loan program

The Secretary of the Treasury would enter into an agreement with the Secretary of Education to process information on repayments and credit such repayments to the Department of Education.

The Secretary of the Treasury would make appropriate provisions to require borrowers to make Self-Reliance Loan repayments through payroll withholding and estimated tax payments to the extent practicable and would determine the liability of borrowers for incorrect withholding according to rules on estimated tax payments.

The Secretary of Education would develop a central data system to administer the Income-Dependent Education Assistance program. Such data system would provide borrowers with information on their Self-Reliance Loan balance and on prepayment options. Not later than January 1 of each year, the Secretary of Education would certify to the Secretary of the Treasury (1) a list of borrowers in repayment status for that year, (2) the sum of each such borrower's total principal amount of such loans plus any accrued interest minus the sum of any amounts collected from such borrower, and (3) the percentage of income each borrower has agreed to repay. A copy of such certification with respect to a borrower would be sent to such borrower.

Demonstration program

In general

The Secretary of Education would select institutions of higher education for participation in the Self-Reliance Loan program from those institutions submitting applications that are eligible to participate in part B loan programs. Not later than May 1, 1993, the Secretary would select not more than 500 institutions to participate in the program. The participating institutions would be chosen so as to represent a cross-section by educational sector, length of academic program, default experience, annual loan volume, highest degree offered, enrollment size, and geographic location. The Secretary would also select participating institutions in such a manner that the projected volume of student borrowing under the demonstration program would not exceed the following amounts:

$450,000,000 in fiscal year 1994
$550,000,000 in fiscal year 1995
$650,000,000 in fiscal year 1996
$900,000,000 in fiscal year 1997.

Each institution wishing to offer an Income-Dependent Education Assistance program would be required to submit an application to the Secretary of Education and, if accepted, enter into an agreement with the Secretary of Education for receipt of funds. Each participating school would agree to follow procedures specified by the Secretary of Education in consultation with the Secretary of the Treasury in disbursing such loans; to accept liability stemming from mismanagement of loans or false origination of loans; to provide the Secretary of Education at least once a month with a list of Self-Reliance Loan participants and any change in their enrollment status; and to counsel borrowers on their repayment options and their obligations.

The Secretary of Education would have the same authority to limit, suspend, or terminate an institution's participation in the Income-Dependent Education Assistance program as applies to an institution's participation in loan programs under Part B of the Higher Education Act of 1965, and could also impose additional regulations or criteria for participation. The demonstration program would conclude at the end of fiscal year 1997.

Administrative costs

There would be available to the Secretaries of Education and the Treasury for administrative costs amounts not to exceed the following:

Fiscal year	Treasury	Education
1992	$ 0	$ 0
1993	$1,000,000	$40,000,000
1994	$7,500,000	$20,000,000
1995	$4,500,000	$20,000,000
1996	$3,600,000	$20,000,000
1997	$4,000,000	$20,000,000

Evaluation and reporting

Beginning one year after enactment, the Secretary of Education, in consultation with the Secretary of the Treasury, would make annual reports to Congress describing and evaluating the implementation and administration of the Income-Dependent Education Assistance program and identifying problems that require legislative action.

Not later than January 1, 1997, the Secretary of Education, in consultation with the Secretary of the Treasury, would make a report to the Senate Committee on Labor and Human Resources and the House Committee on Education and Labor analyzing the administrative capacity of the Department of Education and any other Federal agency to operate this program; the administrative burden and costs imposed on the Department of Education and any other Federal agency by this program; the accuracy of information provided by the Secretary of Education; the administrative and financial factors that would affect the ability of all schools to participate in the program; the impact of this program on repayments, delinquencies and defaults under all federal student loan programs; and any other relevant information. The report would also publish the tuition and cost of attendance at each institution participating in the program and analyze changes in those costs compared to changes occurring at institutions not participating in the program. The report would examine the feasability of integrating the Income-Dependent Education Assistance program with a national service program. The report would also make recommendations for legislative actions necessary to implement the Income-Dependent Education Assistance program at all eligible institutions of higher education.

Effective Date

The proposal would be effective upon date of enactment. Amendments made to the Internal Revenue Code would be effective for taxable years beginning after December 31,

1992. The first Self-Reliance Loans would be issued on or after September 1, 1993.

3. Choice of Credit or Deduction for Interest on Student Loans

Present Law

The Tax Reform Act of 1986 repealed the deduction for personal interest. Student loan interest is generally treated as personal interest and thus is not allowable as an itemized deduction from income. There is no tax credit allowed for student loan interest paid by a taxpayer.

Description of Proposal

In general

The provision would allow individuals who have paid interest on qualified education loans to choose either a deduction for such interest or a nonrefundable credit against regular tax liability generally equal to 15 percent of such interest, subject to a maximum credit of $300. In order to qualify for either the deduction or the credit in a given taxable year, the interest must be paid during that taxable year and during the first 48 months (need not be consecutive) that payment on the loan is due. Unused amounts of credit could not be carried forward or backward to other taxable years.

A qualified education loan generally is any indebtedness incurred to pay for qualified higher education expenses of the taxpayer or the taxpayer's spouse or dependents with respect to higher education institutions and certain area vocational education schools (i.e., eligible educational institutions defined in Code section 135(c)(3)) and institutions conducting internship or residency programs leading to a degree or certificate from an institution of higher education, a hospital, or a health care facility conducting postgraduate training.

The qualified higher education expenses must be paid or incurred within a reasonable period of time before or after the indebtedness is incurred and must be attributable to education furnished during a period of time that the individual benefiting from the loan proceeds was at least a half-time student. Indebtedness that is used to refinance any indebtedness described in the previous sentence is also treated as a qualified education loan.

Qualified higher education expenses include tuition, fees, books, supplies, and reasonable living expenses while the student lives away from home. At the time the expenses are incurred, the student must be the taxpayer or the taxpayer's spouse or dependent (as defined under Code section 152). Qualified higher education expenses taken into account for the purpose of this credit are reduced by the amount excluded from gross income under Code section 135 (relating to the redemption of United States savings bonds to pay for higher education expenses) and by the amount of the reduction described in Code section 135(d)(1) (relating to certain scholarships and veterans benefits).

Limitation on claiming deduction

A taxpayer may not claim a deduction for interest on a qualified education loan if the taxpayer claims a deduction for qualified residence interest that is allocable to indebtedness used to pay for qualified higher education expenses of the taxpayer or the taxpayer's spouse or dependent.

Limitations on claiming credit

In general

No credit is allowed to an individual if that individual is claimed as a dependent on another taxpayer's return for the taxable year beginning in the calendar year in which such individual's taxable year begins.

No credit is allowed for interest on any amount of education loan indebtedness for which a deduction is claimed under any other provision.

If the taxpayer is under 23 years old (or, in the case of a joint return, if both spouses are under 23) at the end of the calendar year ending with or within the taxable year, the amount of the credit is not to exceed the taxpayer's regular tax liability multiplied by the ratio of the taxpayer's earned income (defined in Code section 911(d)(2)) to the taxpayer's adjusted gross income.

Credit claimed for interest on borrowing for expenses of taxpayer's dependent

In the case of qualified education loans used to pay the qualified higher education expenses of an individual other than the taxpayer or the taxpayer's spouse, no credit is allowed unless the individual is claimed as a dependent of the taxpayer for that taxable year and the individual is at least a half-time student during that taxable year.

Effective Date

The provision would be effective for taxable years beginning after December 31, 1991 and only for loans whose first payments are due after that date.

4. Formation of, and Contributions to, Tax-Exempt Youth Training Organizations

Present Law

In order to qualify as a tax-exempt organization under section 501(c)(3) and be eligible to receive tax-deductible contributions, an organization must be organized and operated exclusively for charitable, educational, or other exempt purposes specified in section 501(c)(3), and no part of the organization's net earnings may inure to the benefit of any private shareholder or individual. Section 501(c) also provides tax-exempt status for other types of organizations (e.g., social welfare organizations and business associations), provided certain requirements are satisfied.

Charitable contributions to organizations described in section 501(c)(3) are allowed as an itemized deduction, subject to certain percentage limitations (sec. 170). In addition, donations to States or political subdivisions are deductible as charitable contributions, provided that the donation is made for exclusively public purposes. Depending on the type of property contributed and the type of the donee organization, the amount of a taxpayer's charitable contribution deduction generally is allowed in an amount up to the contributed property's fair market value. However, special rules provide for an augmented charitable contribution deduction for certain contributions made by corporations of inventory property used for the care of the ill, the needy, or infants, and certain scientific research property donated to educational or scientific organizations (sec. 170(e)(3) and (4)). The deduction allowed for such donations is equal to the corporation's basis in the property plus one-half of the amount of ordinary income that would have been realized if the property had been sold (but in no event may the deduction exceed twice the basis in the contributed property).

Payments made by a taxpayer to a tax-exempt organization are deductible as ordinary and necessary business expenses under section 162, provided that the taxpayer has a reasonable expectation of financial return to his trade or business commensurate with the amount of the transfer. In such a case, a "gift or contribution" has not been made for purposes of section 170.[1]

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[1] See Treas. Reg. sec. 1.170A-1(c)(5); Rev. Rul. 84-110, 1984-2 C.B. 35.

Description of Proposal

Tax-exempt status

The proposal would specifically provide tax-exempt status for certain youth training organizations that are organized and operated solely for the purpose of administering a training program that (1) combines supervised on-the-job training for full-time high school students with theoretical academic instruction, (2) requires student participants be provided broad-based competencies and transferable skills suitable for career progression within the industry or trade in which the student is employed, (3) requires student trainees to be treated as employees for purposes of section 6 of the Fair Labor Standards Amendments of 1989, or section 6 or 14 of the Fair Labor Standards Act of 1938, and (4) prohibits the use of contributions to the organization for actual employment training expenses or compensation of student trainees.

The youth training organization would be required to be controlled by representatives of businesses contributing to the organization, schools participating in the training program, State or local governments, and student trainees.

Augmented deduction

The proposal also would provide an augmented deduction for cash contributions made to a tax-exempt youth training organization. The allowable deduction would be 150 percent of the contributed amount.

Department Studies

The Treasury, Labor, and Education Departments would be directed to report to Congress within three years after enactment on the effects of the proposal and any recommendations for legislative modifications.

Effective Date

The proposal would be effective for taxable years beginning after the date of enactment.

5. Extension of Exclusion for Employer-Provided Educational Assistance

Present Law

An employee's gross income and wages for income and employment tax purposes do not include amounts paid or incurred by the employer for education assistance provided to the employee if such amounts are paid or incurred pursuant to an educational assistance program that meets certain requirements. This exclusion, which expires with respect to amounts paid after June 30, 1992, is limited to $5,250 of educational assistance with respect to an individual during a calendar year.

In the absence of this exclusion, an employee generally would be required to include in income and wages, for income and employment tax purposes, the value of educational assistance provided by an employer to the employee, unless the cost of such assistance qualified as a deductible job-related expense of the employee.

Description of Proposal

The exclusion for employer-provided educational assistance would be extended for 18 months, through December 31, 1993.

Effective Date

The proposal would be effective for taxable years ending after June 30, 1992.

6. Expansion of Educational Savings Bond Provisions

Present Law

Code section 135 provides that interest income earned on a qualified U.S. Series EE savings bond issued after December 31, 1989, is excludible from gross income if the proceeds of the bond upon redemption do not exceed qualified higher education expenses paid by the taxpayer during the taxable year.[1] "Qualified higher education expenses" include tuition and required fees for the enrollment or attendance of the taxpayer, the taxpayer's spouse, or a dependent of the taxpayer at an eligible educational institution. A taxpayer cannot qualify for the interest exclusion by paying for the education expenses of another person (such as a grandchild or other relative) who is not a dependent of the taxpayer.

The exclusion provided by section 135 is phased out for certain higher-income taxpayers. A taxpayer's AGI for the year the bond is redeemed (not the year the bond was issued) determines whether or not the phaseout applies. For taxpayers filing a joint return, the phaseout range is for AGI between $60,000 and $90,000 (adjusted for inflation). For single taxpayers and heads of households, the phaseout range is for AGI between $40,000 and $55,000 (adjusted for inflation).

To prevent taxpayers from effectively avoiding the income phaseout limitation (through the issuance of bonds directly in the child's name), section 135(c)(1)(B) provides that the interest exclusion is available only with respect to U.S. Series EE savings bonds issued to taxpayers who are at least 24 years old.

The interest rate on Series EE savings bonds varies, depending on how long the bonds are held. The interest rate on such bonds held for more than five years is based on the market rate for Treasury outstanding obligations with five years to maturity. Bonds held for less than five years earn interest on a fixed, graduated scale (generally below current rates on comparable Treasury instruments). Interest earned on Series EE bonds is paid when the bonds are redeemed.

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[1] If the aggregate redemption amount (i.e., principal plus interest) of all Series EE bonds redeemed by a taxpayer during the taxable year exceeds the qualified education expenses incurred, then the excludable portion of interest income is based on the ratio that the education expenses bears to the aggregate redemption amount.

Description of Proposal

The proposal would expand the definition of "qualified higher education expenses" under section 135 to include tuition and required fees paid by a taxpayer for the enrollment or attendance of any individual at an eligible educational institution (not simply dependents).

The proposal also would repeal the present-law AGI phaseout limitation under section 135 (and the related rule requiring that bonds be issued to a person who is at least 24 years old). Thus, interest earned on a Series EE savings bond would not be subject to tax regardless of the taxpayer's AGI during the year the bond is redeemed if, during that year, the taxpayer pays for qualified education expenses of any individual and the education expenses exceed the proceeds (principal plus interest) received upon redemption.

Effective Date

The proposal would apply to U.S. Series EE savings bonds issued after December 31, 1989, and redeemed after December 31, 1991.

7. **Expansion of 45-Day Interest-Free Period**

Present Law

No interest is paid by the Government on a refund arising from an income tax return if the refund is issued by the 45th day after the later of the due date for the return (determined without regard to any extensions) or the date the return is filed (Code sec. 6611(e)).

There is no parallel rule for refunds of taxes other than income taxes (i.e., employment, excise, and estate and gift taxes), for refunds of any type of tax arising from amended returns, or for claims for refunds of any type of tax.

If a taxpayer files a timely original return with respect to any type of tax and later files an amended return claiming a refund, and if the IRS determines that the taxpayer is due a refund on the basis of the amended return, the IRS will pay the refund with interest computed from the due date of the original return.

Description of Proposal

The provision provides that no interest is to be paid by the Government on a refund arising from any type of original tax return if the refund is issued by the 45th day after the later of the due date for the return (determined without regard to any extensions) or the date the return is filed.

A parallel rule applies to amended returns and claims for refunds: if the refund is issued by the 45th day after the date the amended return or claim for refund is filed, no interest is to be paid by the Government for that 45-day period (interest would continue to be paid for the period from the due date of the return to the date the amended return or claim for refund is filed). If the IRS does not issue the refund by the 45th day after the date the amended return or claim for refund is filed, interest would be paid (as under present law) for the period from the due date of the original return to the date the IRS pays the refund.

A parallel rule also applies to IRS-initiated adjustments (whether due to computational adjustments or audit adjustments). With respect to these adjustments, the IRS is to pay interest for 45 fewer days than it otherwise would.

Effective Date

The extension of the 45-day processing rule is effective for returns required to be filed (without regard to extensions) on or after July 1, 1992.

The amended return rule is effective for amended returns and claims for refunds filed on or after July 1, 1992 (regardless of the taxable period to which they relate).

The rule relating to IRS-initiated adjustments is applicable to refunds paid on or after July 1, 1992 (regardless of the taxable period to which they relate).

8. Extend Health Insurance Deduction for Self-Employed Individuals

Present Law

Under present law, the tax treatment of health insurance expenses depends on whether the taxpayer is an employee and whether the taxpayer is covered under a health plan paid for by the taxpayer's employer. An employer's contribution to a plan providing accident or health coverage for the employee and the employee's spouse and dependents is excludable from an employee's income and wages for income and employment tax purposes. In addition, businesses can generally deduct, as an employee compensation expense, the full cost of any health insurance coverage provided for their employees. The exclusion and deduction are generally available in the case of owners of the business who are also employees.

In the case of self-employed individuals (i.e., sole proprietors or partners in a partnership) no equivalent exclusion applies. However, present law provides a deduction for 25 percent of the amount paid for health insurance for a self-employed individual and the individual's spouse and dependents. The 25-percent deduction is also available to more than 2-percent shareholders of S corporations. The amount of expenses in excess of the deductible amount can be taken into account in determining whether the individual is entitled to deduct medical expenses as an itemized deduction (sec. 213). Thus, such amounts are deductible to the extent that, when combined with other unreimbursed medical expenses, they exceed 7.5 percent of adjusted gross income.

The 25-percent deduction expires for taxable years beginning after June 30, 1992. In the case of years beginning in 1992, only amounts paid before July 1, 1992, for coverage before July 1, 1992, are taken into account in determining the amount of the deduction.

Description of Proposal

The proposal would extend and increase the 25-percent deduction for health insurance expenses of self-employed individuals. For 1992, the deduction would be 25 percent of health insurance expenses. For 1993 and 1994, the deduction would be 100 percent of health insurance expenses. The deduction would expire after December 31, 1994.

Effective Date

The proposal would be effective for taxable years ending after June 30, 1992.

9. Increase Base Tax Rate on Ozone-Depleting Chemicals and Expand List of Taxed Chemicals

Present Law

A excise tax is imposed on certain ozone-depleting chemicals. The amount of tax generally is determined by multiplying the base tax rate applicable for the calendar year by an ozone-depleting factor assigned to the chemical. Certain chemicals are subject to a reduced rate of tax for years prior to 1994.

Between 1992 and 1995 there are two base tax rates applicable, depending upon whether the chemicals were initially listed in the Omnibus Reconciliation Act of 1989 or whether they were newly listed in the Omnibus Reconciliation Act of 1990. The base tax rate applicable to initially listed chemicals is $1.67 per pound for 1992, $2.65 per pound for 1993 and 1994, and an additional 45 cents per pound per year for each year thereafter. The base tax rate applicable to newly listed chemicals is $1.37 per pound for 1992, $1.67 per pound for 1993, $3.00 per pound for 1994, $3.10 per pound for 1995, and an additional 45 cents per pound per year for each year thereafter.

The initially listed chemicals are CFC-11, CFC-12, CFC-113, CFC-114, CFC-115, Halon-1211, Halon-1301, Halon-2402. The newly listed chemicals are carbon tetrachloride, methyl chloroform, CFC-13, CFC-111, CFC-112, CFC-211, CFC-212, CFC-213, CFC-214, CFC-215, CFC-216, CFC-217.

Description of Proposal

The proposal would increase and apply the same base tax rate to both initially listed chemicals and newly listed chemicals. The new base tax rate would be $1.85 per pound for 1992, $2.75 per pound in 1993, $3.65 per pound in 1994, and $4.55 per pound in 1995. For years after 1995, the base tax amount would be increased by 45 cents per pound per year. Present law rates would be retained for chemicals used in rigid foam insulation.

Effective Date

The proposal would be effective for taxable chemicals sold or used on or after July 1, 1992. Appropriate floor stocks taxes would be imposed on taxed chemicals held on the effective dates of changes in the base tax rate.

10. Extension of Tax Credit for Orphan Drug Clinical Testing Expenses

Present Law

A 50-percent nonrefundable tax credit is allowed for a taxpayer's qualified clinical testing expenses paid or incurred in the testing of certain drugs for rare diseases, generally referred to as "orphan drugs." Qualified testing expenses are costs incurred to test an orphan drug after the drug has been approved for human testing by the Food and Drug Administration (FDA) but before the drug has been approved for sale by the FDA. Present law defines a rare disease or condition as one that (1) affects less than 200,000 persons in the United States or (2) affects more than 200,000 persons, but there is no reasonable expectation that businesses could recoup the costs of developing a drug for it from U.S. sales of the drug. These rare diseases and conditions include Huntington's disease, myoclonus, ALS (Lou Gehrig's disease), Tourette's syndrome, and Duchenne's dystrophy (a form of muscular dystrophy).

The orphan drug tax credit is scheduled to expire after June 30, 1992.

Description of Proposal

The proposal would extend the orphan drug tax credit for 18 months (i.e., for qualified clinical testing expenses incurred through December 31, 1993).

Effective Date

The proposal would be effective for expenses incurred during the period July 1, 1992, through December 31, 1993.

11. UBIT Changes Relating to Real Estate Investments by Pension Funds and Others

a. Relax debt-finance restrictions

Present Law

A qualified pension trust or an organization that is otherwise exempt from Federal income tax generally is taxed on any income from a trade or business that is unrelated to the organization's exempt purposes (the Unrelated Business Income Tax or "UBIT") (sec. 511). Certain types of income, including rents, royalties, dividends, and interest, are excluded from the UBIT, except when such income is derived from "debt-financed property." Income from debt-financed property generally is subject to the UBIT in proportion to the amount of debt financing (sec. 514(a)).

An exception to the rule requiring taxation of income from debt-financed property is available to pension trusts, educational institutions, and certain other exempt organizations (collectively referred to as "qualified organizations") that make debt-financed investments in real property (sec. 514(c)(9)(A)). Under this exception, income from investments in real property is not treated as income from debt-financed property. Mortgages are not considered real property for purposes of the exception.

The debt-financed exception, however, is available for investments in debt-financed property only if the following six restrictions of section 514(c)(9)(B) are satisfied: (1) the price of the real property is a fixed amount determined as of the date of the acquisition (the "fixed price" restriction); (2) the amount of the indebtedness or any amount payable with respect to the indebtedness, or the time for making any payment of any such amount, is not dependent (in whole or in part) upon revenues, income, or profits derived from the property (the "participating loan" restriction); (3) the property is not leased by the qualified organization to the seller or to a person related to the seller (the "leaseback" restriction); (4) in the case of a pension trust, the seller or lessee of the property is not a disqualified person (the "disqualified person" restriction); (5) the seller or a person related to the seller (or a person related to the plan with respect to which a pension trust was formed) is not providing financing in connection with the acquisition of the property (the "seller-financing" restriction); and (6) if the investment in the property is held through a partnership, certain additional requirements are satisfied by the partnership (the "partnership" restrictions) (sec. 514(c)(9)(B)(i) through (vi)).

Description of Proposal

Relax the leaseback and disqualified person restrictions

The proposal would relax the leaseback and disqualified person restrictions to permit a de minimis leaseback of debt-financed real property to the seller (or a person related to the seller) or to a disqualified person. The de minimis exception would apply only where (1) no more than 20 percent of the leasable floor space in a building is leased back to the seller (or related party) or to the disqualified person, and (2) the lease is on commercially reasonable terms.

Relax the seller-financing restriction

The proposal would relax the seller-financing restriction to permit seller financing on terms that are commercially reasonable. Regulations would be authorized for the purpose of determining commercially reasonable financing terms. In addition, seller financing that is on terms that include a down payment of at least 15% of the sales price and an interest rate of at least 150% of the applicable Federal rate ("AFR") on any indebtedness would be deemed to be commercially reasonable.

The present-law "fixed price" and "participating loan" restrictions would not be affected by this modification. Thus, for example, income from a financing arrangement (including an equity kicker) based on revenue, income, or profits generally would continue to be treated as income from debt-financed property, unless some other exception applies.

Relax the fixed price and participating loan restriction for property foreclosed on by financial institutions

The proposal also would relax the fixed price and participating loan restrictions for certain sales of real property foreclosed upon by financial institutions.[1] The relaxation of these rules would be limited to cases where: (1) a qualified organization acquires the property from a financial institution that acquired the real property by foreclosure (or after an actual or imminent default); (2) the financial institution treats any income from the sale of the property as ordinary income; (3) the stated principal amount of the seller financing does not exceed the financial institution's outstanding indebtedness (including accrued but unpaid interest) with respect to the property at the time of foreclosure; and (4) the value of the participation feature

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[1] Financial institutions include institutions in conservatorship or receivership and certain affiliates of financial institutions.

at the time of sale does not exceed 25 percent of the value of the property.

Regulations would be authorized for the purpose of clarifying these limitations. In particular, these regulations would be expected to establish standards for determining when the value of a participation feature at the time of sale does not exceed 25 percent of the value of the property. For example, a participation feature that provides the seller with less than a 25 percent interest in net proceeds, net income, or gain on sale of the property would be expected to be valued at less than 25 percent of the value of the property.

Eliminate section 514(c)(9)(B) restrictions for investments through certain large partnerships

The proposal also would eliminate the six section 514(c)(9)(B) restrictions for qualified organizations that invest in real property through certain "large" partnerships.

A "large" partnership would be a partnership having at least 250 partners that satisfies the following three tests: (1) investment units in the partnership are registered with the Securities and Exchange Commission; (2) a significant percentage (at least 50 percent) of each class of interests is owned by taxable individuals; and (3) a principal purpose of the partnership allocations is not tax avoidance. Partnership interests that are subject to the same terms would be considered to be in the same class, regardless of whether the interests are subject to different ownership restrictions (a partnership can therefore monitor the 50 percent ownership restriction by requiring that designated interests be held only by taxable persons).

Treat certain mortgages as real property

The proposal would treat mortgages as real property for purposes of section 514(c)(9), under the following conditions: (1) the mortgages have been acquired from a financial institution that is in conservatorship or receivership, (2) the mortgages have been acquired with a cash down payment of at least 50% of the sales price (i.e., the acquisition indebtedness is less than 50% of the price of the mortgages), (3) the mortgages are not debt-financed property except on account of acquisition indebtedness that is granted by the seller, and (4) the mortgages are acquired prior to January 1, 1994. Mortgages would be eligible for treatment as real property for two-and-a-half years after they are acquired by the tax-exempt purchaser.

Effective Date

The proposal would be effective for debt-financed acquisitions of real estate and mortgages on or after February 1, 1992, and for partnership interests acquired on or after February 1, 1992.

b. Repeal UBIT rule for publicly-traded partnerships

Present Law

In general, the character of a partner's distributive share of income is the same as if the income had been directly realized by the partner. Thus, a tax-exempt organization's share of income from a partnership (other than from a publicly-traded partnership) is treated as unrelated business income, or not, depending on the underlying character of the income (sec. 512(c)(1)).

However, a tax-exempt organization's share of gross income from a publicly-traded partnership (that is not otherwise treated as a corporation) automatically is treated as gross income derived from an unrelated trade or business (sec. 512(c)(2)(A)). The organization's share of the partnership deductions is allowed in computing the organization's taxable unrelated business income (sec. 512(c)(2)(B)).

Description of Proposal

The proposal would repeal the rule that automatically treats income from publicly-traded partnerships as unrelated business income. Thus, under the proposal, investments in publicly-traded partnerships would be treated the same as investments in other partnerships for purposes of the UBIT rules.

Effective Date

The proposal would be effective for partnership interests acquired on or after February 1, 1992.

c. Permit title-holding companies to receive small amounts of income that is subject to UBIT

Present Law

Code section 501(c)(2) provides tax-exempt status to certain corporations organized for the exclusive purpose of holding title to property and turning over any income from the property to one or more related tax-exempt organizations. Section 501(c)(25) provides tax-exempt status to certain corporations and trusts that are organized for the exclusive purposes of acquiring and holding title to real property, collecting income from such property, and remitting the income therefrom to no more than 35 shareholders or beneficiaries that are: (1) qualified pension, profit-sharing, or stock bonus plans (sec. 401(a)); (2) governmental pension plans (sec. 414(d)); (3) the United States, a State or political subdivision, or governmental agencies or instrumentalities; or (4) tax-exempt charitable, educational, religious, or other organizations described in section 501(c)(3).

Ordinarily, a tax-exempt organization will not lose its exempt status because it generates unrelated business taxable income (UBTI), so long as the activities producing such taxable income are not substantial in comparison to the organization's activities that further its exempt purposes. However, the IRS has taken the position that a title-holding company described in section 501(c)(2) or 501(c)(25) will lose its tax-exempt status if it generates any amount of income subject to the UBIT.[2]

Description of Proposal

The proposal would permit a title-holding company that is exempt from tax under sections 501(c)(2) or 501(c)(25) to receive UBTI up to 10 percent of its gross income for the taxable year, provided that the UBTI is incidentally derived from the holding of real property. For example, income generated from parking or operating vending machines located on real property owned by a title-holding company generally would qualify for the 10-percent de minimis rule, while income derived from an activity that is not incidental to the holding of real property (e.g., manufacturing) would not qualify.[3]

In addition, the proposal would provide that a section 501(c)(2) or 501(c)(25) title-holding company will not lose its tax-exempt status if UBTI that is incidentally derived from the holding of real property exceeds the 10-percent limitation, provided that the title-holding company establishes to the satisfaction of the Secretary of the Treasury that the receipt of UBTI in excess of the 10-percent limitation was inadvertent and reasonable steps are being

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2 IRS Notice 88-121, 1988-2 C.B. 457. See also Treas. Reg. sec. 1.501(c)(2)-1(a).

3 In cases where unrelated income is incidentally derived from the holding of real property, receipt by a title-holding company of such income (up to the 10-percent limit) will not jeopardize the title-holding company's tax-exempt status, but nonetheless, will be subject to tax under the general UBIT rules.

taken to correct the circumstances giving rise to such excess UBTI.

Effective Date

The proposal would be effective for taxable years beginning after December 31, 1991.

d. Exclude from UBTI any gains from the disposition of property acquired from financial institutions in conservatorships or receiverships

Present Law

In general, gains or losses from the sale, exchange or other disposition of property are excluded from UBTI (sec. 512(b)(5)). However, gains or losses from the sale, exchange or other disposition of property held primarily for sale to customers in the ordinary course of the trade or business are not excluded from UBTI (the "dealer UBTI rule") (sec. 512(b)(5)(B)).

Description of Proposal

The proposal would create an exception to the dealer UBTI rule by excluding gains from the sale, exchange or other disposition of real property and mortgages acquired from financial institutions that are in conservatorship or receivership. The exclusion would be limited to properties designated as disposal property within six months of acquisition, and disposed of within two-and-a-half years of acquisition. The two-and-a-half year period may be extended by the Secretary if an extension is necessary for the orderly liquidation of the property. The exclusion would not be available for properties that are substantially improved or renovated after acquisition and before disposition. The exclusion generally would not be available for property that is developed except if the property is developed only in a limited manner (e.g., by securing zoning permits).

Effective Date

The proposal would be effective for property acquired after February 1, 1992.

e. Exclude loan commitment fees and certain option premiums from UBTI

Present Law

Income from a trade or business that is unrelated to an exempt organization's purpose generally is UBTI. Passive income such as dividends, interest, royalties, and gains or losses from the sale, exchange or other disposition of property generally is excluded from UBTI (sec. 512(b)). In addition, gains on the lapse or termination of options on securities are explicitly exempted from UBTI (sec. 512(b)(5).

Present law is unclear on whether loan commitment fees and premiums from unexercised options on real estate are UBTI.

Description of Proposal

The proposal would clarify that loan commitment fees and premiums from unexercised options on real estate are excluded from UBTI.

Effective Date

The proposal would be effective for premiums or loan commitment fees that are received after February 1, 1992.

f. Exclude certain hotel rental income from UBTI

Present Law

Rents from real property generally are excluded from UBTI unless the rents are measured by reference to the net income derived by any person from the leased property (sec. 512(b)(3)). Payments for the use or occupancy of rooms and other space where services are also rendered to the occupant, such as for the use or occupancy of rooms or other quarters in hotels, do not constitute rents from real property (Treas. Reg. sec. 1.512(b)-1(c)(5)).

Description of Proposal

The proposal would exclude from UBTI any hotel rental income when (i) the hotel has been acquired from a financial institution in receivership or conservatorship, (ii) the hotel has been designated as disposal property within six months of acquisition, and (iii) the hotel either is disposed within two-and-a-half years of acquisition or, after two-and-a-half years, any related services are rendered by an independent contractor pursuant to a contract that does not permit the exempt organization to share any of the net income of the independent contractor.

Effective Date

The proposal would be effective for hotels acquired after February 1, 1992.

12. Tax Credit for First-Time Homebuyers

Present Law

There is no tax credit for the purchase of a principal residence under present law.

Description of Proposal

Under the proposal, individuals who purchase a new principal residence would be eligible to receive a tax credit equal to 10 percent of the purchase price of the residence, up to a maximum credit of $5,000. The credit would apply to a new principal residence if the original use of the residence commences with the taxpayer and if the taxpayer (1) acquires such residence on or after February 1, 1992, and before January 1, 1994, or (2) enters into a binding contract to acquire the residence on or after February 1, 1992, and before January 1, 1994, and purchases the residence within 90 days of entering into that binding contract. Only one tax credit could be claimed per residence.

First-time homebuyers would be defined as individuals who did not have a present interest in a residence in the 3 years preceding the purchase of a home. If an individual is deferring tax on gain from the sale of a previous principal residence and is permitted an extended rollover period, he or she would not be considered a first-time homebuyer until after the end of the extended rollover period.

The first-time homebuyer credit would be nonrefundable, and thus would be available only to the extent the taxpayer had income tax liability to offset. However, any unused portion of the credit could be carried forward for up to 5 years and applied against future income tax liability.

The credit would be recaptured if the residence on which the credit was claimed was sold or otherwise disposed of within 3 years of the date the residence was purchased. The recapture rule would not apply, however, to dispositions by reason of the taxpayer's death or divorce. If the taxpayer sold the residence within 3 years but purchased a new home within the rollover period, the credit would be recaptured to the extent the taxpayer would have claimed a smaller credit on the new residence had it been purchased during the period when the credit was available.

Effective Date

The proposal would be effective for purchases on or after February 1, 1992.

13. Passive Loss Relief for Real Estate Developers

Present Law

The passive loss rules limit deductions and credits from passive trade or business activities. Deductions attributable to passive activities, to the extent they exceed income from passive activities, generally may not be deducted against other income, such as wages, portfolio income, or business income that is not derived from a passive activity. Deductions that are suspended under this rule are carried forward and treated as deductions from passive activities in the next year. The suspended losses from a passive activity are allowed in full when a taxpayer disposes of the entire interest in the passive activity to an unrelated person.

Passive activities are defined to include trade or business activities in which the taxpayer does not materially participate. Material participation requires a taxpayer to be involved in the operations of the activity on a regular, continuous, and substantial basis.

Rental activities are also included in the definition of passive activities (regardless of the level of the taxpayer's participation). In general, rental activities are treated as separate from other business activities. A special rule permits the deduction of up to $25,000 of losses from certain rental real estate activities (even though they are considered passive), if the taxpayer actively participates in them. This $25,000 amount is allowed for taxpayers with adjusted gross incomes of $100,000 or less, and is phased out for taxpayers with adjusted gross incomes between $100,000 and $150,000. In general, active participation is a lesser standard of involvement than material participation and generally requires that the taxpayer participate in making management decisions or arrange for others to provide services such as repairs in a significant and bona fide sense. The active participation standard requires an ownership interest of no less than 10 percent in the rental real estate. A taxpayer generally is deemed not to satisfy the active participation standard (or the material participation standard) with respect to property he holds through a limited partnership interest.

Description of Proposal

Under the proposal, a taxpayer who materially participates in a real estate development activity during the taxable year may treat the rental of certain real property ("Qualified Property") as a non-rental activity that is part of such taxpayer's real estate development activity. Income and loss for the taxable year from Qualified Property would not be treated as passive, but net losses from Qualified Property would be allowed only to the extent of net income from Qualified Property and 80 percent of the taxpayer's taxable income for the year that is attributable to real estate development activities other than the rental of Qualified Property. Losses from Qualified Property that exceed this amount for the year are carried forward and treated as losses from Qualified Property in the next year. Losses arising from Qualified Property in a prior year that were suspended and carried forward as passive activity losses would be subject to the same limitation as losses from Qualified Property. Credits from Qualified Property would be treated similarly.

In order to be Qualified Property, rental real property must meet the following criteria: (1) the taxpayer owns a non-de minimis interest in the rental real property; and (2) the taxpayer actively participates in the rental real property during the current taxable year.

A taxpayer's real estate development activity would be considered a single trade or business activity which includes all activities in which the taxpayer actively participates and which consist of (1) construction, substantial renovation, or management services provided with respect to real property, (2) sales or lease-up services provided with respect to real property in which the taxpayer has at least a non-de minimis ownership interest, and (3) the rental of Qualified Property. Material participation and active participation would generally have the same meaning as under present law; however, active participation would not require a 10-percent ownership interest.

The proposal would apply only to property placed in service before the date of Committee action. Property that is substantially improved after that date would be treated as placed in service after that date.

Effective Date

The proposal would be effective with respect to taxable years ending on or after December 31, 1992.

14. **Increase Recovery Period for Depreciation of Nonresidential Real Property**

Present Law

A taxpayer is allowed to recover, through annual depreciation allowances, the cost or other basis of nonresidential real property that is used in a trade or business or that is held for the production of rental income. For regular tax purposes, the amount of the depreciation deduction allowed with respect to nonresidential real property for any taxable year generally is determined using the straight-line method and a recovery period of 31.5 years. For alternative minimum tax purposes, the amount of the depreciation deduction allowed with respect to nonresidential real property for any taxable year is determined using the straight-line method and a recovery period of 40 years.

Description of Proposal

The depreciation deduction allowed with respect to nonresidential real property for any taxable year would be determined by using the straight-line method and a recovery period of 40 years for purposes of the regular tax and the alternative minimum tax.

Effective Date

The proposal generally would apply to property placed in service after February 12, 1992. The proposal would not apply to property that is placed in service by a taxpayer before January 1, 1995, if (1) the taxpayer or a qualified person entered into a binding written contract to purchase or construct the property before February 13, 1992, or (2) construction of the property was commenced by or for the taxpayer or a qualified person before February 13, 1992. For this purpose, a qualified person would be defined as any person who transfers his or her rights in such a contract or in the property to the taxpayer, but only if the property is not placed in service by such person before such rights are transferred to the taxpayer.

15. Extension of Low-Income Housing Tax Credit

Present Law

A tax credit is allowed in annual installments over 10 years for qualifying newly constructed or substantially rehabilitated low-income rental housing. For most qualifying housing, the credit has a present value of 70 percent of the cost of low-income housing units. For housing receiving other Federal subsidies (e.g., tax-exempt bond financing) and for the acquisition cost of existing housing that is substantially rehabilitated (e.g., costs other than rehabilitation expenditures), the credit has a present value of 30 percent of qualified costs. Generally, the portion of the building for which the credit is claimed must be rented to qualified low-income tenants at restricted rents for 15 years after the building is placed in service. In addition, a subsequent additional 15-year period of low-income use is required.

Each State receives an annual low-income housing credit volume limitation of $1.25 per resident. To qualify for the credit, a building owner generally must receive a credit allocation from the appropriate State credit authority. An exception is provided for property which is substantially financed with the proceeds of tax-exempt bonds subject to the State's private-activity bond volume limitation.

The low-income housing credit is scheduled to expire after June 30, 1992.

Description of Proposal

The low-income housing credit would be extended for 18 months, through December 31, 1993.

The proposal also would make several modifications to the credit:

(1) For purposes of the carryforward rules, credits carried forward from previous years would be treated as used before current year credits. Under present law, current year credits are deemed to be used before credits which have been carried forward.

(2) A waiver from the credit's ten-year anti-churning rule would be provided for certain projects substantially assisted, financed, or operated under sec 221(d)(4) of the National Housing Act. Absent such waiver these properties are not eligible for the credit if they were placed in service within the previous ten years.

(3) The eligible basis of each unit of a credit project would be limited to an amount equal to the maximum FHA single

family insurance amount (currently $124,875). This amount would be indexed for inflation.

(4) Clarification would be provided that a unit occupied entirely by full-time students may qualify for the credit if the full-time students are a parent and his or her minor children and the tenants are not dependents of a third party.

(5) The Treasury Department would be authorized to grant a waiver of penalties for de minimis errors in the application of the low-income tenant set-aside rules.

(6) The Treasury Department would be authorized to grant a waiver from the annual recertification of tenant income, for tenants in a building, if the population of a building is composed entirely of low-income tenants.

(7) The bill would provide that community service buildings in projects in qualified census tracts are included in eligible basis as functionally related and subordinate facilities if (a) the size of the facilities is commensurate with tenant needs, and (b) the use of the facilities is predominantly (although not exclusively) by tenants and employees of the project owner, and (c) no more than 20 percent of the credit project's eligible basis is attributable to the aggregate basis of such facilities.

Effective Date

The proposal would be effective on the date of enactment.

The modifications to the low-income housing tax credit program rules generally would be effective for allocations of low-income credit volume limitation (and bond-financed buildings financed with tax-exempt bonds issued after) June 30, 1992. The change to the credit carryforward rules would be effective on and after January 1, 1992.

16. Extension of Qualified Mortgage Bond and Mortgage Credit Certificate Programs

Present Law

Qualified mortgage bonds

Qualified mortgage bonds ("QMBs") are tax-exempt bonds the proceeds of which are used to finance the purchase, or qualifying rehabilitation or improvement, of single-family, owner-occupied residences located within the jurisdiction of the issuer of the bonds. Persons receiving QMB loans must satisfy principal residence, purchase price, borrower income, first-time homebuyer, and other requirements. Part or all of the interest subsidy provided by QMBs is recaptured if the borrower experiences substantial increases in income and either disposes of the residence acquired with the QMB loan or no longer uses the residence as his or her principal residence, within nine years after its purchase.

Mortgage credit certificates

Qualified governmental units may elect to exchange private activity bond volume authority for authority to issue mortgage credit certificates ("MCCs"). MCCs entitle home buyers to nonrefundable income tax credits for a specified percentage of the interest paid on mortgage loans on their principal residences. Once issued, an MCC remains in effect as long as the loan remains outstanding and the residence being financed continues to be the MCC-recipient's principal residence. MCCs are subject to the same targeting requirements as QMBs. MCCs also are subject to recapture rules like those applicable to QMBs.

Expiration

Authority to issue QMBs and to elect to trade in private activity bond volume authority to issue MCCs is scheduled to expire after June 30, 1992.

Description of Proposal

Authority to issue QMBs and to elect to trade in bond volume authority to issue MCCs would be extended for 18 months, through December 31, 1993.

Effective Date

The proposal would apply to bonds issued after June 30, 1992.

17. Special Depreciation Allowance for Certain Equipment Acquired in 1992

Present Law

Depreciation deductions

A taxpayer is allowed to recover, through annual depreciation deductions, the cost of certain property used in a trade or business or for the production of income. The amount of the depreciation deduction allowed with respect to tangible property for a taxable year is determined under the accelerated cost recovery system ("ACRS"), as modified by the Tax Reform Act of 1986. Under ACRS, different types of property are assigned applicable recovery periods and depreciation methods. The recovery periods applicable to most tangible personal property (generally tangible property other than residential rental property and nonresidential real property) range from 3 to 20 years. The depreciation methods generally applicable to tangible personal property are the 200-percent and 150-percent declining balance methods, switching to the straight-line method for the taxable year in which the depreciation deduction would be maximized.

For purposes of the alternative minimum tax ("AMT"), most tangible personal property is depreciated using the 150-percent declining balance method over useful lives that typically are longer than the applicable recovery periods for regular tax purposes. In addition, for purposes of the adjusted current earnings ("ACE") component of the corporate AMT, tangible personal property is depreciated using the straight-line method over these longer useful lives.

Expensing election

In lieu of depreciation, a taxpayer with a sufficiently small amount of annual investment may elect to deduct up to $10,000 of the cost of qualifying property placed in service for the taxable year. In general, qualifying property is defined as depreciable tangible personal property that is purchased for use in the active conduct of a trade or business. The $10,000 amount is reduced (but not below zero) by the amount by which the cost of qualifying property placed in service during the taxable year exceeds $200,000. In addition, the amount eligible to be expensed for a taxable year may not exceed the taxable income of the taxpayer for the year that is derived from the active conduct of a trade or business (determined without regard to this provision).

Description of Proposal

The proposal would allow an additional first-year depreciation deduction equal to 10 percent of the adjusted basis of certain qualified property that is placed in service before July 1, 1993. The additional depreciation deduction would be allowed for both regular tax and AMT purposes for the taxable year in which the property is placed in service. The basis of the property and the depreciation allowances in the year of purchase and later years would be appropriately adjusted to reflect the additional first-year depreciation deduction. A taxpayer would be allowed to elect not to claim the additional first-year depreciation for qualified property.

Property would qualify for the additional first-year depreciation deduction if (1) the property is section 1245 property to which ACRS applies (other than property that is required to be depreciated under the alternative depreciation system of ACRS) and (2) the original use of the property commences with the taxpayer on or after February 1, 1992. In addition, the property must be acquired by the taxpayer (1) on or after February 1, 1992, and before January 1, 1993, but only if no binding written contract for the acquisition is in effect before February 1, 1992, or (2) pursuant to a binding written contract which was entered into on or after February 1, 1992, and before January 1, 1993. Finally, property that is manufactured, constructed, or produced by the taxpayer for use by the taxpayer would qualify if the taxpayer begins the manufacture, construction, or production of the property on or after February 1, 1992, and before January 1, 1993 (and all other requirements are met).

The limitations on the amount of depreciation deductions allowed with respect to certain passenger automobiles (sec. 280F of the Code) would be adjusted to reflect the additional first year depreciation deduction.

The following examples illustrate the operation of the proposal.

Example 1.--Assume that on July 1, 1992, a calendar year taxpayer acquires and places in service qualified property that costs $1 million. Under the proposal, the taxpayer would be allowed an additional first-year depreciation deduction of $100,000. The remaining $900,000 of adjusted basis would be recovered in 1992 and subsequent years pursuant to the depreciation rules of present law.

Example 2.--Assume that on July 1, 1992, a calendar year taxpayer acquires and places in service qualified property that costs $30,000. In addition, assume that the property qualifies for the expensing election under section 179. Under the proposal, the taxpayer first would be allowed a $10,000 deduction under section 179. The taxpayer would then be allowed an additional first-year depreciation deduction of $2,000 based on $20,000 ($30,000 original cost less the section 179 deduction of $10,000) of adjusted basis.

Finally, the remaining adjusted basis of $18,000 ($20,000 adjusted basis less $2,000 additional first-year depreciation) would be recovered in 1992 and subsequent years pursuant to the depreciation rules of present law.

Effective Date

The proposal would apply to property placed in service on or after February 1, 1992.

18. Extension of Relief for AMT Purposes for Contributions of Appreciated Property

Present Law

In computing taxable income, a taxpayer who itemizes deductions generally is allowed to deduct the fair-market value of property contributed to a charitable organization.[1] However, in the case of a charitable contribution of inventory or other ordinary-income property, short-term capital gain property, or certain gifts to private foundations, the amount of the deduction generally is limited to the taxpayer's adjusted basis in the property. In the case of a charitable contribution of tangible personal property, a taxpayer's deduction is limited to the adjusted basis in such property if the use by the recipient charitable organization is unrelated to the organization's tax-exempt purpose (sec. 170(e)(1)(B)(i)).

For purposes of computing alternative minimum taxable income (AMTI), the deduction for charitable contributions of capital gain property (real, personal, or intangible) is disallowed to the extent that the fair-market value of the property exceeds its adjusted basis (sec. 57(a)(6)). However, in the case of a contribution made in a taxable year beginning in 1991 or made before July 1, 1992, in a taxable year beginning in 1992, this rule does not apply to contributions of tangible personal property.

Description of Proposal

AMT treatment of donated appreciated property

The proposal provides that all charitable contributions of appreciated property (real, personal, or intangible property) made during 1992 and 1993 would not be treated as a tax preference item for alternative minimum tax (AMT) purposes.

Advance determination of IRS position of value of donated tangible personal property

The Secretary of the Treasury would be directed to develop and implement a procedure under which the Secretary's position as to the value of tangible personal property could be ascertained for Federal income tax purposes prior to the

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[1] The amount of the deduction allowable for a taxable year with respect to a charitable contribution may be reduced depending on the type of property contributed, the type of charitable organization to which the property is contributed, and the income of the taxpayer (secs. 170(b) and 170(e)).

transfer of such property to a charitable organization. The Secretary would be required to submit a report not later than December 31, 1992, to the Senate Committee on Finance and the House Committee on Ways and Means, reporting on the development of such a procedure and the projected timetable for its implementation.

Study of tax treatment of corporate sponsorship payments to charitable organizations

The Treasury Department would be directed to conduct a study on the tax treatment of corporate sponsorship payments received by charitable and other tax-exempt organizations in connection with athletic (and other) events and the ramifications of IRS proposed examination guidelines contained in Announcement 92-15, 1992-5 I.R.B. 51. Within one year after the date of enactment, the Treasury Department would be required to report the results of this study to the Senate Committee on Finance and the House Committee on Ways and Means.

Effective Date

The proposal governing the AMT treatment of gifts of appreciated property would be effective for contributions made in 1992 and 1993.

The Secretary of Treasury would be required to report to Congress prior to December 31, 1992, on the development of an advance valuation procedure for certain donations, and within one year after the date of enactment, the results of a study of corporate sponsorship payments received by tax-exempt organizations.

19. Alternative Minimum Tax Relief for Intangible Drilling Costs of Oil and Gas Independent Producers

Present Law

Independent oil and gas producers who pay or incur intangible drilling or development costs ("IDCs") in the development of domestic oil or gas properties or certain geothermal wells, may elect either to expense or capitalize such amounts. If an election to expense IDCs is made, the taxpayer deducts the amount of the IDCs as an expense in the taxable year the cost is paid or incurred. Generally, if IDCs are not expensed, but are capitalized, they can be recovered through depletion or depreciation, as appropriate; or at the election of the taxpayer, they may be amortized over a 60-month period.

The difference between the amount of a taxpayer's IDC deductions and the amount which would have been currently deductible had IDCs been capitalized and recovered over a 10-year period constitute an item of tax preference for the alternative minimum tax (AMT) to the extent that this difference exceeds 65 percent of the taxpayer's net income from oil, gas, and geothermal properties for the taxable year. Moreover, for purposes of computing the "adjusted current earnings" (ACE) adjustment of the corporate AMT, IDCs are capitalized and amortized over the 60-month period beginning with the month in which they are paid or incurred.

A portion of the IDC tax preference and IDC-related ACE adjustment (together with a portion of preference and ACE adjustment related to percentage depletion from marginal properties) may operate to reduce an independent oil and gas producer's alternative minimum taxable income under a provision enacted as part of the Omnibus Budget Reconciliation Act of 1990 (the so-called "special energy deduction"). The special energy deduction is initially determined by determining the taxpayer's (1) IDC preference[1] and (2) marginal production depletion preference.[2] The IDC preference is apportioned between the portion of the preference related to exploratory drilling costs and the

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[1] The IDC preference is the amount by which the taxpayer's alternative minimum taxable income would be reduced if it were computed without regard to the excess IDC preference and the ACE IDC adjustment.

[2] The marginal production depletion preference is the amount by which the taxpayer's alternative minimum taxable income would be reduced if it were computed without regard to the excess depletion preference and the ACE depletion adjustment related to marginal property.

portion related to all other drilling costs. The portion of the preference related to exploratory IDCs is multiplied by 75 percent and the remaining portion is multiplied by 15 percent. The marginal production depletion preference is multiplied by 50 percent. These three products are then added together to arrive at the taxpayer's special energy deduction. The special energy deduction, however, may not reduce the taxpayer's alternative minimum taxable income by more than 40 percent.

Description of Proposal

For purposes of computing the AMT preference for IDCs of an independent oil and gas producer, the proposal would raise the 65-percent net oil and gas income offset to 80 percent. Thus, the difference between the amount of a taxpayer's IDC deductions and the amount which would have been currently deductible had IDCs been capitalized and recovered over a 10-year period would constitute an item of tax preference for an independent producer to the extent that this difference exceeds 80 percent of the taxpayer's net income from oil, gas, and geothermal properties for the taxable year.

In addition, for purposes of computing adjusted current earnings, the proposal would eliminate the requirement that independent oil and gas producers make an adjustment to alternative minimum taxable income for IDCs.

The proposal also would alter the special energy deduction. Under the proposal, the IDC component of the special energy deduction would be computed by multiplying the IDC preference by 50 percent. Thus, the proposal would eliminate any necessity to apportion the IDC preference between exploratory and all other IDCs. As under present law, the special energy deduction would be allowed to reduce a taxpayer's alternative minimum taxable income by no more than 40 percent.

Effective date

The proposal would be effective for taxable years beginning after December 31, 1991.

20. Elimination of ACE Depreciation Adjustment

Present Law

Under present law, a corporation is subject to an alternative minimum tax ("AMT") which is payable, in addition to all other tax liabilities, to the extent that it exceeds the corporation's regular income tax liability. Alternative minimum taxable income ("AMTI") is the corporation's taxable income increased by the corporation's tax preferences and adjusted by determining the tax treatment of certain items in a manner which negates the deferral of income resulting from the regular tax treatment of those items.

One of the adjustments which is made to taxable income to arrive at AMTI relates to depreciation. Depreciation on personal property to which the modified ACRS system adopted in 1986 applies is calculated using the 150-percent declining balance method (switching to straight line in the year necessary to maximize the deduction) over the life described in Code section 168(g) (generally the ADR class life of the property).

For taxable years beginning after 1989, AMTI is increased by an amount equal to 75 percent of the amount by which adjusted current earnings ("ACE") exceed AMTI (as determined before this adjustment). The ACE adjustment replaced the book-income adjustment applicable to tax years 1987 through 1989. In general, ACE means AMTI with additional adjustments that generally follow the rules presently applicable to corporations in computing their earnings and profits. For purposes of ACE, depreciation is computed using the straight-line method over the class life of the property. Thus, a corporation generally must make two depreciation calculations for purposes of the AMT--once using the 150-percent declining balance method and again using the straight-line method.

Description of Proposal

Effective for property placed in service on or after February 1, 1992, the proposal would eliminate the depreciation component of ACE for corporate AMT purposes. Thus, in computing ACE, a corporation would use the same depreciation methods and lives that it uses in computing AMTI (generally, the 150-percent declining balance method for tangible personal property).

Effective Date

The proposal would be effective for property placed in service on or after February 1, 1992.

21. Research and Experimentation Tax Credit

Present Law

A 20-percent tax credit is allowed to the extent that a taxpayer's qualified research expenditures for the current year exceed its base amount for that year. The credit will not apply to amounts paid or incurred after June 30, 1992.

The base amount for the current year generally is computed by multiplying the taxpayer's "fixed-base percentage" by the average amount of the taxpayer's gross receipts for the four preceding years. If a taxpayer both incurred qualified research expenditures and had gross receipts during each of at least three years from 1984 through 1988, then its "fixed-base percentage" is the ratio that its total qualified research expenditures for the 1984-1988 period bears to its total gross receipts for that period (subject to a maximum ratio of .16). All other taxpayers (such as "start-up" firms) are assigned a fixed-base percentage of .03.

In computing the credit, a taxpayer's base amount may not be less than 50 percent of its current-year qualified research expenditures.

Qualified research expenditures eligible for the credit consist of: (1) "in-house" expenses of the taxpayer for research wages and supplies used in research; (2) certain time-sharing costs for computer use in research; and (3) 65 percent of amounts paid by the taxpayer for contract research conducted on the taxpayer's behalf. Expenditures attributable to research that is conducted outside the United States do not enter into the credit computation. In addition, the credit is not available for research in the social sciences, arts, or humanities, nor is it available for research to the extent funded by any grant, contract, or otherwise by another person (or governmental entity).

In addition, the 20-percent tax credit also applies to the <u>excess</u> of (1) 100 percent of corporate cash expenditures (including grants or contributions) paid for university basic research <u>over</u> (2) the sum of (a) the greater of two fixed research floors plus (b) an amount reflecting any decrease in nonresearch giving to universities by the corporation as compared to such giving during a fixed-base period, as adjusted for inflation.

Deductions for qualified research expenditures allowed to a taxpayer under section 174 are reduced by an amount equal to 100 percent of the taxpayer's research credit determined for that year.

Description of Proposal

The research tax credit would be extended for 18 months (i.e., for qualified research expenditures and university basic research expenditures incurred through December 31, 1993).

Effective Date

The proposal would apply to qualified expenditures incurred during the period July 1, 1992, through December 31, 1993.

22. Progressive Capital Gains Tax Rates

Present Law

Under present law, ordinary income of an individual is taxed at a maximum marginal rate of 31 percent. The net capital gain of an individual is taxed at the same rates applicable to ordinary income, subject to a maximum marginal rate of 28 percent. Individuals with a net capital loss generally may deduct up to $3,000 of the loss each year against ordinary income. Net capital losses in excess of the $3,000 limit may be carried forward indefinitely.

Description of Proposal

An individual's net capital gain from the sale or exchange of qualified capital assets held more than two years ("qualified capital gain") would be taxed pursuant to a new progressive rate system.

A capital gains tax rate of 5, 19, 23, or 28 percent would apply depending on the individual's taxable income. The applicable capital gains tax rate would be determined by first taking into account taxable income computed without regard to the qualified capital gain. The qualified capital gain then would be added to such amount. The portion of qualified capital gain otherwise taxed at a 15-percent rate would be taxed at a rate of 5 percent; the portion otherwise taxed at a 28-percent rate would be taxed at a rate of 19 percent; the portion otherwise taxed at a 31-percent rate would be taxed at a rate of 23 percent; and the portion otherwise taxed at the 36-percent rate (as added by the proposal) would be taxed at a rate of 28 percent.

Qualified capital assets generally would be capital assets as defined under present law, except that collectibles would be excluded.

The entire amount of qualified capital gain would be included in alternative minimum taxable income.

Gain on the disposition of depreciable real property would be taxed as ordinary income to the extent of all previous depreciation allowances with respect to the property, subject to a maximum marginal rate of 31 percent.

Effective Date

The proposal would apply to dispositions (and installment payments received) on or after February 1, 1992. For the portion of 1992 to which the proposal would apply, the new capital gains rates would apply for qualified capital assets held more than one year. For 1993 and thereafter, the proposal would be fully phased in, and the new rates would apply for qualified capital assets held more than two years.

23. Exclusion for Capital Gains on Certain Small Business Stock

Present Law

Under present law, ordinary income of an individual is taxed at a maximum marginal rate of 31 percent. The net capital gain of an individual is taxed at the same rates applicable to ordinary income, subject to a maximum marginal rate of 28 percent. For corporations, the maximum rate on net capital gain is the same as the maximum rate on ordinary income, i.e., 34 percent.

The Tax Reform Act of 1986 repealed a provision allowing a noncorporate taxpayer a deduction for 60 percent of its net capital gain for the taxable year. Also under prior law, corporations were subject to an alternative tax of 28 percent on net capital gain. Net capital gain is the excess of net long-term capital gain for the taxable year over net short-term capital loss for that year. Gain or loss from the sale or exchange of a capital asset is treated as long term if the asset is held for more than one year.

Description of Proposal

Taxpayers would be entitled to exclude 50 percent of the gain realized on the sale or exchange of certain small business stock held for more than five years.[1]

In order to qualify as small business stock, the following requirements must be met: (1) the stock must be in a domestic corporation (other than a corporation engaged in certain disqualified activities);[2] (2) the corporation must satisfy an active business test (certain start-up activities would qualify); (3) the excess of (i) the amount of cash and

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1 A corporation would not be entitled to the exclusion if it owns more than 50 percent of the vote or value of the corporation issuing the small business stock.

2 An eligible corporation would not include a corporation predominantly engaged in a disqualified business (i.e., farming business, any business of operating a hotel, motel, restaurant or similar property, or any banking, insurance, financing or similar business). An eligible corporation also would not include a corporation with more than 10 percent of its assets in portfolio stock investments or real property not used in an active business (owning, renting or dealing in real property would not be active), a corporation the principal activity of which is the performance of personal services, a DISC, a 936 company, a RIC, REIT or REMIC, or any cooperative.

the aggregate adjusted bases of the corporation's assets, over (ii) the corporation's short-term debt, must not exceed $100 million;[3] and (4) the stock must be originally issued on or after February 1, 1992 to the taxpayer in exchange for money or other property (not including stock) or as compensation for services.[4]

In the case of stock acquired through the exercise of an option or through the conversion of convertible debt, the determination whether the $100 million assets test is met would be made at the time of exercise or conversion. In addition, the holding period of such stock would be treated as beginning on the date of exercise or conversion.

In the case of convertible preferred stock, the assets test would be made at the time the convertible stock is issued, and the holding period of the convertible stock would be added to that of the stock acquired upon conversion.

Stock received in connection with the performance of services would be treated as issued when included in the taxpayer's gross income.

The exclusion would be a preference for purposes of the alternative minimum tax.

Any gain from the sale or exchange of small business stock that is eligible for the exclusion would not also be eligible for the new progressive capital gains rate system (as added by the proposal).

Effective Date

The proposal would apply to stock issued on or after February 1, 1992.

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[3] If a corporation exceeds this limit at any time on or after February 1, 1992, the corporation could never issue stock that would qualify for the exclusion. A corporation that exceeds this limit could not split itself into smaller companies in an attempt to qualify new stock issued by such companies for the exclusion. If a corporation acquires substantially all the assets of a trade or business from another corporation whose assets exceed $100 million, stock in the acquiring corporation also would not qualify for the exclusion.

[4] In order to prevent evasion of the requirement that the stock be newly issued, the exclusion would not apply if the issuing corporation purchases any of its stock either one year before or one year after the new issuance, unless the corporation has a business purpose for the redemption.

24. Extension of Qualified Small-Issue Bonds

Present Law

Interest on certain small issues of private activity bonds ("qualified small-issue bonds") is excluded from gross income if certain conditions are met. First, at least 95 percent of the bond proceeds must be used to finance manufacturing facilities or certain agricultural land or equipment. Second, the bond issues must have an aggregate face amount of $1 million or less, or the aggregate face amount of the issue, together with the aggregate amount of certain related capital expenditures during the six-year period beginning three years before the date of the issue and ending three years after that date, may not exceed $10 million.

Authority to issue qualified small-issue bonds is scheduled to expire after June 30, 1992.

Description of Proposal

Authority to issue qualified small-issue bonds would be extended for 18 months, through December 31, 1993.

Effective Date

The proposal would be effective for bonds issued after June 30, 1992.

25. Business Energy Tax Credits for Solar and Geothermal Property

Present Law

Nonrefundable business energy tax credits are allowed for 10 percent of the cost of qualified solar and geothermal energy property (Code sec. 48(a)). Solar energy property that qualifies for the credit includes any equipment that uses solar energy to generate electricity, to heat or cool (or provide hot water for use in) a structure, or to provide solar process heat. Qualifying geothermal property includes equipment that produces, distributes, or uses energy derived from a geothermal deposit, but, in the case of electricity generated by geothermal power, only up to (but not including) the electrical transmission stage.[1]

The business energy tax credits currently are scheduled to expire with respect to property placed in service after June 30, 1992.

The business energy tax credits are components of the general business credit (sec. 38(b)(1)). The business energy tax credits, when combined with all other components of the general business credit, generally may not exceed for any taxable year the excess of the taxpayer's net income tax over the greater of (1) 25 percent of net regular tax liability above $25,000 or (2) the tentative minimum tax. An unused general business credit generally may be carried back 3 years and carried forward 15 years.

Description of Proposal

The proposal would extend the business credits for solar and geothermal property for 18 months, through December 31, 1993.

Effective Date

The proposal would be effective for qualifying solar and geothermal property placed in service after June 30, 1992.

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1 For purposes of the credit, a geothermal deposit is defined as a domestic geothermal reservoir consisting of natural heat which is stored in rocks or in an aqueous liquid or vapor, whether or not under pressure (sec. 613(e)(2)).

26. Classification of Multi-Purpose Vehicles

Present Law

Under present regulations, multi-purpose vehicles (MPVs) such as mini-vans and sport utility vehicles are inconsistently classified as autos or trucks. For purposes of emission and fuel economy standards, most MPVs are classified as trucks. However, for customs purposes, MPVs with more than two doors are generally classified under the Harmonized Tariff System (HTS) as vehicles "principally designed for the transport of persons" (HTS heading 8703), subject to a 2.5 percent duty. Two-door MPVs are generally classified as vehicles "principally designed for the transport of goods" (HTS heading 8704), subject to a 25 percent duty. The current tariff classification resulted from a controversial Treasury Department ruling in 1989 reversing an earlier Customs Service ruling which classified all MPVs under HTS heading 8704 and subjected them to the 25 percent duty.

Description of Proposal

The amendment would incorporate into the HTS language from the regulations of the Environmental Protection Agency and the Department of Transportation such that MPVs classified as trucks for emission and fuel economy standards would also be classified as trucks for tariff purposes. The effect would be to raise the duty on certain MPVs from 2.5 percent to 25 percent.

Effective Date

The proposal would be effective 15 days after the bill's enactment.

27. Limit Deduction for Executive Compensation

Present Law

Under present law, a deduction is allowed in computing Federal income tax liability for ordinary and necessary expenses paid or incurred during the taxable year in carrying on a trade or business, including a reasonable allowance for salaries or other compensation for personal services actually rendered.

Description of Proposal

For purposes of the regular income tax and the alternative minimum tax, the otherwise allowable deduction for compensation paid or accrued with respect to a covered employee would be limited to no more than $1 million per year. A covered employee means any employee of the taxpayer who is an officer of the taxpayer, other than an employee-owner of a personal service corporation.

The term covered employee would include former employees. Thus, for example, the proposal would apply to compensation paid to former employees (e.g., nonqualified deferred compensation that is not paid until after termination of employment) as well as current employees.

The proposal would not apply to compensation paid to employees who are not officers. Similarly, the proposal would not apply to payments to partners in a partnership because they are not employees. The proposal also would not apply to payments to independent contractors.

The deduction limitation generally would apply to all remuneration for services, including the cash value of all remuneration (including benefits) paid in a medium other than cash. The limit would not apply to fringe benefits excludable from income under section 132, meals and lodging furnished on the business premises of the employer that are excludable under section 119, or contributions to qualified pension and annuity plans or tax-sheltered annuities.

Effective Date

The proposal would be effective for taxable years beginning on or after January 1, 1992.

28. Employer-Provided Transportation Benefits

Present Law

Under Treasury regulations, monthly transit passes, tokens, etc., provided by an employer are excludable from an employee's income and wages for income and employment tax purposes as a de minimis fringe benefit if the total value of the transit pass does not exceed $21. If the total value of such benefits exceeds $21 per month, the full value of the benefits is includible in income.

Parking at or near the employer's business premises that is paid for by the employer is excludable from the gross income of the employee as a working condition fringe benefit, regardless of the value of the parking.

Description of Proposal

Under the proposal, gross income would not include qualified transportation fringe benefits. In general, a qualified transportation fringe would be (1) transportation in a commuter highway vehicle if such transportation is in connection with travel between the employee's residence and place of employment, (2) a transit pass, or (3) qualified parking. The maximum amount of qualified parking that could be excluded from an employee's gross income would be $160 per month (regardless of the total value of the parking). Other qualified transportation fringes would be excludable from gross income to the extent that the aggregate value of the benefits does not exceed $60 per month. Both dollar limits would be indexed for inflation.

A transit pass would include any pass, token, farecard, voucher, or similar item entitling a person to transportation on mass transit facilities (whether or not publicly owned). Types of transit facilities that could qualify for the exclusion include, for example, rail, bus, and ferry.

Qualified parking would be parking provided to an employee on or near the business premises of the employer or on or near a location from which the employee commutes to work by mass transit, in a commuter highway vehicle, or by carpool.

Effective Date

The proposal would apply to benefits provided by the employer on or after January 1, 1992, except that the $160 per month limit on the exclusion for qualified parking benefits would apply to benefits provided after the date of enactment.

29. Repeal of Luxury Excise Tax on Boats, Aircraft, Jewelry, and Furs; Modification of Luxury Excise Tax on Vehicles

Present Law

Present law imposes ten-percent excise taxes on the portion of the retail price of the following items that exceeds the thresholds specified: automobiles above $30,000; boats above $100,000; aircraft above $250,000; jewelry above $10,000; and furs above $10,000.

The tax generally applies only to the first retail sale after manufacture, production or importation of items subject to the tax. It does not apply to subsequent sales of these items. The taxes on automobiles, boats, and aircraft generally do apply to items used in a trade or business.

The tax applies to sales before January 1, 2000.

Description of Proposal

The proposal would repeal the excise taxes imposed on boats, airplanes, jewelry, and furs.

The proposal also would modify the tax on automobiles to provide that the $30,000 threshold is indexed for inflation occurring after 1990.

Effective Date

The repeal of the taxes on boats, aircraft, jewelry, and furs would be effective for sales on or after January 1, 1992. The indexation of the threshold applicable to automobiles would be effective for sales on or after January 1, 1992.

30. Impose Excise Tax on Diesel Fuel Used in Noncommercial Motorboats

Present Law

Federal excise taxes generally are imposed on gasoline and special motor fuels used in highway transportation and by certain off-highway recreational trail vehicles and by motorboats (14 cents per gallon). A Federal excise tax also is imposed on diesel fuel (20 cents per gallon) used in highway transportation. Diesel fuel used in trains generally is taxed at 2.5 cents per gallon.

The revenues from these taxes, minus 2.5 cents per gallon, are deposited in the Highway Trust Fund ("HTF"), the National Recreational Trails Trust Fund, or the Aquatic Resources Trust Fund through September 30, 1999. Revenues from the remaining 2.5 cents per gallon are retained in the General Fund through September 30, 1995, after which time the 2.5-cents-per-gallon portion of the taxes (including the tax on diesel fuel used in trains) is scheduled to expire.

An additional 0.1-cent-per-gallon tax applies to these fuels to finance the Leaking Underground Storage Trust Fund ("LUST Fund"), generally through December 31, 1995.

Diesel fuel used in motorboats is not taxed.

Description of Proposal

The provision would extend the current 20.1-cents-per-gallon diesel fuel excise taxes to diesel fuel used by recreational motorboats. Fuel used by motorboats for commercial fishing, transportation for compensation or hire, or for business use other than predominantly for entertainment, amusement, or recreation, would remain exempt.

As under the President's budget proposal, the tax is collected at the same point in the distribution chain as the highway diesel fuel tax (i.e., on sale to a retailer). However, to prevent unnecessary tax-paid sales followed by refunds, retailers that sell diesel fuel exclusively to commercial (i.e., nonpleasure) boats are permitted to buy the fuel tax-free.

The revenues from the entire 20.1-cents-per-gallon tax on diesel fuel used by motorboats would be retained in the General Fund.

Effective Date

The provision would be effective after June 30, 1992.

31. Access to Tax Information by the Department of Veterans Affairs

Present Law

The Internal Revenue Code prohibits disclosure of tax returns and return information of taxpayers, with exceptions for authorized disclosure to certain Governmental entities in certain enumerated instances (sec. 6103). Unauthorized disclosure is a felony punishable by a fine not exceeding $5,000 or imprisonment of not more than five years, or both (sec. 7213). An action for civil damages also may be brought for unauthorized disclosure (sec. 7431).

Among the disclosures permitted under the Code is disclosure to the Department of Veterans Affairs (DVA) of self-employment tax information and certain tax information supplied to the IRS and SSA by third-parties. Disclosure is permitted to assist DVA in determining eligibility for, and establishing correct benefit amounts under, certain of its needs-based pension and other programs (sec. 6103(l)(7)(D)(viii)). The income tax returns filed by the veterans themselves are not disclosed to DVA.

The DVA disclosure provision is scheduled to expire after September 30, 1992.

Description of Proposal

The proposal would extend this authority to disclose tax information for six years.

Effective Date

The DVA disclosure provision would expire after September 30, 1998.

32. Extension of Excise Tax on Certain Vaccines for the Vaccine Injury Compensation Trust Fund

Present Law

The Vaccine Injury Compensation Trust Fund ("Vaccine Trust Fund") provides a source of revenue to compensate individuals who are injured (or die) as a result of the administration of certain vaccines: diphtheria, pertussis, and tetanus ("DPT"); diphtheria and tetanus ("DT"); measles, mumps, and rubella ("MMR"); and polio. The Vaccine Trust Fund provides the funding source for the National Vaccine Injury Compensation Program ("Program"), which provides a substitute, Federal "no-fault" insurance system for the State-law tort and private liability insurance systems otherwise applicable to vaccine manufacturers.

The Vaccine Trust Fund is funded by a manufacturer's excise tax on DPT, DT, MMR, and polio vaccines (and any other vaccines used to prevent these diseases). The excise tax per dose is $4.56 for DPT, $0.06 for DT, $4.44 for MMR, and $0.29 for polio vaccines.

The vaccine excise tax will expire after the later of: (1) December 31, 1992; or (2) the date on which the Vaccine Trust Fund revenues exceed the projected liabilities with respect to compensable injuries from vaccines administered before October 1, 1992. Amounts in the Vaccine Trust Fund are available for the payment of compensation under the Program with respect to vaccines administered after September 30, 1988, and before October 1, 1992.

Description of Proposal

The present-law excise taxes imposed on certain vaccines and the Vaccine Trust Fund would be extended for two years (through December 31, 1994, and October 1, 1994, respectively).

The Treasury and Health and Human Services Departments would be required to study and report to the Committees on Finance and Ways and Means by January 1, 1994, certain issues regarding Vaccine Trust Fund funding needs and appropriateness of imposition and rate of tax on covered vaccines.

Effective Date

The provisions would be effective on the date of enactment.

33. Permanent Extension of General Fund Transfer to Railroad Retirement Tier 2 Fund

Present Law

The proceeds from the income taxation of railroad retirement Tier 2 benefits are transferred from the general fund of the Treasury to the Railroad Retirement Account. This transfer applies only to proceeds from the taxation of benefits which have been received prior to October 1, 1992. Proceeds from the taxation of benefits received after this date remain in the general fund.

Description of Proposal

The transfer of proceeds from the income taxation of railroad retirement Tier 2 benefits from the general fund of the Treasury to the Railroad Retirement Account would be made permanent.

Effective Date

The provision would be effective beginning September 30, 1992.

34. Allocation and Apportionment of Research Expenses

Present Law

U.S. persons are taxable on their worldwide income, including their foreign income. Foreign source taxable income equals foreign source gross income less the expenses, losses and other deductions properly apportioned or allocated to that income. The Internal Revenue Code generally articulates only the broad principles of how expenses reduce U.S. and foreign source gross income, leaving the Treasury Department to provide detailed rules for the task of allocating and apportioning expenses.

Treasury regulations issued in 1977 described methods for allocating expenses between U.S. and foreign source income, including rules for the allocation of research and development (R&D) expenses. Upon issuance of these regulations, a significant dispute regarding the appropriate allocation of R&D expenses developed between taxpayers and the Treasury Department. This unresolved dispute between taxpayers and the Treasury Department precipitated Congressional involvement on this issue, and since 1981, the R&D allocation regulations have been subject to a series of eight suspensions and temporary modifications. The current temporary provision is applicable generally for the first six months of the first taxable year beginning after August 1, 1991, and among other rules, automatically allocates 64 percent of U.S. performed R&D to U.S. source income, and generally permits a greater amount of taxable income to be classified as foreign source than under the 1977 regulations. This will increase the benefits of the foreign tax credit to many taxpayers.

Description of Proposal

The report of the Senate Finance Committee on the bill would contain language indicating that it believes that the Administration has broad authority under current law to revise the current R&D allocation regulations. The report would state that since the Administration has indicated its support of an allocation system that provides incentives to increase the performance of U.S.-based research activities, the committee expects, and in the strongest terms, urges the Treasury Department to revise its permanent regulations in a manner consistent with the Administration's stated objectives and proposals. The report would state that the committee believes that such a revision would be consistent both with current law regulatory authority and with the stated goals of the Administration.

The report would state that the committee further urges the Treasury Department, when revising its regulations, to take into consideration that taxpayers, in appropriate circumstances, are required for business purposes to conduct significant amounts of R&D at foreign sites and should not be penalized by the allocation rules.

Effective Date

The report would state that the committee expects and requests the Treasury Department to issue regulations no later than June 1, 1992, to be effective after the termination of the current temporary rules.

C. Provisions to Ensure High-Income Taxpayers Pay Their Fair Share

1. Individual Income Tax Rates (36-Percent Bracket)

Present Law

For 1992, the individual income tax rate schedules are as follows--

If taxable income is	Then income tax equals
Single individuals	
$0-$21,450	15 percent of taxable income.
$21,450-$51,900	$3,217.50 plus 28% of the amount over $21,450.
Over $51,900	$11,743.50 plus 31% of the amount over $51,900.
Heads of households	
$0-$28,750	15 percent of taxable income.
$28,750-$74,150	$4,312.50 plus 28% of the amount over $28,750.
Over $74,150	$17,024.50 plus 31% of the amount over $74,150.
Married individuals filing joint returns	
$0-$35,800	15 percent of taxable income.
$35,800-$86,500	$5,370 plus 28% of the amount over $35,800.
Over $86,500	$19,566 plus 31% of the amount over $86,500.
Married individuals filing separate returns	
$0-17,900	15 percent of taxable income.
$17,900-$43,250	$2,685 plus 28% of the amount over $17,900.
Over $43,250	$9,783 plus 31% of the amount over $43,250.

Estates and trusts

$0-3,600	15 percent of taxable income.
$3,600-$10,900	$540 plus 28% of the amount over $3,600.
Over $10,900	$2,584 plus 31% of the amount over $10,900.

Description of Proposal

The proposal would create a 36-percent bracket for taxable incomes above: $150,000 (unmarried individuals filing single returns); $162,500 (unmarried individuals filing as heads of households); $175,000 (married individuals filing joint returns); $87,500 (married individuals filing separate returns); and $3,500 (estates and trusts). The thresholds for the 36-percent bracket would be adjusted for inflation in the same manner as under present law. The individual income tax rate schedules for 1992 would be as follows--

If taxable income is	Then income tax equals
Single individuals	
$0-$21,450	15 percent of taxable income.
$21,450-$51,900	$3,217.50 plus 28% of the amount over $21,450.
$51,900-$150,000	$11,743.50 plus 31% of the amount over $51,900.
Over $150,000	$42,154.50 plus 36% of the amount over $150,000.
Heads of households	
$0-$28,750	15 percent of taxable income.
$28,750-$74,150	$4,312.50 plus 28% of the amount over $28,750.
$74,150-$162,500	$17,024.50 plus 31% of the amount over $74,150.
Over $162,500	$44,413 plus 36% of the amount over $162,500.
Married individuals filing joint returns	
$0-$35,800	15 percent of taxable income.
$35,800-$86,500	$5,370 plus 28% of the amount over $35,800.

$86,500-$175,000	$19,566 plus 31% of the amount over $86,500.
Over $175,000	$47,001 plus 36% of the amount over $175,000.

Married individuals filing individuals separate returns

$0-$17,900	15 percent of taxable income.
$17,900-$43,250	$2,685 plus 28% of the amount over $17,900.
$43,250-$87,500	$9,783 plus 31% of the amount over $43,250.
Over $87,500	$23,500.50 plus 36% of the amount over $87,500.

Estates and trusts

$0-3,500	15 percent of taxable income.
Over $3,500	$525 plus 36% of the amount over $3,500.

Effective Date

The proposal would be effective for taxable years beginning after December 31, 1991.

2. Surtax on Taxable Income in Excess of $1 Million

Present Law

Under present law, there is no surtax imposed on higher-income individuals.

Description of Proposal

The proposal would impose a 10-percent surtax on individuals with taxable income over $1,000,000 ($500,000 for married taxpayers filing separate returns). The surtax would equal 10 percent of otherwise computed tax liability multiplied by the ratio of taxable income in excess of $1,000,000 to total taxable income. The effect of the proposal would be that the more that taxable income exceeds $1,000,000, the closer the surtax approaches a 10-percent increase in total tax liability.

A 2.4-percentage point surtax would apply to individuals with alternative minimum taxable income above $1,000,000 ($500,000 for married taxpayers filing separate returns). The surtax would be applied by increasing the taxpayer's tentative minimum tax by 2.4 percent of the amount by which the taxpayer's alternative minimum taxable income exceeds $1,000,000 ($500,000 for married taxpayers filing separate returns).

Effective Date

The proposal would be effective for taxable years beginning after December 31, 1991.

3. Extension of Itemized Deduction Limitation

Present Law

Under present law, individuals who do not elect the standard deduction may claim itemized deductions (subject to certain limitations) for certain nonbusiness expenses incurred during the taxable year. Among these deductible expenses are unreimbursed medical expenses, casualty and theft losses, charitable contributions, qualified residence interest, State and local income and property taxes, unreimbursed employee business expenses, and certain other miscellaneous expenses.

Certain itemized deductions are allowed only to the extent that the amount exceeds a specified percentage of the taxpayer's adjusted gross income (AGI). Unreimbursed medical expenses for care of the taxpayer and the taxpayer's spouse and dependents are deductible only to the extent that the total of these expenses exceeds 7.5 percent of the taxpayer's AGI. Nonbusiness casualty or theft losses are deductible only to the extent that the amount of loss arising from each casualty or theft exceeds $100 and only to the extent that the net amount of casualty and theft losses exceeds 10 percent of the taxpayer's AGI. Unreimbursed employee business expenses and certain other miscellaneous expenses are deductible only to the extent that the total of these expenses exceeds 2 percent of the taxpayer's AGI.

The total amount of otherwise allowable itemized deductions (other than medical expenses, casualty and theft losses, and investment interest) is reduced by 3 percent of the amount of the taxpayer's AGI in excess of $105,250 in 1992 (indexed for inflation). Under this provision, otherwise allowable itemized deductions may not be reduced by more than 80 percent. In computing the reduction of total itemized deductions, all present-law limitations applicable to such deductions are first applied and then the otherwise allowable total amount of deductions is reduced in accordance with this provision.

The reduction of otherwise allowable itemized deductions does not apply to taxable years beginning after December 31, 1995.

Description of Proposal

The proposal would extend permanently the present-law itemized deduction limitation applicable to higher-income individuals.

Effective Date

The proposal would be effective for taxable years beginning in 1996 and thereafter.

4. Extension of Personal Exemption Phaseout

Present Law

Present law permits a personal exemption deduction from gross income for an individual, the individual's spouse, and each dependent. For 1992, the amount of this deduction is $2,300 for each exemption claimed. This exemption amount is adjusted for inflation. The deduction for personal exemptions is phased out for taxpayers with adjusted gross income (AGI) above a threshold amount (indexed for inflation) which is based on filing status. For 1992, the threshold amounts are $157,900 for married taxpayers filing joint returns, $78,950 for married taxpayers filing separate returns, $131,550 for unmarried taxpayers filing as head of household, and $105,250 for unmarried taxpayers filing as single.

The total amount of exemptions which may be claimed by a taxpayer is reduced by 2 percent for each $2,500 (or portion thereof) by which the taxpayer's AGI exceeds the applicable threshold (the phaseout rate is 4 percent for married taxpayers filing separate returns). Thus, the personal exemptions claimed are phased out over a $122,500 range, beginning at the applicable threshold.

This provision does not apply to taxable years beginning after December 31, 1995.

Description of Proposal

The proposal would extend permanently the present-law personal exemption phaseout.

Effective Date

The proposal would be effective for taxable years beginning in 1996 and thereafter.

5. Conform Book and Tax Accounting for Securities Inventories

Present Law

A taxpayer that is a dealer in securities is required for Federal income tax purposes to maintain an inventory of securities held for sale to customers. A dealer in securities is allowed for Federal income tax purposes to determine (or value) the inventory of securities held for sale based on: (1) the cost of the securities; (2) the lower of the cost or market value of the securities; or (3) the market value of the securities.

If the inventory of securities is determined based on cost, unrealized gains and losses with respect to the securities are not taken into account for Federal income tax purposes. If the inventory of securities is determined based on the lower of cost or market value, unrealized losses (but not unrealized gains) with respect to the securities are taken into account for Federal income tax purposes. If the inventory of securities is determined based on market value, both unrealized gains and losses with respect to the securities are taken into account for Federal income tax purposes.

For financial accounting purposes, the inventory of securities generally is determined based on market value.

Description of Proposal

Under the proposal, taxpayers who hold securities as inventory would be required to include such securities in inventory at market value for Federal income tax purposes.

Effective Date

The proposal would apply to taxable years ending on or after December 31, 1993. Any increase in inventory required by this change in method of accounting would be included in gross income ratably over 10 taxable years.

6. Modify Estimated Tax Payment Rules for Large Corporations

Present Law

A corporation is subject to an addition to tax for any underpayment of estimated tax. For taxable years beginning in 1993, 1994, 1995, and 1996, a corporation does not have an underpayment of estimated tax if it makes four equal timely estimated tax payments that total at least 95 percent of the tax liability shown on the return for the current taxable year. In addition, a corporation may annualize its taxable income and make estimated tax payments based on 95 percent of the tax liability attributable to such annualized income.

For taxable years beginning in 1992, the 95 percent requirement is a 93 percent requirement; the 95 percent requirement becomes a 90 percent requirement for taxable years beginning in 1997 and thereafter.

A corporation that is not a "large corporation" generally may avoid the addition to tax if it makes four timely estimated tax payments each equal to at least 25 percent of its tax liability for the preceding taxable year (the "100 percent of last year's liability safe harbor"). A large corporation may use this rule with respect to its estimated tax payment for the first quarter of its current taxable year. A large corporation is one that had taxable income of $1 million or more for any of the three preceding taxable years.

Description of Proposal

For taxable years beginning after 1996, a corporation that does not use the 100 percent of last year's liability safe harbor for its estimated tax payments would be required to base its estimated tax payments on 95 percent (rather than 90 percent) of its current year tax liability, whether such liability is determined on an actual or annualized basis.

The proposal would not change the present-law availability of the 100 percent of last year's liability safe harbor for large or small corporations.

Effective Date

The proposal would be effective for estimated tax payments with respect to taxable years beginning after December 31, 1996.

7. Modify Individual Estimated Tax Requirements

Present Law

Under present law, an individual taxpayer generally is subject to an addition to tax for any underpayment of estimated tax. An individual generally does not have an underpayment of estimated tax if he or she makes timely estimated tax payments at least equal to: (1) 100 percent of the tax liability of the prior year (the "100 percent of last year's liability safe harbor") or (2) 90 percent of the tax liability of the current year. Income tax withholding from wages is considered to be a payment of estimated taxes.

In addition, under a special rule, for taxable years beginning after 1991 and before 1997, a taxpayer generally may not use the 100 percent of last year's liability safe harbor if (1) the taxpayer has an adjusted gross income (AGI) in the current year that exceeds the taxpayer's AGI in the prior year by more than $40,000 ($20,000 in the case of a separate return by a married individual) and (2) the taxpayer has an AGI in excess of $75,000 in the current year ($37,500 in the case of a separate return by a married individual).

Description of Proposal

The special rule that denies the use of the 100 percent of last year's liability safe harbor would be made permanent.

In addition, the proposal would clarify the application of the special rule to estates and trusts.

Effective Date

The proposal would be effective for estimated tax payments applicable to taxable years beginning after December 31, 1991.

DESCRIPTION OF S. 1394
(TAX SIMPLIFICATION ACT OF 1991)
AND PROPOSED MODIFICATIONS

Scheduled for Markup

by the

SENATE COMMITTEE ON FINANCE

On March 3, 1992

Prepared by the Staff

of the

JOINT COMMITTEE ON TAXATION

March 3, 1992

JCX-8-92

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INTRODUCTION

This document,[1] prepared by the staff of the Joint Committee on Taxation, provides a brief description of the provisions of S. 1394 ("Tax Simplification Act of 1991") and proposed modifications. These provisions are scheduled for markup by the Senate Committee on Finance on March 3, 1992.

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[1] This document may be cited as follows: Joint Committee, Description of S. 1394 (Tax Simplification Act of 1991) and Proposed Modifications (JCX-8-92), March 3, 1992.

S. 1394 -- THE TAX SIMPLIFICATION ACT OF 1991

Title I.--Individual Tax Provisions

1. Rollover of gain on sale of principal residence (sec. 101 of the bill)

Description of Bill

Under present law no gain is recognized on the sale of a principal residence if a new residence at least equal in cost to the sales price of the old residence is purchased and used by the taxpayer as his or her principal residence within a specified period of time. This replacement period generally begins two years before and ends two years after the date of sale of the old residence. The basis of the replacement residence is reduced by the amount of any gain not recognized on the sale of the old residence by reason of section 1034.

The determination whether property is used by a taxpayer as a principal residence depends upon all the facts and circumstances in each case, including the good faith of the taxpayer. No safe harbor is provided for sales of principal residences incident to divorce or marital separation.

In general, nonrecognition treatment is available only once during any two-year period. In addition, if the taxpayer purchases more than one residence during the replacement period and such residences are each used as the taxpayer's principal residence within two years after the date of sale of the old residence, only the last residence so used is treated as the new replacement residence.

Special rules apply, however, if residences are sold in order to relocate for employment reasons. First, the number of times nonrecognition treatment is available during a two-year period is not limited. Second, if a residence is sold within two years after the sale of the old residence, the residence sold is treated as the last residence used by the taxpayer and thus as the only replacement residence.

Under the bill, gain is rolled over from one residence to another residence in the order the residences are purchased and used, regardless of the taxpayer's reasons for the sale of the old residence. In addition, gain may be rolled over more than once within a two-year period. Thus, the rules that formerly applied only if a taxpayer sold his or her residence in order to relocate for employment purposes will apply in all cases.

As under present law, the basis of each succeeding residence is reduced by the amount of gain not recognized on the sale of the prior residence.

Effective date.--The provision applies to sales of old residences (within the meaning of section 1034) after the date of enactment.

Proposed Modification

Delete the provision relating to multiple residences within the rollover period.

Also, provide a safe harbor in the determination of principal residence in certain cases incident to divorce or marital separation. Specifically, provide that a residence is treated as the taxpayer's principal residence at the time of sale if (1) the residence is sold pursuant to a divorce or marital separation, and (2) the taxpayer used such residence as his or her principal residence at any time during the two-year period ending on the date of sale.

Effective date.--The provision applies to sales of old residences (within the meaning of section 1034) after the date of enactment.

2. Due dates for estimated tax payments of individuals (sec. 102 of the bill)

Description of Bill

Under the bill, the due date for the second estimated tax payment of individuals is July 15th of the taxable year for which the payment relates.

Effective date.--The provision is effective for taxable years beginning after December 31, 1991.

Proposed Modification

Delete the provision.

3. Payment of tax by credit card (sec. 103 of the bill)

Description of Bill

The bill permits payment of taxes by credit card, to the extent and under the conditions provided by regulations.

Effective date.--The provision is effective on the date of enactment.

4. Election by parent to claim unearned income of certain children on parent's return (sec. 104 of the bill)

Description of Bill

The bill adjusts for inflation the dollar amounts entered on the Federal income tax return of a parent electing to report a child's unearned income. It likewise indexes the fixed dollar amount used in computing the child's exemption under the alternative minimum tax.

Effective date.--Taxable years beginning after December 31, 1991.

5. Simplified foreign tax credit limitation for individuals (sec. 105 of the bill)

Description of Bill

The bill allows individuals with no more than $200 of creditable foreign taxes, and no foreign source income other than income which is in the passive basket, to elect a simplified foreign tax credit limitation equal to the lesser of 25 percent of the individual's foreign source gross income or the amount of the creditable foreign taxes paid or accrued by the individual during the taxable year. A person who elects the simplified foreign tax credit limitation is not allowed a credit for any foreign tax not shown on a payee statement furnished to him or her, nor is the person entitled to treat any excess credits for a taxable year to which the election applied as a carryover to another taxable year.

For purposes of the simplified limitation, passive income generally is defined to include all types of income that would be foreign personal holding company income under the subpart F rules, plus income inclusions from passive foreign corporations (as defined by the bill), so long as the income is shown on a payee statement furnished to the individual. The statutory exceptions to treating these types of income as passive for foreign tax credit limitation purposes, such as the exceptions for high-taxed income and high withholding tax interest, are not applicable in determining eligibility to use the simplified limitation.

Effective date.--Taxable years beginning after December 31, 1991.

6. Personal transactions by individuals in foreign currency (sec. 106 of the bill)

Description of Bill

In a case where an individual acquires nonfunctional currency and then disposes of it in a personal transaction, and where exchange rates have changed in the intervening period, the bill provides for nonrecognition of an individual's resulting exchange gains not exceeding $200. The bill does not change the treatment of resulting exchange losses. It is understood that under other Code provisions, such losses typically are not deductible by individuals (e.g., sec. 165(c)).

Effective date.--Taxable years beginning after December 31, 1991.

7. Due date for furnishing information to partners of large partnerships (sec. 107 of the bill)

Description of Bill

The bill provides that a large partnership must furnish information returns to partners by the 15th day of the third month following the close of the partnership's taxable year. A large partnership is any partnership with 250 or more partners as well as any partnership subject to the simplified reporting rules for large partnerships (contained in sec. 201 of this bill, described below).

Effective date.--The provision is effective for taxable years ending on or after December 31, 1992.

Proposed Modification

Require information returns to be furnished by the first March 15 following the close of the partnership's taxable year, applicable only to those partnerships subject to the simplified reporting rules for large partnerships.

8. Make income tax withholding rules parallel to rules for exclusion from income for combat pay (sec. 108 of the bill)

Description of Bill

The bill makes the income tax withholding exemption rules parallel to the rules providing for an exclusion from gross income for combat pay.

Effective date.--The provision is effective as of January 1, 1992.

9. Expanded access to simplified income tax returns (sec. 109 of the bill)

Description of Bill

The bill provides that the Secretary of the Treasury (or his delegate) shall take such actions as may be appropriate to expand access to simplified individual income tax forms and to otherwise simplify the individual income tax returns.

The bill also requires that the Secretary submit a report to the Congress on the actions undertaken pursuant to this provision, together with any recommendations he may deem advisable.

Effective date.--The report is due no later than one year after the date of enactment.

10. Simplification of tax treatment of rural letter carriers' vehicle expenses (sec. 110 of the bill)

Description of Bill

The bill repeals the special reimbursement rate available to rural letter carriers who are employees of the U.S. Postal Service of 150 percent of the standard mileage rate. In its place, the bill provides that the rate of reimbursement provided by the Postal Service to rural letter carriers is considered to be equivalent to their expenses. The rate of reimbursement that is considered to be equivalent to their expenses is the current rate of reimbursement contained in the 1991 collective bargaining agreement, which may in the future be increased by no more than the rate of inflation.

Effective date.--The provision is effective for taxable years beginning after December 31, 1991.

11. Exemption from luxury excise tax for certain equipment installed on passenger vehicles for use by disabled individuals (sec. 111 of the bill)

Description of Bill

The bill provides that the luxury excise tax does not apply to a part or accessory installed on a passenger vehicle which compensates for the effect of the disability and enables or assists an individual with a disability to operate the vehicle, or to enter or exit the vehicle.

Effective date.--The provision is effective for purchases after December 31, 1990.

Title II. Treatment of Large Partnerships

A. General Provisions

1. Simplified flow-through for large partnerships (sec. 201 of the bill)

Description of Bill

The bill modifies the tax treatment of a large partnership (generally, a partnership with at least 250 partners, or an electing partnership with at least 100 partners) and its partners. The bill provides that each partner takes into account separately the partner's distributive share of the following items, which are determined at the partnership level: (1) taxable income or loss from passive loss limitation activities; (2) taxable income or loss from other activities (e.g., portfolio income or loss); (3) net capital gain to the extent allocable to passive loss limitation activities and other activities; (4) net alternative minimum tax adjustment separately computed for passive loss limitation activities and other activities; (5) general credits; (6) low-income housing credit; (7) rehabilitation credit; (8) for certain partnerships, tax-exempt interest; and (9) for certain partnerships, foreign taxes paid and foreign source partnership items.

All limitations and other provisions affecting the computation of taxable income or any credit generally are applied at the partnership (and not the partner) level. In addition, all elections affecting the computation of taxable income or any credit are made by the partnership.

In general, the large partnership rules do not apply to an excluded partner's distributive share of partnership items. An excluded partner is any partner (1) owning more than a five percent partnership interest, or (2) materially participating in the partnership's activities and holding any interest that is not a limited partnership interest.

The large partnership rules do not apply to a partnership if at least 50 percent of the value of its assets consists of oil or gas properties. In addition, the rules do not apply to any item attributable to any partnership oil or gas property. An election to apply these rules, however, generally can be made, in which event depletion is computed without regard to percentage depletion, and integrated oil companies and partners holding working interests in oil and gas are treated as excluded partners.

For all partners contributing property to a large partnership, the bill replaces section 704(c) with a "deferred sale" approach. Under the bill, a large partnership takes a fair market value basis in the property, and the contributing partner's precontribution gain or loss is deferred until the occurrence of specified recognition events.

Effective date.--The provisions generally apply to partnership taxable years ending on or after December 31, 1992.

Proposed Modifications

The modifications proposed to be made to the simplified reporting provisions of the large partnership proposal include the following: (1) generally eliminating the excluded partner concept; (2) separately stating creditable foreign taxes and foreign source items for all large partnerships, regardless of whether foreign source income is at least 25 percent of the partnership's gross income; (3) separately stating tax-exempt interest for all large partnerships, regardless of whether at least 50 percent of the value of the partnership's assets consists of tax-exempt obligations; (4) separately stating net capital loss as well as net capital gain, and treating such gain or loss as long-term capital gain or loss; (5) with respect to corporate partners, determining the net AMT adjustment by using the adjustments applicable to corporations; (6) excluding REMIC excess inclusion income from the gross income of the partnership; (7) separately stating a large partnership's discharge of indebtedness income, and clarifying that the provisions of section 108 apply without regard to the large partnership rules; (8) applying certain installment sale rules at the partnership level; (9) modifying the exclusion for service partnerships; (10) allowing the partnership (and not the partners) any credit for RIC capital gains; (11) excluding from the simplified reporting and audit regimes any partnership the principal activity of which is the buying and selling of commodities, or options, futures or forwards with respect to commodities; (12) modifying the deferred sale rules so that certain nonrecognition transactions would not be treated as dispositions that would trigger a contributing partner's deferred gain or loss; and (13) separately stating the credit for producing fuel from a nonconventional source.

The special rules applicable to large partnerships holding oil and gas properties would be modified as follows: (a) the simplified reporting regime would be made elective for large partnerships with at least 25 percent (measured by value) of their assets in oil or gas properties; (b) the computation of both cost depletion and percentage depletion (without application of either the "65-percent of taxable income" limitation or the 1,000-barrel-per-day limitation) would be made at the partnership level; and (c) partners who either do not qualify for percentage depletion deductions or for full expensing of intangible drilling and development costs (i.e., integrated oil and gas companies), or who have average daily production of more than 500 barrels of oil and gas, would be disqualified from the large partnership simplified reporting regime with respect to items related to partnership oil or gas property.

In addition to the modifications described above, other clarifying, conforming, clerical and miscellaneous modifications are proposed to the simplified reporting provisions.

2. Simplified audit procedures for large partnerships (sec. 202 of the bill)

Description of Bill

The bill creates a new audit system for large partnerships. The bill defines "large partnership" the same way for audit and reporting purposes (generally, partnerships with at least 250 partners) except that certain oil and gas partnerships are large partnerships for the audit rules but are not subject to the large partnership reporting requirements.

As under present law, large partnerships and their partners are subject to unified audit rules. Unlike present law, however, partnership adjustments generally will flow through to the partners for the year in which the adjustment takes effect. Thus, the current-year partners will adjust their current-year share of partnership items of income, gains, losses, deductions, or credits to reflect partnership adjustments that take effect that year. The adjustments generally will not affect prior year returns of any partners (except in the case of changes to any partner's distributive shares).

Effective date.--The bill applies to partnership taxable years ending on or after December 31, 1992.

Proposed Modification

None (other than modifications to conform to the modifications described in 1., above).

3. Partnership returns on magnetic media (sec. 203 of the bill)

Description of Bill

The bill authorizes the IRS to require large partnerships, and other partnerships with 250 or more partners, to provide the tax return of the partnership and copies of the schedules sent to each partner, to the IRS on magnetic media.

Effective date.--Partnership taxable years ending on or after December 31, 1992.

Proposed Modification

Effective date.--For partnerships that are large partnerships (as defined in the simplified reporting provision), effective for partnership taxable years ending on or after December 31, 1992. For partnerships that are not large partnerships (as defined) but that have 250 or more partners, effective for partnership taxable years ending on or after December 31, 1998.

B. Modification to TEFRA Partnership Proceedings (secs. 211 through 222 of the bill)

Description of Bill

The bill modifies the TEFRA partnership audit proceedings as follows:

1. Treatment of partnership items (sec. 211 of the bill)

The bill clarifies the treatment of partnership items in deficiency proceedings.

Effective date.--The provision is effective for partnership taxable years ending after the date of enactment.

2. Determination of proper audit procedures (sec. 212 of the bill)

The bill permits the IRS to rely on partnership returns to determine the proper audit procedures.

Effective date.--The provision is effective for partnership taxable years ending after the date of enactment.

3. Suspension of statute of limitations for untimely petitions and during bankruptcy proceedings (sec. 213 of the bill)

The bill suspends the statute of limitations for untimely petitions and during bankruptcy proceedings.

Effective date.--The bill shall take effect as if included in the amendments made by section 402 of the Tax Equity and Fiscal Responsibility Act of 1982.

4. TEFRA small partnership exception (sec. 214 of the bill)

The bill expands the small partnership exception from TEFRA.

Effective date.--The bill is effective for partnership taxable years ending after the date of enactment.

5. Exclude partial settlements from 1-year assessment rules (sec. 215 of the bill)

The bill excludes partial settlements from 1-year assessment rules.

Effective date.--The bill is effective for partnership taxable years ending after the date of enactment.

6. Request for administrative adjustments (sec. 216 of the bill)

The bill extends the time for filing a request for administrative adjustment.

Effective date.--The bill is effective as if included in the amendments made by section 402 of the Tax Equity and Fiscal Responsibility Act of 1982.

7. Innocent spouse relief (sec. 217 of the bill)

The bill provides innocent spouse relief for TEFRA proceedings.

Effective date.--The bill is effective as if included in the amendments made by section 402 of the Tax Equity and Fiscal Responsibility Act of 1982.

8. Partnership level penalties (sec. 218 of the bill)

The bill determines penalties at the partnership level.

Effective date.--The bill is effective for partnership taxable years ending after December 31, 1991.

9. Tax Court jurisdiction (sec. 219 of the bill)

The bill clarifies jurisdiction of the Tax Court.

Effective date.--The bill is effective for partnership taxable years ending after the date of enactment.

10. Premature petitions (sec. 220 of the bill)

The bill modifies the treatment of premature petitions filed by certain partners.

Effective date.--The bill is effective with respect to petitions filed after the date of enactment.

11. TEFRA bond requirements (sec. 221 of the bill)

The bill clarifies the bond requirement for appeals from TEFRA proceedings.

Effective date.--The bill is effective as if included in the amendments made by section 402 of the Tax Equity and Fiscal Responsibility Act of 1982.

12. Interest suspension (sec. 222 of the bill)

The bill suspends interest where there is a delay in computational adjustment resulting from TEFRA settlements.

Effective date.--The bill is effective with respect to settlements entered into after December 31, 1991.

Proposed Modification

Change the effective date of (3) to make it prospective; add a new provision to allow the IRS to rely on extensions of the statute of limitations that are signed by a tax matters partner who is bankrupt.

Title III.--Foreign Provisions

1. Deferral of tax on income earned through foreign corporations and exceptions to deferral (secs. 301-304 of the bill and secs. 453, 532, 535, 542, 543, 551-558, 563, 954, 1246-1247, and 1291-1297 of the Code)

Description of Bill

In general

The bill replaces the separate anti-deferral regimes of present law with a unified set of rules providing for either partial or full elimination of deferral depending on the circumstances. The bill preserves the present-law approach under which partial current taxation is a function of the type of income earned by the foreign corporation and a level of U.S. ownership in the corporation exceeding some threshold (as currently embodied in subpart F). The bill also preserves the present-law approach under which full current taxation is a function of a type of income or assets of the corporation exceeding some threshold (as currently embodied in subpart F, the PFIC rules, and the foreign personal holding company rules). In both cases, the bill generally applies current taxation through the operating rules of subpart F. The bill eliminates regimes that are redundant or marginally applicable, and ensures that no more than one set of rules generally will apply to a shareholder's interest in any one corporation in any one year.

Replacement of current law regimes for full elimination of deferral

The bill creates a single definition of a passive foreign corporation (PFC) that will unify and replace the foreign personal holding company and PFIC definitions. The rules applicable to PFCs represent a hybrid of characteristics of the foreign personal holding company rules, the PFIC rules, and the controlled foreign corporation rules (subpart F), plus a new mark-to-market regime, as well as a variety of simplifying or technical changes to rules under the existing systems. The differences between the PFIC provisions of present law and the PFC provisions that will be applicable under the bill are explained below.

A PFC is any foreign corporation if (1) 60 percent or more of its gross income is passive income, (2) 50 percent or more of its assets (on average during the year, measured by value) produce passive income or are held for the production of passive income, or (3) it is registered under the Investment Company Act of 1940 (as amended) either as a management company or as a unit investment trust. As under the PFIC rules, the foreign corporation is permitted to elect to measure its assets based on their adjusted bases rather than their value.

As under present law, passive income for this purpose is defined in the bill generally as any income of a kind which would be foreign personal holding company income as defined in section 954(c), subject to the current law exceptions for banking and insurance income and the current look-through rules for certain payments from related persons (current sec. 1296(b)(2)). In addition, the bill provides two clarifications to present law. First, the bill clarifies that, as indicated in the legislative history of the 1988 Act, the same-country exceptions from the definition of foreign personal holding company income in section 954(c) are disregarded. Second, the bill clarifies that any foreign trade income of a foreign sales corporation does not constitute passive income for purposes of the PFIC definition (cf. sec. 951(e)).

The bill modifies the present-law application of the asset test by treating certain leased property as assets held by the foreign corporation for purposes of the PFC asset test. This rule applies to tangible personal property with respect to which the foreign corporation is the lessee under a lease with a term of at least 12 months.

The bill also modifies the present-law rules that provide an exception from the definition of a PFIC in the case of a company changing businesses. Under the bill, if a foreign corporation holds 25 percent or more of the stock of a second corporation that qualifies for the change-of-business exception (current sec. 1297(b)(3)), then in applying the look-though rules (current sec. 1296(c)), the first corporation may treat otherwise passive assets or income of the second corporation as active.

The bill provides a new election that will allow certain passive foreign corporations to be treated as domestic corporations. A foreign corporation is eligible to make this election if (1) it would qualify for treatment as a regulated investment company (RIC) under the relevant provisions of the Code if it actually were a domestic corporation, (2) it meets such requirements as the Secretary may prescribe to ensure the collection of taxes imposed by the Internal Revenue Code on the passive foreign corporation, and (3) the electing passive foreign corporation waives all benefits which are granted by the United States under any treaty (including treaties other than tax treaties) and to which the corporation is otherwise entitled by reason of being a resident of another country. The rules governing such an election will be similar to those applicable to the election by a foreign insurance company to be treated as a domestic corporation under section 953(d).

The bill provides a special rule regarding the application of the PFC rules to tax-exempt organizations that own stock in passive foreign corporations. The passive foreign corporation rules, under the bill, do not apply to any organization exempt from tax under section 501 unless the organization is subject to unrelated business income taxation on its investment income under section 512(a)(3) of the Code. In the case of a tax-exempt organization that is subject to tax on its investment income, the PFC rules apply with respect to amounts taken into account in computing unrelated business taxable income in the same manner as if the organization were fully taxable.

Tax treatment under full elimination of deferral

The benefits of deferral are eliminated with respect to the income of a PFC under three alternative methods: current inclusion, mark-to-market, or interest charge on excess distributions.

Current inclusion method

Mandatory current inclusion.--If a passive foreign corporation is U.S. controlled, the bill will subject every U.S. person owning (directly or indirectly) stock in the PFC to income inclusions under a modified version of the controlled foreign corporation rules. If a PFC is not U.S. controlled, every U.S. person owning (directly or indirectly) 25 percent or more of the vote or value of the stock of the PFC will be subject to the same rules. Under the bill, the entire gross income of the passive foreign corporation (subject to applicable deductions) is treated as foreign personal holding company income, and thus is included (net of appropriate deductions) on a pro rata basis in the income of each U.S. person directly or indirectly owning stock in the PFC, under a modified application of the rules of sections 951 and 961. Actual distributions of earnings by such a PFC are treated similarly to distributions of previously taxed income under section 959 and 961. These rules supersede all application of the present-law rules applicable to foreign personal holding companies, under which earnings are deemed distributed and then contributed to the capital of the foreign personal holding company.

In applying the subpart F inclusion rules to PFC inclusions, the bill departs from subpart F in that foreign personal holding company income is included in the income of U.S. persons without regard to otherwise applicable reductions pursuant to the high-tax exception (under sec. 954(b)(4)) or the export trade corporation rules (secs. 970 and 971). This modification to the application of the controlled foreign corporation rules preserves present law in that no high-tax exception generally is available to PFICs or foreign personal holding companies, and that the PFIC provisions apply in full force to export trade corporations.

A passive foreign corporation is treated under the bill as U.S. controlled for this purpose either if it would be treated as a controlled foreign corporation under the rules of subpart F, or if, at any time during the taxable year, more than 50 percent of the vote or value of the corporation's stock were owned directly or indirectly by five or fewer U.S. persons (including but not limited to individuals, and including all U.S. citizens regardless of their residence).

Elective current inclusion.--A U.S. person not subject to the above mandatory current inclusion rules--that is, a U.S. person owning less than 25 percent of the stock in a PFC that is not U.S. controlled--may elect application of those rules. As under current law, the PFC is characterized as a "qualified electing fund" with respect to such a U.S. person. In the application of the elective current-inclusion rules, the passive foreign corporation is treated as a controlled foreign corporation with respect to the taxpayer, and the taxpayer is treated as a U.S. shareholder of the corporation. For foreign tax credit purposes, amounts included in the taxpayer's gross income under this modified application of the controlled foreign corporation rules are treated as dividends received from a foreign corporation which is not a controlled foreign corporation.

Mark-to-market method

Less-than-25-percent shareholders of passive foreign corporations that are not U.S.-controlled, and who do not elect current inclusion ("nonelecting shareholders"), are subject under the bill to one of two methods for taxing the economic equivalent of the PFC's current income: the mark-to-market method or the interest-charge method.

Under the bill, nonelecting shareholders of a PFC with marketable stock are required to mark their PFC shares to market annually. Under the mark-to-market method, the U.S. person is required to include in gross income each taxable year an amount equal to the excess (if any) of the fair market value of the PFC stock as of the close of the taxable year over the adjusted basis of the stock. In the event the adjusted basis of the stock exceeds its fair market value, the U.S. person is allowed a deduction for the taxable year equal to the lesser of the amount of the excess or the "unreversed inclusions" with respect to the stock. The bill defines the term "unreversed inclusions" to mean, with respect to any stock in a passive foreign corporation, the excess (if any) of the total amount of mark-to-market gains with respect to the stock included by the taxpayer for prior taxable years, over the amount of mark-to-market losses with respect to such stock that were allowed as deductions for prior taxable years.

The adjusted basis of stock in a passive foreign corporation is increased by the amount of mark-to-market gain included in gross income, and is decreased by the amount of mark-to-market losses allowed as deductions with respect to such stock.

All amounts of mark-to-market gain on PFC stock, as well as gain on the actual sale or distribution of PFC stock, are treated as ordinary income. Similarly, ordinary loss treatment applies to the deductible portion of any mark-to-market loss on PFC stock, as well as to any loss realized on the actual sale or other disposition of PFC stock to the extent that the amount of such loss does not exceed the unreversed inclusions with respect to that stock. These loss deductions are treated as deductions allowable in computing adjusted gross income.

The source of any amount of mark-to-market gain on PFC stock is determined in the same manner as if the amount of income were actual gain from the sale of stock in the passive foreign corporation. Similarly, the source of any amount allowed as a deduction for mark-to-market loss on PFIC stock is determined in the same manner as if that amount were an actual loss incurred on the sale of stock in the passive foreign corporation.

The mark-to-market method under the bill only applies to passive foreign corporations the stock of which is "marketable." PFC stock is treated as marketable if it is regularly traded on a qualified exchange, whether inside or outside the United States. PFC stock is also treated as marketable, to the extent provided in Treasury regulations, if the PFC continuously offers for sale or has outstanding any stock (of which it is the issuer) that is redeemable at its net asset value in a manner comparable to a U.S. regulated investment company (RIC).

In addition, the bill treats as marketable any stock in a passive foreign corporation that is owned by a RIC that continuously offers for sale or has outstanding any stock (of which it is the issuer) that is redeemable at its net asset value. The bill also treats as marketable any stock in a passive foreign corporation that is held by any other RIC, except to the extent provided in regulations.

The bill coordinates the application of the mark-to-market method with the tax rules generally applicable to RICs. The bill treats mark-to-market gain on PFC stock as a dividend for purposes of both the 90-percent investment income test of section 851(b)(2) and the 30-percent short-short limitation of section 851(b)(3).

The mark-to-market method does not apply to the stock of a U.S. person in any PFC that is U.S. controlled (as discussed above), to the stock of a person choosing qualified electing fund treatment, or to stock of a U.S. person who is a 25-percent shareholder (as defined above).

In the case of a controlled foreign corporation (including a passive foreign corporation that is treated under the bill as a controlled foreign corporation) that owns or is treated as owning stock in a passive foreign corporation, the mark-to-market method generally is applied as if the controlled foreign corporation were a U.S. person. For purposes of the application of subpart F to the controlled foreign corporation, mark-to-market gains are treated as if they were foreign personal holding company income of the character of dividends, interest, royalties, rents or annuities, and allowable deductions for mark-to-market losses are treated as deductions allocable to that category of foreign personal holding company income. The source of such income or loss, however, is determined by reference to the actual (foreign) residence of the controlled foreign corporation.

Interest-charge method

Nonelecting shareholders of a PFC with stock that is not marketable are subject to the interest-charge method, based on the PFIC interest-charge method that is currently provided in Code section 1291, with certain modifications.

First, although allowable foreign tax credits may reduce a U.S. person's net U.S. tax liability on an excess distribution, the interest charge computed on that excess distribution is computed, under the bill, without regard to reductions in net U.S. tax liability on account of direct foreign tax credits.

The PFIC provisions of present law, to the extent provided in regulations, impose recognition of gain in the case of a transfer of PFIC stock in a transaction that would otherwise qualify for the nonrecognition provisions of the Code. The bill imposes that result as a general rule, except as otherwise provided in Treasury regulations. In addition, the bill requires that proper adjustment be made to the basis of property, held by the U.S. person, through which the U.S. person is treated as owning stock in the passive foreign corporation.

The PFIC provisions of present law provide special rules for the application of the interest-charge method in the case of PFIC stock held by an U.S. person through an intermediary entity. These rules describe the dispositions that are treated as dispositions of PFIC stock by the U.S. person, and include rules to eliminate the possibility of double taxation (sec. 1297(b)(5)). The bill clarifies that these rules apply to any transaction that results in the U.S. person being treated as no longer owning the PFC stock, as well as any disposition of the PFC stock by the entity actually owning the PFC stock. These rules apply regardless of whether the transaction involves a disposition of the PFC stock, and regardless of whether the parties to the transaction include the U.S. person, the entity actually owning the PFC stock, or some other entity. The bill also clarifies that an income inclusion under the interest-charge method takes precedence over an income inclusion under subpart F resulting from the same disposition.

Under the bill, the interest-charge method applies to any stock in a passive foreign corporation unless either the stock is marketable (and therefore the mark-to-market method applies) as of the time of the distribution or disposition involved, or the stock in the passive foreign corporation was subject to the current inclusion method (under the bill or under prior law) for each taxable year beginning after December 31, 1986 which includes any portion of the taxpayer's holding period in the PFC stock. In the event that PFC stock, not subject to the current inclusion method, becomes marketable during the taxpayer's holding period, the interest-charge method applies to any distributions and dispositions during the year in which the stock becomes marketable, as well as to the mark-to-market gain (if any) as of the close of that year. In the event that PFC stock was initially marketable, and later becomes unmarketable and subject to the interest-charge method, the taxpayer's holding period in the PFC stock for purposes of the interest-charge method is treated as beginning on the first day of the first taxable year beginning after the last taxable year for which the mark-to-market method applies to the taxpayer's stock in the PFC.

The bill also provides for full basis adjustment for partnerships and S corporations that own stock in a passive foreign corporation subject to the interest-charge method. Although tax is imposed on a distribution or disposition under the interest-charge method without including the distribution or disposition in gross income, thus precluding the natural basis adjustments for amounts included in gross income, the bill grants regulatory authority for appropriate basis adjustments to partnerships and S corporations based on the amount of income subject to tax under the interest-charge method and thereby excluded from gross income.

The bill also includes a special rule to coordinate the application of the interest-charge method to nonelecting shareholders of a passive foreign corporation who are or were residents of Puerto Rico. Under the bill, no interest charge is applicable to amounts of an excess distribution that, were the amounts actually earned in the year to which they are treated as earned under the interest-charge method, would have been eligible for the exclusion under section 933 (for income derived by residents of Puerto Rico from sources within Puerto Rico).

Modification or repeal of other antideferral regimes

The bill treats as foreign personal holding company income for subpart F purposes an amount received under a personal service contract if a person other than the corporation has the right to designate (by name or by description) the individual who is to perform the services, or if the individual who is to perform the services is designated (by name or by description) in the contract. The bill similarly treats as foreign personal holding company income for subpart F purposes any amount received from the sale or distribution or disposition of such a contract. This rule applies only if at some time during the taxable year 25 percent or more of the value of the corporation's stock is owned (directly, indirectly, or constructively) by or for the individual who may be designated to perform the services. Income from such personal service contracts is not, however, treated as passive for foreign tax credit purposes.

The bill repeals the foreign personal holding company provisions, the PFIC provisions (except as modified and preserved as the passive foreign corporation provisions), and the foreign investment company provisions. The bill also excludes all foreign corporations from the application of the accumulated earnings tax and the personal holding company tax.

In addition, the bill denies installment sales treatment for any installment obligation arising out of a sale of stock in a passive foreign corporation. This will prevent shareholders in passive foreign corporations from avoiding the interest charge by means of an installment sale of their PFC stock.

Effective date.--The bill generally is effective for taxable years of U.S. persons beginning after December 31, 1991, and taxable years of foreign corporations ending with or within such taxable years of U.S. persons.

The denial of installment sales treatment is effective for sales or dispositions after December 31, 1991.

The bill does not affect the determination of the basis of stock in a PFIC that was acquired from a decedent in a taxable year beginning before January 1, 1991.

Proposed Modifications

a. Mark-to-market attribution rule.--The attribution rule which, for purposes of the mark-to-market method, treats stock owned (directly or indirectly) by or for a foreign partnership or foreign trust or foreign estate as owned proportionately by its partners or beneficiaries, applies except as provided in regulations.

b. Mark-to-market transition rules.--Mark-to-market gain representing appreciation in the value of PFC stock prior to the effective date of the bill is subject to tax under the interest-charge method, and each shareholder may elect to defer the payment of the tax. Subsequent mark-to-market losses may be deducted to the extent of the pre-effective-date appreciation, and an election to defer the payment of tax is terminated to the extent of such deductions taken and to the extent of excess distributions received. In the case of a regulated investment company, in place of applying the interest-charge method to pre-effective-date gain, a separate nondeductible interest charge is added to the company's tax. The mark-to-market method does not apply to appreciation in the value of the PFC stock prior to the time that a shareholder becomes subject to tax in the United States.

c. Fiscal year for regulated investment companies.--Regulated investment companies are permitted to compute their mark-to-market gain on the basis of a fiscal year ending two months before the close of the calendar year, solely for purposes of determining their ordinary income for purposes of the excise tax on the undistributed income of regulated investment companies.

d. Look-through treatment of capital gains.--As under present law, pass through the characterization of capital gains realized by the PFC to those shareholders who are subject to the current-inclusion method and who are not otherwise treated as "U.S. shareholders" of a CFC under subpart F. Unlike present law, make this treatment also available to qualifying shareholders of corporations that would also be foreign personal holding companies under present law.

e. High-tax exception.--As under present law, make the high-tax exception from current inclusion of PFC income available to shareholders who are otherwise treated as "U.S. shareholders" of a CFC under subpart F. Unlike present law, make this treatment also available to qualifying shareholders of corporations that would also be foreign personal holding companies under present law.

f. Character of income.--Clarify that, as under present law, PFC income included under subpart F is treated as base company income rather than foreign personal holding company income, and is eligible for look-through treatment for foreign tax credit limitation purposes, assuming the look-through rule would otherwise apply under present law.

g. Special basis rules applicable to stock in interest-charge PFCs acquired from decedents.--As under present law, apply the rules that deny basis step-up at death only to interest-charge PFCs. Unlike present law, conform to these basis rules the basis rules for stock acquired from a decedent in a corporation that would also be a foreign personal holding company under present law.

h. Nonrecognition override rules.--As under present law, apply the rules that override nonrecognition transactions only to interest-charge PFCs.

i. Attribution rules for pass-through entities.--Apply the bill's rules attributing stock ownership from partnerships, S corporations, estates, and trusts to their partners, shareholders, or beneficiaries except as provided in regulations.

j. Tiered PFCs.--Under regulations, apply the bill's recognition rules for dispositions by, and distributions to, entities through which U.S. persons own PFC stock.

k. Conform treatment of all income from active assets to the treatment of the assets.--Exclude from the definition of passive income for purposes of the definition of a PFC any income derived from assets that are treated as active assets for purposes of the definition of a PFC.

l. Application to tax exempts.--In the case of a tax-exempt organization, clarify that the PFC rules apply to stock held in a PFC only to the extent that a dividend on that stock would be taken into account in determining the unrelated business taxable income of the organization, and only to that extent.

m. Application to residents of U.S. possessions.--The PFC rules apply equally to all U.S. citizens, without regard to their residence. Special tax treatment available to possessions residents is unaffected by the bill.

n. Regulatory authority to prevent avoidance through renunciation of citizenship.--Give regulatory authority to prevent avoidance of interest charge through changes in citizenship, as well as through changes in residence.

o. Installment sale treatment.--The denial of installment sale treatment to dispositions of PFC stock is limited to stock in interest-charge PFCs.

p. Effect of income with respect to CFCs and PFCs on RICs.--Confirm that a RIC's income from a CFC or PFC, derived from the business of investing in stock or securities, counts toward satisfying the RIC's mandatory 90-percent income threshold (sec. 851(b)(2)).

Effective date.--Generally effective for taxable years of U.S. persons beginning after December 31, 1992, and taxable years of foreign corporations ending with or within such taxable years of U.S. persons.

The denial of installment sales treatment is effective for sales or dispositions after December 31, 1992.

The determination of the basis of stock that was acquired from a decedent in a taxable year beginning before January 1, 1992 is not affected.

2. Modifications to provisions affecting controlled foreign corporations (secs. 311 and 313 of the bill)

Description of Bill

a. Characterization of gain on disposition of stock of lower-tier controlled foreign corporations

The bill provides that if a controlled foreign corporation is treated as having gain from the sale or exchange of stock in a foreign corporation, the gain is treated as a dividend to the same extent that it would have been so treated under section 1248 if the controlled foreign corporation were a U.S. person. However, this rule does not affect the determination of whether the second corporation is a controlled foreign corporation.

Gain on disposition of stock in a related corporation created or organized under the laws of, and having substantial part of assets in a trade or business in, the same foreign country as the gain recipient, even if recharacterized as a dividend under the bill, is not therefore excluded from foreign personal holding company income under the same-country exception that applies to actual dividends.

Effective date.--Effective for gains recognized on transactions occurring after date of enactment of the bill.

b. Subpart F inclusions in year of disposition

Where a U.S. shareholder acquires the stock of a controlled foreign corporation from another U.S. shareholder during the middle of a year in which the controlled foreign corporation earns subpart F income, the bill reduces the acquirer's subpart F inclusion for that year by a portion of the amount of the dividend deemed (under sec. 1248) to be received by the transferor. The portion by which the inclusion is reduced would not exceed the subpart F inclusion for that year times the proportion of the year for which the acquirer did not own the stock.

Effective date.--Effective with respect to dispositions occurring after the date of enactment of the bill.

c. Adjustments to basis of stock held by foreign corporations

The bill provides that when a lower-tier controlled foreign corporation earns subpart F income, and stock in that corporation is later sold by an upper-tier controlled foreign corporation, the resulting income inclusion of the U.S. shareholders are, under regulations, adjusted to account for previous inclusions, in a manner similar to the adjustments now provided to the basis of stock in a first-tier controlled foreign corporation.

Effective date.--Effective for adjustments attributable to inclusions for taxable years of U.S. shareholders beginning after December 31, 1991.

d. Avoiding double inclusions in other cases

The bill contemplates that in the case of a cross-chain section 304 dividend out of the earnings of controlled foreign corporations that were previously included in the income of a U.S. shareholder under subpart F, the Treasury Secretary in his discretion may by regulation treat such dividends as distributions of previously taxed income, with appropriate basis adjustments. In addition to cases involving section 304, the bill provides that the Secretary may by regulation modify the application of subpart F in any other case where there would otherwise be a multiple inclusion of any item of income (or an inclusion or exclusion without an appropriate basis adjustment) by reason of the structure of a U.S. shareholder's holdings in controlled foreign corporations or by reason of other circumstances.

Effective date.--Date of enactment of the bill.

e. Treatment of United States income earned by a controlled foreign corporation

The bill provides that an exemption or reduction by treaty of the branch profits tax that would be imposed under section 884 on a controlled foreign corporation does not affect the general statutory exemption from subpart F income that is granted for U.S. source effectively connected income.

Effective date.--Taxable years ending after the date of enactment.

Proposed Modification

a. Characterization of gain on disposition of stock of lower-tier controlled foreign corporations

The proposed modification would repeal the provision added to section 904(d)(2)(E) by the 1988 Act which, except as provided by regulations, requires a recipient of a distribution from a controlled foreign corporation to have been a United States shareholder in that controlled foreign corporation for the period during which the earnings and profits which gave rise to the distribution were generated in order to avoid treating the distribution as one coming from a noncontrolled section 902 corporation.

Effective date.--Effective for distributions after date of enactment.

b. Subpart F inclusions in year of disposition

None.

c. Adjustments to basis of stock held by foreign corporations

None.

Effective date.--Effective for purposes of determining U.S. shareholder inclusions in taxable years of U.S. shareholders beginning after December 31, 1992.

d. Avoiding double inclusions in other cases

None.

e. Treatment of United States income earned by a controlled foreign corporation

None.

Effective date.--Taxable years beginning after December 31, 1986.

3. **Foreign tax credit in year of receipt of previously taxed earnings and profits (sec. 312 of the bill)**

Description of Bill

The bill repeals the rules that permit an indirect foreign tax credit to be claimed with respect to a distribution of previously taxed earnings and profits. Under the bill, foreign taxes paid by a foreign corporation with respect to previously taxed earnings and profits remain in that corporation's pool (or pools) of foreign taxes which are available for the indirect foreign tax credit upon subsequent distributions or deemed distributions of earnings and profits that have not been previously taxed at the U.S. shareholder level.

Effective date.--Generally for taxable years beginning after December 31, 1991. However, the provision is not effective with respect to distributions of previously taxed income which occur in taxable years beginning prior to January 1, 1997, if the distributions relate to subpart F income inclusions for taxable years of the U.S. corporate shareholders beginning before January 1, 1992.

Proposed Modification

The proposed modification would retain the present-law provision that permits an indirect foreign tax credit to be claimed with respect to a distribution of previously taxed earnings and profits. However, it would provide authority for Treasury regulations to establish a simplified method for computing the increase in foreign tax credit limitation that results from the application of that provision.

4. **Translation of foreign taxes into U.S. dollar amounts (section 321 of the bill)**

Description of Bill

The bill grants the Secretary of the Treasury authority to issue regulations that would allow foreign tax payments made by a foreign corporation or by a foreign branch of a U.S. person to be translated into U.S. dollar amounts using an average U.S. dollar exchange rate for a specified period. It is anticipated that the applicable average exchange rate would be the rate as published by a qualified source of exchange rates for the period during which the tax payments were made.

Effective date.--Date of enactment.

Proposed Modification

The proposed modification generally would permit accrual-basis taxpayers to accrue foreign taxes at the average exchange rate for the taxable year to which such taxes relate. If at the close of the second taxable year after the close of the accrual year any tax so accrued has not yet been paid, a redetermination of foreign tax under section 905(c) would be required for the amount of such unpaid tax. That is, the accrual of any tax that is unpaid as of that date would be retroactively denied. In the case of a direct foreign tax credit under section 901, a section 905(c) adjustment for the year of accrual would be required -- generally resulting in the requirement to file an amended tax return for that year. In the case of an indirect foreign tax credit under section 902, an adjustment to the taxpayer's pool of foreign taxes generally would be required.

If tax in excess of the accrued amount (or in excess of the net accrual amount following a section 905(c) adjustment) is actually paid, such excess amount would be translated at the average exchange rate in effect for the year of payment.

Rules similar to those set forth in the bill would apply (1) to tax payments in inflationary currencies, (2) to taxpayers that are not on the accrual basis for determining creditable foreign taxes, or (3) with respect to taxes of an accrual-basis taxpayer that are actually paid in a year prior to the year to which they relate.

Effective date.--Taxes paid or accrued in taxable years beginning after December 31, 1991.

5. Foreign tax credit limitation under the alternative minimum tax (sec. 322 of the bill and sec. 59(a) of the Code)

Description of Bill

For purposes of the alternative minimum tax, the bill permits taxpayers to elect to use as their foreign tax credit limitation fraction the ratio of foreign source regular taxable income to entire alternative minimum taxable income, rather than the ratio of foreign source alternative minimum taxable income to entire alternative minimum taxable income. Foreign source regular taxable income may be used, however, only to the extent it does not exceed entire alternative minimum taxable income.

The election under the bill is available only in the first taxable year beginning after December 31, 1991, for which the taxpayer claims an alternative minimum tax foreign tax credit. The election applies to all subsequent taxable years, and may be revoked only with the permission of the Secretary of the Treasury.

Effective date.--The provision applies to taxable years beginning after December 31, 1991.

Proposed Modification

None.

Effective date.--Taxable years beginning after December 31, 1992.

6. Authority to simplify regulations relating to certain transfers of property involving foreign corporations

Description of Bill

No provision.

Proposed Modification

In inbound cases where nonrecognition treatment must be based on the status of a foreign corporation as a corporation, permit the Secretary to require certain income inclusions without regard to a gain limitation, in cases where anti-abuse rules would otherwise apply. Permit better coordination between inbound and outbound reorganization provisions.

Effective date.--Transfers after December 31, 1993.

7. Simplification of tax on transfers to avoid income tax

Description of Bill

No provision.

Proposed Modification

Outbound transfers now subject to section 1491 would continue to be subject to tax, but the tax would be an income tax, rather than an excise tax, and recognized gain would result in a step-up of basis of the property transferred.

Effective date.--Transfers after date of enactment.

Title IV.--Other Income Tax Provisions

A. Provisions Relating to S Corporations

1. Determination of whether an S corporation has one class of stock (sec. 401 of the bill)

Description of Bill

The bill provides that for purposes of determining whether a corporation meets the subchapter S one-class-of-stock requirement, a corporation is treated as having only one class of stock if all outstanding shares of stock of the corporation confer identical rights to distribution and liquidation proceeds.

Effective date.--Taxable years beginning after December 31, 1982.

2. Authority to validate certain invalid elections (sec. 402 of the bill)

Description of Bill

Under the bill, the authority of the Internal Revenue Service to waive the effect of an inadvertent termination is extended to allow the Service to waive the effect of an invalid election caused by an inadvertent failure to qualify as a small business corporation or to obtain the required shareholder consents.

The bill also allows the Internal Revenue Service to treat a late Subchapter S election as timely where the Service determines that there was reasonable cause for the failure to make the election timely.

Effective date.--Taxable years beginning after December 31, 1982.

3. Treatment of distributions by S corporations during loss year (sec. 403 of the bill)

Description of Proposal

The bill provides that the adjustments for distributions made by an S corporation during a taxable year are taken into account before applying the loss limitation for the year. Thus, distributions during a year reduce the adjusted basis for purposes of determining the allowable loss for the year, but the loss for a year does not reduce the adjusted basis for purposes of determining the tax status of the distributions made during that year.

The bill also provides that in determining the amount in the accumulated adjustment account for purposes of determining the tax treatment of distributions made during a taxable year by an S corporation having accumulated earnings and profits, net negative adjustments (i.e., the excess of losses and deductions over income) for that taxable year are disregarded.

Effective date.--Distributions made in taxable years beginning after December 31, 1991.

4. Treatment of S corporations as shareholders in C corporations (sec. 404(a) of the bill)

Description of Bill

The bill repeals the rule that treats an S corporation in its capacity as a shareholder of another corporation as an individual. Thus, the liquidation of a C corporation into an S corporation will be governed by the generally applicable subchapter C rules, including the provisions of sections 332 and 337 allowing the tax-free liquidation of a corporation into its parent corporation. An S corporation will also be eligible to make a section 338 election (assuming all the requirements are otherwise met), resulting in immediate recognition of all the acquired C corporation's gains and losses (and the resulting imposition of a tax).

Effective date.--Taxable years beginning after December 31, 1991.

5. S corporations permitted to hold subsidiaries (sec. 404(b) of the bill)

Description of Bill

The bill repeals the rule that an S corporation may not be a member of an affiliated group of corporations. Thus, an S corporation will be allowed to own up to 100 percent of the stock of a C corporation. However, an S corporation cannot be included in a group filing a consolidated return.

Effective date.--Taxable years beginning after December 31, 1991.

6. Elimination of pre-1983 earnings and profits of S corporations (sec. 404(c) of the bill)

Description of Bill

The bill provides that if a corporation is an S corporation for its first taxable year beginning after December 31, 1991, the accumulated earnings and profits of the corporation as of the beginning of that year are reduced by the accumulated earnings and profits (if any) accumulated in any taxable year beginning before January 1, 1983, for which the corporation was an electing small business corporation under subchapter S.

Effective date.--Taxable years beginning after December 31, 1991.

7. Determination of shareholder's pro rata share where disposition of entire interest (sec. 404 (d) of the bill)

Description of Bill

Under the bill, the present-law rule, allowing an S corporation to elect to close its books for purposes of determining shares of income on the termination of a shareholder's interest, will be the mandatory rule in the case of the disposition of a shareholder's entire interest in the corporation.

Effective date.--Taxable years beginning after December 31, 1991.

Proposed Modification

Delete the provision from the bill.

8. Treatment of items of income in respect of a decedent held by an S corporation (sec. 404(e) of the bill)

Description of Bill

The bill provides that a person acquiring stock in an S corporation from a decedent will treat as income in respect of a decedent ("IRD") his pro rata share of any item of income of the corporation which would have been IRD if that item had been acquired directly from the decedent. Where a item is treated as IRD, a deduction for the estate tax attributable to the item generally will be allowed under the provisions of section 691(c). The stepped-up basis in the stock will be reduced by the extent to which the value of the stock is attributable to items consisting of IRD. This basis rule is comparable to the present-law partnership rule.

Effective date.--Decedents dying after date of enactment of the bill.

B. Accounting Provisions

1. Modifications to the look-back method for long-term contracts (sec. 411 of the bill)

Description of Bill

Election not to apply the look-back method for de minimis amounts

The bill provides that a taxpayer may elect not to apply the look-back method with respect to a long-term contract if for each prior contract year, the cumulative taxable income (or loss) under the contract as determined using estimated contract price and costs is within 10 percent of the cumulative taxable income (or loss) as determined using actual contract price and costs.

Thus, under the election, upon completion of a long-term contract, a taxpayer would be required to apply the first step of the look-back method (the reallocation of gross income using actual, rather than estimated, contract price and costs), but would not be required to apply the additional steps of the look-back method if the application of the first step resulted in de minimis changes to the amount of income previously taken into account for each prior contract year.

The election applies to all long-term contracts completed during the taxable year for which the election is made and to all long-term contracts completed during subsequent taxable years, unless the election is revoked with the consent of the Secretary of the Treasury.

Election not to reapply the look-back method

The bill provides that a taxpayer may elect not to reapply the look-back method with respect to a contract if, as of the close of any taxable year after the year the contract is completed, the cumulative taxable income (or loss) under the contract is within 10 percent of the cumulative look-back income (or loss) as of the close of the most recent year in which the look-back method was applied (or would have applied but for the other de minimis exception described above). In applying this rule, amounts that are taken into account after completion of the contract are not discounted.

Thus, an electing taxpayer need not apply or reapply the look-back method if amounts that are taken into account after the completion of the contract are de minimis.

The election applies to all long-term contracts completed during the taxable year for which the election is made and to all long-term contracts completed during subsequent taxable years, unless the election is revoked with the consent of the Secretary of the Treasury.

Interest rates used for purposes of the look-back method

The bill provides that for purposes of the look-back method, only one rate of interest is to apply for each accrual period. An accrual period with respect to a taxable year begins on the day after the return due date (determined without regard to extensions) for the taxable year and ends on such return due date for the following taxable year. The applicable rate of interest is the overpayment rate in effect for the calendar quarter in which the accrual period begins.

Effective date.--Contracts completed in taxable years ending after the date of enactment.

2. Simplified method for applying uniform cost capitalization rules (sec. 412 of the bill)

Description of Bill

The bill authorizes (but does not require) the Treasury Department to issue regulations that allow taxpayers in appropriate circumstances to determine the costs of any administrative, service, or support function or department that are allocable to production or resale activities by multiplying the total amount of costs of any such function or department by a fraction, the numerator of which is the amount of costs of the function or department that was allocable to production or resale activities for a base period and the denominator of which is the total amount of costs of the function or department for the base period.

Effective date.--Generally taxable years beginning after the date of enactment of the bill.

C. Minimum Tax Provisions

1. Depreciation under the corporate alternative minimum tax (sec. 421 of the bill)

Description of Bill

The bill applies a 120-percent declining balance method (switching to straight-line at a point maximizing depreciation deductions) for personal property (other than transition property to which the ACRS system in effect before the Tax Reform Act of 1986 applies) for determining the alternative minimum taxable income (AMTI) of a corporation. No further depreciation adjustment for this property would be required for the adjusted current earnings (ACE) component of the corporate alternative minimum tax (AMT).

Corporate taxpayers may elect to use the 120-percent declining balance method of depreciation for regular tax purposes.

Effective Date.--The provision is effective for property placed in service in taxable years beginning after December 31, 1990.

Proposed Modification

Delete provision. (Another item in the Chairman's proposal would provide that no additional adjustment be made for adjusted current earnings for property placed in service on or after February 1, 1992.)

2. Treatment of built-in losses for purposes of the corporate alternative minimum tax (sec. 422 of the bill)

Description of Bill

The bill repeals the ACE rule relating to the treatment of built-in losses after a change of ownership. Thus, for ACE purposes, the treatment of built-in losses would be similar to the treatment of net operating loss carryovers (in the same way that the treatment of built-in losses is similar to the treatment of net operating losses for regular tax purposes).

Effective date.--The provision is effective for changes of ownership occurring after December 31, 1991.

D. Tax-Exempt Bond Provisions

1. Simplification of arbitrage rebate requirement for governmental bonds (sec. 431 of the bill)

Description of Bill

The bill expands an exception to the arbitrage rebate requirement to exempt from rebate certain governmental and qualified 501(c)(3) bonds if at least 95 percent of the bond proceeds are spent within six months after the bonds are issued, and the remainder is spent within one year. Present law requires that no more than the lesser of five percent of $100,000 remain unspent after six months.

Effective date.--The provision applies to bonds issued after the date of the bill's enactment.

2. Simplification of compliance with 24-month arbitrage rebate exception for construction bonds (sec. 432 of the bill)

Description of Bill

The bill exempts earnings on construction bond proceeds invested in bona fide debt service funds from rebate if the spending and penalty requirements of the 24-month exception to the arbitrage rebate requirement for such bonds otherwise are satisfied.

Effective date.--The provision applies to bonds issued after the date of the bill's enactment.

3. Automatic extension of initial temporary period for certain construction bonds (sec. 433 of the bill)

Description of Bill

The bill provides that the initial temporary period for construction bonds is automatically extended for a period of 12 months if at least 85 percent of the available construction proceeds are spent within the original initial temporary period and the issuer reasonably expects to spend the remaining proceeds within the 12-month extension period. Construction bonds eligible for this automatic extension include only those bonds currently eligible for the 24-month rebate exception for construction bonds.

Effective date.--The provision applies to bonds issued after the date of the bill's enactment.

4. Simultaneous issuance of certain discrete issues not aggregated (sec. 434 of the bill)

Description of Bill

The bill allows discrete issues of governmental bonds to be issued simultaneously without being treated as a single issue if one of the issues is a tax and revenue anticipation note that is reasonably expected to be exempt from the arbitrage rebate requirement.

Effective date.--The provision applies to bonds issued after the date of the bill's enactment.

Proposed Modification

Include no inference language with respect to the proper treatment of bonds issued before the date of the bill's enactment.

5. Authority for Treasury Department to exempt certain taxpayers from tax-exempt interest reporting requirement (sec. 435 of the bill)

Description of Bill

The bill authorizes the Internal Revenue Service to provide exceptions from the requirement that taxpayers report interest on State and local government bonds on their Federal income tax returns.

Effective date.--The provision is effective for taxable years beginning after the date of the bill's enactment.

6. Repeal deadwood provisions (sec. 436 of the bill)

Description of Bill

The bill deletes as deadwood two expired exceptions to the arbitrage rebate requirement which applied to certain student loan bonds issued before January 1, 1989.

Effective date.--The provision is effective on and after the date of the bill's enactment.

7. Expansion of exception to pro rata disallowance of bank interest expense related to investment in tax-exempt bonds

Description of Bill

No provision.

Proposed Modification

Financial institutions that invest in tax-exempt bonds are precluded from deducting a pro rata portion of their interest expense determined by reference to the percentage of their assets that consist of such bonds. This pro rata disallowance rule does not apply to governmental bonds issued by entities that issue no more than $10 million of such bonds during a calendar year (the "small issuer exception"). Bond issues in excess of $10 million do not qualify for the small-issuer exception even if the proceeds are re-loaned to issuers borrowing less than $10 million in a calendar year.

The proposed modification would increase the $10 million annual issuance limit to $25 million, and would provide that pooled financing bonds would qualify for the exception if all borrowers from the pool would qualify if borrowing directly from a financial institution, and if certain other requirements were satisfied.

Effective date.--The proposed modification would apply to bonds issued after December 31, 1992.

8. Recharacterize qualified 501(c)(3) bonds and repeal $150 million per-organization limit on certain of these bonds

Description of Bill

No provision.

Proposed Modification

Tax-exempt bonds for use by private, nonprofit organizations ("section 501(c)(3) organizations") are characterized as private activity bonds, and except for qualified hospital bonds, are subject to a per-organization limit of $150 million of bonds that may be outstanding at any time.

The proposed modification would reinstate the pre-1986 characterization of these bonds which treated them as more similar to governmental (rather than private activity) bonds, and would repeal the $150 million limit and made other technical and conforming amendments.

Effective date.--The proposed modification would apply to bonds issued after December 31, 1992.

E. Other Provisions

1. Treatment of Certain Revocable Trusts as Estates (sec. 441 of the bill)

Description of Bill

The bill treats as estates certain grantor trusts receiving the residue of the probate estate under the grantor's will. If no will is admitted to probate, the revocable trust that is primarily responsible for paying taxes, debts and expenses of administration is treated as an estate. The bill applies only to years beginning within three years, nine months of the decedent's death.

Effective date.--Decedents dying after date of enactment.

Proposed Modification

Delete the provision of the bill.

2. Matching rules for payments to partners (sec. 442 of the bill)

Description of Bill

The bill defers the deduction of guaranteed payments by a partnership until the year in which they are includible in the partner's income.

Effective date.--Amounts taken into account after date of enactment.

Proposed Modification

Delete the provision of the bill.

3. Close partnership taxable year with respect to deceased partner (sec. 443 of the bill)

Description of Bill

The bill provides that the taxable year of a partnership closes with respect to a partner whose entire interest in the partnership terminates, whether by death, liquidation or otherwise.

Effective date.--Partnership taxable years beginning after December 31, 1991.

4. Clarification of Amount of Gain Recognized by a Securityholder in a Reorganization, Etc. (sec. 444 of the bill)

Description of Bill

The bill provides that for purposes of determining the amount of gain recognized to a securityholder in a reorganization (or a sec. 355 distribution), the excess of the issue price (as defined in secs. 1273 and 1274) of the securities received over the adjusted issue price of the securities surrendered will be treated as other property. If securities are received and none surrendered, the entire issue price is treated as other property. If the issue price of the securities received does not exceed the adjusted issue price of the securities surrendered, then no amount of the securities is treated as other property.

The adjusted issue price of a security surrendered means the issue price of the security, increased by the OID previously included in the gross income of any holder of the security (determined without to the special rule for subsequent holders), or decreased by the amount of bond premium which would have been allowed as a deduction (or offset) if the bond had always been held by the original holder. Where section 1273(b)(4) applies to a security, the stated redemption price is reduced by the amount of the redemption price which is treated as interest (for example, under sec. 483).

Effective date.--Exchanges and distributions after the date of enactment.

Proposed Modification

Delete the provision from the bill.

Title V.--Estate and Gift Tax Provisions

1. Waiver of right of recovery for certain marital deduction property (sec. 501 of the bill)

Description of Bill

Under the bill, a surviving spouse's estate has a right of recovery with respect to qualified terminable interest property (QTIP) unless the spouse otherwise directs in a provision of the will (or revocable trust) specifically referring to Code section 2207A, which grants such right.

Effective date.--Decedents dying after the date of enactment.

Proposed Modification

Revise the bill to provide that the right of recovery with respect to QTIP is waived by language specifically indicating intent to waive the right, rather than by language specifically referring to section 2207A. Adopt the same rule for waiving the right of contribution with respect to property over which the decedent retained the right to enjoyment or income.

2. Inclusion in gross estate of certain gifts made within three years of death (sec. 502 of the bill)

Description of Bill

The bill provides that a transfer from a revocable trust within three years of death does not result in including the transfer in the gross estate. The bill also revises section 2035 to improve its clarity.

Effective date.--Decedents dying after the date of enactment.

Proposed Modification

Revise the bill to provide that a transfer from a trust over which the grantor held the power to revoke would be treated as if made directly by the grantor (and not includible in the grantor's gross estate).

3. Definition of qualified terminable interest property (sec. 503 of the bill)

Description of Bill

Under the bill, an income interest does not fail to be a qualified income interest, a prerequisite for the marital deduction, solely because income accumulated prior to death is not required to be distributed to the surviving spouse's estate. Such income is included in the surviving spouse's gross estate.

Effective date.--Decedents dying, and gifts made, after date of enactment.

4. Requirements for qualified domestic trust (sec. 504 of the bill)

Description of Bill

A transfer to an noncitizen spouse qualifies for the marital deduction only if made to a qualified domestic trust. The bill provides that, if the governing instrument requires all trustees be U.S. citizens or domestic corporations, the requirement that U.S. trustees have the right to withhold estate tax on distributions shall be waived.

Effective date.--As if included in the Technical and Miscellaneous Revenue Act of 1988 (i.e., decedents dying after November 10, 1988).

5. Election of special use valuation of farm property for estate tax purposes (sec. 505 of the bill)

Description of Bill

The bill allows an estate to use special use valuation if the executor makes an election and submits the required recapture agreement, so long as the executor supplies missing requisite information within a reasonable period of time (not exceeding 90 days) after IRS notification. The bill also allows signatures to be added to the agreement during that time period.

Effective date.--Decedents dying after the date of enactment.

Title VI.--Excise Tax Provisions

A. Motor Fuel Excise Tax Provisions

1. Consolidate provisions imposing diesel and aviation fuel excise taxes (sec. 601 of the bill)

Description of Bill

The bill combines the diesel and aviation fuel tax provisions currently divided between Code sections 4041 and 4091 into a revised section 4091.

Effective date.--The provision is effective for sales or uses on or after January 1, 1992.

Proposed Modification

Delay effective date to sales or uses on or after January 1, 1993.

2. Revision of fuel tax credit and refund procedures (sec. 602 of the bill)

Description of Bill

The bill allows a refund or credit to taxpayers for diesel and aviation fuel sold tax-paid to certain persons who resell for tax-exempt uses. The bill also consolidates the user credit and refund provisions for the fuels excise taxes into one section of the Code. Finally, the bill eliminates the waiver requirement for fuels tax refunds for cropdusters and other fertilizer applicators.

Effective date.--The provision is effective for sales or uses on or after January 1, 1992.

Proposed Modification

Delay effective date to sales or uses on or after January 1, 1993.

3. Authority to provide exceptions from information reporting with respect to diesel fuel and aviation fuel (sec. 603 of the bill)

Description of Bill

The bill permits the IRS by regulation to provide exceptions to the mandatory information return requirement for certain sales or uses of diesel and aviation fuel.

Effective date.--The provision applies to sales or uses on or after January 1, 1992.

Proposed Modification

Delay effective date to sales or uses on or after January 1, 1993.

B. Provisions Relating to Distilled Spirits, Wine, and Beer

1. Refund of tax on certain imported bottled distilled spirits (sec. 611 of the bill)

Description of Bill

Present law provides that when tax-paid distilled spirits which have been withdrawn from bonded premises of a distilled spirits plant are returned for destruction or redistilling, the excise taxes are refunded (sec. 5008(c)), but this provision does not apply to imported bottled distilled spirits, which are withdrawn from customs custody and not from bonded premises. The bill conforms the procedures for refunds of tax collected on imported bottled distilled spirits returned to bonded premises to the rules for domestically produced and imported bulk distilled spirits. Thus, refunds would be available for all distilled spirits on their return to a bonded distilled spirits plant.

Effective date.--The provision is effective beginning 180 days after enactment.

2. Bond for exported distilled spirits (sec. 612 of the bill)

Description of Bill

Bond generally must be furnished to the Department of the Treasury when distilled spirits are removed from bonded premises for exportation without payment of tax. Under present law, these bonds are cancelled or credited when evidence is submitted to the Department of the Treasury that the distilled spirits have been exported (sec. 5175(c)). The bill authorizes the Department of the Treasury to permit records of exportation to be maintained by the exporter, rather than requiring submission to it of proof of exportation in all cases.

Effective date.--The provision is effective beginning 180 days after enactment.

3. Distilled spirits plant records (sec. 613 of the bill)

Description of Bill

Under present law, distilled spirits plant proprietors are required to maintain records of their production, storage, denaturation, and other processing activities on the premises where the operations covered by the records are carried on (sec. 5207(c)). The bill permits distilled plant proprietors to maintain records of their activities at locations other than the premises where the operations covered by the records are carried on (e.g., corporate headquarters), provided that the records are available for inspection by the Treasury Department during business hours.

Effective date.--The provision is effective beginning 180 days after enactment.

4. Transfers from breweries to distilled spirits plants (sec. 614 of the bill)

Description of Bill

Under present law, beer may be transferred without payment of tax from a brewery to a distilled spirits plant to be used in the production of distilled spirits, but only if the brewery is contiguous to the distilled spirits plant (sec. 5222(b)). The bill allows beer to be transferred without payment of tax from a brewery to a distilled spirits plant to be used in the production of distilled spirits, regardless of whether the brewery is contiguous to the distilled spirits plant.

Effective date.--The provision is effective beginning 180 days after enactment.

Proposed Modification

Allow brewers to receive credits/refunds on beer transferred directly from wholesale and retail outlets to distilled spirits plants as well as that transferred from or through brewery premises.

5. Posting of sign by wholesale liquor dealers (sec. 615 of the bill)

Description of Bill

Under present law, wholesale liquor dealers (i.e., dealers, other than wholesale dealers in beer alone, who sell distilled spirits, wine, or beer to other persons who re-sell such products) are required to post a sign conspicuously on the outside of their place of business indicating that they are wholesale liquor dealers (sec. 5115). The bill repeals this requirement.

Effective date.--The provision is effective upon enactment.

6. Refund of tax for wine returned to bond (sec. 616 of the bill)

Description of Bill

Under present law, when unmerchantable wine is returned to bonded production premises, tax that has been paid is refunded or credited to the proprietor of the bonded wine cellar to which the wine is delivered (sec. 5044). In contrast, when beer is returned to a brewery, tax that has been paid is refunded or credited, regardless of whether the beer is unmerchantable (sec. 5056(a)). The bill deletes the requirement that wine returned to bonded premises be "unmerchantable" in order for tax to be refunded or credited to the proprietor of the bonded wine cellar to which the wine is delivered.

Effective date.--The provision is effective beginning 180 days after enactment.

7. Use of ameliorating material in certain wines (sec. 617 of the bill)

Description of Bill

The Code contains rules governing the extent to which ameliorating material (e.g., sugar) may be added to wines made from high acid fruits and the product still be labelled as a standard, natural wine. In general, ameliorating material may not exceed 35 percent of the volume of juice and ameliorating material combined (sec. 5383(b)(1)). However, wines made exclusively from loganberries, currants, or gooseberries are permitted a volume of ameliorating material of up to 60 percent (sec. 5384(b)(2)(D)). The bill modifies the wine labeling restrictions to allow any wine made exclusively from a fruit or berry with a natural fixed acid of 20 parts per thousand or more (before any correction of such fruit or berry) to contain a volume of ameliorating material not in excess of 60 percent.

Effective date.--The provision is effective beginning 180 days after enactment.

8. Domestically produced beer for use by foreign embassies, etc. (sec. 618 of the bill)

Description of Bill

Under present law, domestically produced distilled spirits and wine may be removed from bond, without payment of tax, for transfer to any customs bonded warehouse for storage pending removal for the official or family use of representatives of foreign governments or public international organizations (secs. 5066 and 5362(e)). (A similar rule also applies under present law to imported distilled spirits, wine, and beer.) The bill extends this rule to domestically produced beer.

Effective date.--The provision is effective beginning 180 days after enactment.

9. Withdrawal of beer for destruction (sec. 619 of the bill)

Description of Bill

Present law does not specifically permit beer to be removed from a brewery for destruction without payment of tax. The bill allows beer to be removed from a brewery without payment of tax for purposes of destruction, subject to Treasury Department regulations.

Effective date.--The provision is effective beginning 180 days after enactment.

10. Records of exportation of beer (sec. 620 of the bill)

Description of Bill

Present law provides that a brewer is allowed a refund of tax paid on exported beer upon submission to Department of the Treasury of certain records indicating that the beer has been exported (sec. 5055). The bill repeals the requirement that proof of exportation be submitted to the Treasury Department in all cases as a condition of receiving a refund of tax. This proof will continue to be required to be maintained at the exporter's place of business.

Effective date.--The provision is effective beginning 180 days after enactment.

11. Transfer to brewery of beer imported in bulk (sec. 621 of the bill)

Description of Bill

Under present law, distilled spirits imported into the United States in bulk containers may (under certain circumstances) be transferred from customs custody to bonded premises of a distilled spirits plant without payment of tax (sec. 5232). The bill extends this rule to beer imported into the United States in bulk containers and transferred to a brewery, subject to Treasury Department regulations.

Effective date.--The provision is effective beginning 180 days after enactment.

C. Other Excise Tax Provisions

1. Authority to grant exemptions from registration requirements (sec. 631 of the bill)

Description of Bill

The bill gives the IRS authority to exempt parties to the transfer of articles subject to Federal excise taxes from certain registration requirements.

Effective date.--The provision applies to sales after the 180th day after the date of enactment.

2. Repeal expired reduction in tax on piggyback trailers (sec. 632(a) of the bill)

Description of Bill

Piggyback trailers and semitrailers sold within the 1-year period beginning on July 18, 1984 were permitted a temporary reduction in the retail excise tax on trailers. The bill repeals as "deadwood" the temporary reduction in tax on piggyback trailers.

Effective date.--The provision is effective on the date of enactment.

3. Repeal expired deep seabed minerals excise tax (sec. 632(b) of the bill)

Description of Bill

The bill deletes as deadwood certain expired Code provisions imposing an excise tax on certain minerals mined on the deep seabed. The tax had been imposed in anticipation of a Law of the Sea Treaty which the United States did not sign.

Effective date.--The provision is effective on the date of the bill's enactment.

Title VII -- Administrative Provisions

A. General Administrative Provisions

1. Simplification of employment taxes on domestic services (sec. 701 of the bill)

Description of Bill

The bill changes the threshold for withholding and paying social security taxes from $50 a quarter to $300 a year. The bill requires an individual who employs only household employees to report any social security or Federal unemployment tax obligation for wages paid to such employees on his or her income tax return for the year.

Effective date.--The provision is effective for remuneration paid in calendar years beginning after December 31, 1991.

Proposed Modification

Effective date.--Remuneration paid in calendar years beginning after December 31, 1992.

2. Penalties for failure to provide reports relating to pension payments (sec. 702 of the bill)[1]

Description of Bill

The bill incorporates into the general penalty structure for failure to file information reports the penalties for failure to provide information reports relating to pension payments to the IRS and to recipients.

Effective date.--The bill applies to returns and statements the due date for which is after December 31, 1991.

Proposed Modification

Effective date.--Returns and statements the due date for which is after December 31, 1992.

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[1] This provision is also in section 310 of S. 1364, the Employee Benefits Simplification and Expansion Act of 1991.

3. Use of reproductions of returns stored in digital image format (sec. 703 of the bill)

Description of Bill

The bill provides that the term reproduction includes a reproduction from a digital image.

Effective date.--The provision is effective on the date of enactment.

4. Repeal of requirement to register tax shelters (sec. 704 of the bill)

Description of Bill

The bill repeals the tax shelter registration requirements.

Effective date.--The provision is effective on the date of enactment.

Proposal Modification

Drop provision.

5. Repeal of authority to disclose whether prospective juror has been audited (sec. 705 of the bill)

Description of Bill

The bill repeals the requirement that the Secretary disclose, upon the written request of either party to the lawsuit, whether an individual who is a prospective juror has or has not been the subject of an audit or other tax investigation by the Internal Revenue Service.

Effective date.--The provision is effective for judicial proceedings pending on, or commenced after, the date of enactment.

6. Repeal of special audit provisions for subchapter S items (sec. 706 of the bill)

Description of Bill

The bill repeals the unified audit procedures for S corporations.

Effective date.--The provision is effective for taxable years beginning after the date of enactment.

7. Clarification of statute of limitations (sec. 707 of the bill)

Description of Bill

The bill clarifies that the return that starts the running of the statute of limitations for a taxpayer is the return of the taxpayer and not the return of another person from whom the taxpayer has received an item of income, gain, loss, deduction, or credit.

Effective date.--The provision is effective for taxable years beginning after the date of enactment.

8. Clarification of employment tax status of fishermen

Description of Bill

No provision.

Proposed Modification

The present-law exemption from employment taxes for certain fishermen on boats with a normal operating crew of fewer than 10 individuals would be modified. The operating crew of a boat would be treated as normally made up of fewer than 10 individuals if average size of the operating crew on trips made during the preceding 4 calendar quarters consisted of 10 or fewer individuals. In addition, the exemption would continue to apply if the crew member receives, in addition to the cash remuneration permitted under present law, cash remuneration which does not exceed $100 per trip, is contingent on a minimum catch, and is paid solely for additional duties (e.g., mate, engineer, or cook) for which additional cash remuneration is traditional.

Effective date.--The proposal would generally apply to remuneration paid after December 31, 1991. In addition, the amendments would apply to remuneration paid after December 31, 1984, and before January 1, 1992, unless the payer treated such remuneration when paid as being subject to employment taxes.

B. Tax Court Provisions

1. Overpayment determinations of Tax Court (sec. 711 of the bill)

Description of Bill

The bill clarifies that an order to refund an overpayment is appealable in the same manner as a decision of the Tax Court.

Effective date.--The provision is effective on the date of enactment.

2. Awarding of administrative costs (sec. 712 of the bill)

Description of Bill

The bill provides that a taxpayer who seeks an award of administrative costs must apply for such costs within 90 days of the date on which the taxpayer was determined to be a prevailing party. The bill also provides that a taxpayer who seeks to appeal an IRS denial of an administrative cost award must petition the Tax Court within 90 days after the date that the IRS mails the denial notice.

Effective date.--The provision is effective on the date of enactment.

3. Redetermination of interest pursuant to motion (sec. 713 of the bill)

Description of Bill

The bill provides that a taxpayer must file a "motion" (rather than a "petition") to seek a redetermination of interest in the Tax Court.

Effective date.--The provision is effective on the date of enactment.

4. Application of net worth requirement for awards of litigation costs (sec. 714 of the bill)

Description of Bill

The bill provides that the net worth limitations currently applicable to individuals also apply to estates and trusts for purposes of awards of litigation costs. The bill also provides that individuals who file a joint tax return shall be treated as one individual for purposes of computing the net worth limitations.

Effective date.--The provision applies to proceedings commenced after the date of enactment.

C. Cooperative Agreements with State Tax Authorities (sec. 721 of the bill)

Description of Bill

The bill authorizes the Secretary to enter into cooperative agreements with State tax authorities to enhance joint tax administration. These agreements may include (1) joint filing of Federal and State income tax returns, (2) single processing of these returns, and (3) joint collection of taxes (other than Federal income taxes).

Effective date.--This provision is effective on the date of enactment.

Title VIII--Additional Provisions

1. Income taxation of accumulation trusts

Description of Bill

No provision.

Proposed Modification

Exempt amounts accumulated in domestic trusts after December 31, 1992, from the so-called "throwback rule," under which distributions of accumulated income to the beneficiaries are thrown back to the year in which the income would have been taxed to the beneficiary if it had been distributed currently. Also provide that precontribution gain on property sold by a domestic trust is no longer taxed at the contributor's marginal tax rates. These modifications would not apply to any trust created before March 1, 1984, unless the taxpayer establishes that the trust would not have been aggregated under the standard contained in section 643(f).

Effective date.--Taxable years beginning after December 31, 1992.

2. Include fractional share of property qualifying for the marital deduction in the gross estate

Description of Bill

No provision.

Proposed Modification

To qualify for the marital deduction under present law, a trust generally must grant the surviving spouse an income interest in, or a power of appointment over, a specified portion of property. The modification would require that the specified portion be expressed as a fraction or percentage of trust property.

Effective date.--Gifts made, and decedents dying, after date of enactment. The bill exempts a transfer under a will or revocable trust executed before the date of enactment if either (1) on that date the decedent was under a mental disability to change the disposition of his property and did not regain his competence to dispose of such property before the date of death, or (2) the decedent dies within three years after the date of enactment. The exemption does not apply if the will or trust is amended after the date of enactment in any respect that increases the amount of the transfer or alters the terms by which the interest passes.

3. Simplify payroll tax deposit requirements

Description of Bill

No provision.

Proposed Modification

In general

The proposal would replace the entire payroll tax deposit system. In general, the new system would consist of three basic deposit timetables. The first, which would be most generally applicable (and would replace the eighth-monthly system), would require deposits twice a week, on Tuesdays and Fridays. The second, which would apply to large depositors, would retain the requirement of present law that cumulations of an amount to be deposited of $100,000 or more must be deposited on the next day. The third, which would apply to many small depositors, would provide generally that if the amount required to be deposited was $12,000 or less per quarter for a previous one-year base period, deposits must be made only once a month, on or before the fifteenth day of the following month.

Tuesday, Friday deposit rule

The Tuesday/Friday rule would operate in the following manner. Amounts attributable to wage payments made on Wednesday, Thursday, or Friday would be required to be deposited on or before the following Tuesday. Amounts attributable to wage payments made on Saturday, Sunday, Monday, or Tuesday would be required to be deposited on or before the following Friday.

Small depositor rules

The small depositor rules would operate as follows. If an employer is a small depositor, deposits of employment taxes attributable to wage payments during a month must be made on or before the fifteenth day of the following month.

A person would be a small depositor for a calendar quarter if, for each calendar quarter in the base period, the amount of employment taxes attributable to payments in each of those calendar quarters was $12,000 or less. The base period would be defined to be the four calendar quarters ending with the second preceding calendar quarter before the quarter with respect to which the deposit requirements were being determined. The only exception to this would be that the $100,000 rule would apply to all depositors, including small depositors.

New companies would initially be treated as small depositors. For purposes of performing the base period determination, a company would be considered to have employment taxes of zero for any calendar quarter in which a company did not exist. Consequently, new companies would, for at least the first two calendar quarters of their existence, be required to deposit only once a month (unless they fall within the $100,000 rule).

Safe harbor

The proposal would provide a statutory safe harbor with respect to certain shortfalls in deposits. An employer would be treated as having deposited the required amount of employment taxes in any deposit if the shortfall did not exceed the greater of $100 or two percent of the amount of employment taxes otherwise required to be deposited. A shortfall would be the excess of the amount required to be deposited (without regard to this rule) over the amount actually deposited on or before the last day on which that deposit is required. Any shortfall would be required to be deposited as required by Treasury regulations.

Definitions and other rules

The proposal would provide that deposits are required only on banking days. If a deposit would be required to be made on or before a day that is not a banking day, the deposit would be considered to have been made on a timely basis if made on or before the close of the next banking day.

Effective date.--The proposal would be effective for amounts attributable to payments made after December 31, 1992.

4. Firearms Excise Tax Exemption for Custom Gunsmiths

Description of Bill

No provision.

Proposed Modification

The proposal would exempt small manufacturers and importers from the present-law 11-percent excise tax on firearms (rifles and shotguns) and ammunition and the present-law 10-percent tax on pistols and revolvers, if such manufacturer or importer manufactures or imports less than 50 such articles per year.

Effective date.--The proposal would be effective for articles sold after September 30, 1983. In the case of any taxable year ending before the date of enactment, the period for claiming a credit or refund of any overpayment of tax resulting from the proposed exemption from tax shall not expire before one year after the date of enactment.

5. Discharge of Indebtedness Income from Prepayment of REA Loans at a Discount

Description of Bill

No provision.

Proposed Modification

Under Code section 501(c)12), a rural electric cooperative is exempt from tax if at least 85 percent of its income is derived from its members. In two prior technical corrections, Congress has provided that the 85-percent test would be determined without regard to discharge of indebtedness income arising from the prepayment at a discount of loans made by the Rural Electrification Administration pursuant to the provisions of the 1988 and 1989 Budget Reconciliation Acts. The proposed amendment would extend that treatment to certain prepayment of REA loans provided by the 1990 Farm Act.

6. Private Foundation Common Investment Fund

Description of Bill

No provision.

Proposed Modification

Section 501(c)(3) requires that an organization be organized and operated exclusively for an exempt purpose in order to qualify for tax-exempt status under that section. Section 501(f) provides that an organization is treated as organized and operated exclusively for charitable purposes if it is comprised solely of members that are educational institutions and is organized and operated solely to collectively invest in stocks and securities on behalf of the members.

The proposed modification would provide that a cooperative service organization comprised solely of members that are tax-exempt private foundations and community foundations shall be treated as organized and operated exclusively for charitable purposes if: (1) it has at least 20 members; (2) no one member holds (after the organization's second taxable year) more than 10 percent (by value) of the interests in the organization; (3) no one member controls the organization or any other member; (4) the members are permitted to dismiss any of the organization's investment advisors upon a vote of members holding a majority of interest in the account managed by such advisor; (5) the organization is organized and operated solely to collectively invest in stocks and securities.

A cooperative service organization meeting the criteria of the proposed modification would be subject to the present-law excise tax provisions applicable to private foundations, other than sections 4940 and 4942. For purposes of section 4940, the proportionate share (whether or not distributed) for each member of the net income of the organization would be flowed through to the member.

Effective date.--The proposed modification would apply to taxable years beginning after December 31, 1991.

7. **Treatment of Nuclear Decommissioning Funds**

Description of Bill

No provision.

Proposed Modification

The present-law investment restrictions applicable to nuclear decommissioning funds would be repealed.

Effective date.--The proposal would apply to taxable years beginning after December 31, 1991.

8. Taxable Year Election for Partnerships, S Corporations, and Personal Service Corporations

Description of Bill

No provision.

Proposed Modification

A partnership, S corporation, or personal service corporation would be allowed to elect any taxable year without regard to the length of the deferral period of the taxable year elected if the annual financial statements (if any) of the entity used for credit purposes or provided to the partners, shareholders, or other proprietors of the entity cover the same period as the taxable year elected.

The proposal would increase the amount of the required payment that must be made by a partnership or S corporation that elects a taxable year other than the required taxable year (including any partnership or S corporation that has an election in effect on the date of enactment of the bill).[1] In addition, the proposal would require an additional payment for any taxable year that a partnership or S corporation first makes a taxable year election or changes a taxable year election to increase the deferral period.

The proposal would also modify the minimum distribution requirement that must be satisfied by a personal service corporation that elects a taxable year other than the required taxable year (including a personal service corporation that has an election in effect on the date of enactment of the bill).

Effective date.--The proposal would apply to taxable years beginning after December 31, 1991.

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[1] The required payment would be determined by using the highest rate of tax in effect under section 1 of the Code plus 2 percentage points.

9. **Treatment of amounts received by telephone cooperatives**

Description of Bill

No provision.

Proposed Modification

Mutual or cooperative telephone companies ("telephone cooperatives") are exempt from Federal income tax if 85 percent or more of their income consists of amounts collected from members for the sole purpose of meeting losses and expenses (sec. 501(c)(12)(A)). In applying this 85-percent test, certain income received by a telephone cooperative is disregarded, including income received from a nonmember telephone company for the performance of communication services which involve members of the telephone cooperative, certain pole rental income, and income from the sale of display listings in a telephone directory sold to members of the telephone cooperative (sec. 501(c)(12)(B)).

The proposal would amend section 501(c)(12) to provide that a 50 percent of the income received by a telephone cooperative from a nonmember telephone company (e.g., fees received for originating a long-distance call placed by a member) would be treated as collected from members of the telephone cooperative. The remaining 50 percent of income received by a telephone cooperative from a nonmember telephone company would, as under present law, be excluded from the 85-percent test under section 501(c)(12)(B)(i).

The proposal also would exclude from the 85-percent test under section 501(c)(12) amounts received by a telephone cooperative from billing and collection services performed for another telephone company (e.g., a long-distance carrier).

In addition, the proposal would provide that tax-exempt telephone cooperatives would be permitted to earn certain investment income in excess of 15 percent of their total income (but not in excess of 35 percent of total income) without losing their tax-exempt status. Tax-exempt telephone cooperatives would be subject to the unrelated business income tax (UBIT) on such investment income between the 15-percent and 35-percent range.

Effective date.--The proposal would be effective for taxable years beginning before, on, or after the date of enactment.

10. Modifications to the Reforestation Trust Fund

Description of Bill

No provision.

Proposed Modification

The maximum amount that may be transferred to the Reforestation Trust Fund for any fiscal year would be increased from $30 million to $45 million. The additional $15 million that is transferred to the Reforestation Trust Fund for any fiscal year would be available to the Department of the Interior for the reforestation and forest conservation activities of the Bureau of Land Management in any State and related administrative costs. To the extent that the wood product tariffs are insufficient to provide an additional $15 million for any fiscal year, the Treasury Department would be required to transfer to the Reforestation Trust Fund an amount equal to the Federal portion of the receipts from the sale of certain timber located on Federal land.

Effective date.--The proposal would be effective on October 1, 1992.

11. Determinations of gas produced from qualifying sources under the nonconventional fuels production credit

Description of Bill

No provision.

Proposed Modification

With respect to determinations required under the Internal Revenue Code of whether gas is produced from geopressured brine, Devonian shale, coal seams, or from a tight formation, in the event that such a determination is not made by the Federal Energy Regulatory Commission in accordance with section 503 of the Natural Gas Policy Act of 1978 due to the expiration of that statute through enactment of the Natural Gas Wellhead Decontrol Act of 1989,[1] the proposed modification would require the Secretary of Treasury to make such a determination. For this purpose, the proposal would mandate that any such determination by the Treasury Department be made using the guidelines set forth in section 503 of the Natural Gas Policy Act of 1978 prior to its repeal.

In addition, the proposed modification would clarify that for purposes of the nonconventional fuels production credit, the definitions of gas produced from geopressured brine, Devonian shale, coal seams, or from a tight formation would be as established by the Federal Energy Regulatory Commission under the Natural Gas Policy Act of 1978 prior to repeal of provisions of that statute relating to such definitions.

Effective date.--With respect to well and formation determinations required to be made by the Treasury Department, the proposed modification would be effective for determinations with respect to which no such determination is made by the Federal Energy Regulatory Commission as a result of the repeal of section 503 of the Natural Gas Policy Act of 1978. The proposed modification clarifying the definitions of certain qualifying fuels would be effective after December 31, 1992.

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[1] P.L. 101-60; 103 Stat. 157 (1989).

12. Treatment of housing cooperatives

Present Law

Unlike other corporations, a cooperative association is not taxable on income from patronage sources.

A membership organization operated primarily to furnish services or goods to its members may deduct costs attributable to furnishing services or goods to its members only to the extent of income derived from the members (sec. 277).

Explanation of Proposal

The proposal provides that section 277 would not apply to a cooperative housing corporation and that patronage losses of such a corporation could not offset earnings that are not patronage earnings.

Patronage earnings and losses would generally include earnings and losses derived from business done with or for patrons of the corporation. In addition, the proposal would treat as patronage sourced: (1) interest on reasonable reserves established in connection with the corporation, (2) income from laundry and parking attributable to tenants-stockholders and their guests, and (3) (in the case of a limited equity cooperative housing corporation) rental income attributable to a housing project operated by the corporation.

Effective Date

The proposal applies to taxable years beginning after date of enactment.

Joint Committee on Taxation
March 3, 1992
JCX-9-92

- Senate Finance Committee -

ESTIMATED REVENUE EFFECTS OF CHAIRMAN'S MARK

Fiscal Years 1992-1996

[Billions of Dollars]

Item	Effective	1992	1993	1994	1995	1996	1992-96
PROVIDE FAIR TREATMENT OF WORKING FAMILIES							
1. Provide $300 tax credit for dependents under 16 years; phased out for AGI between $50,000-$70,000	1/1/92	-0.8	-8.2	-7.6	-7.5	-7.2	-31.4
2. Earned income tax credit (EITC):							
a. Repeal young child credit	1/1/92	(1)	0.3	0.3	0.3	0.3	1.1
b. EITC expansion and simplification	1/1/92	(2)	-0.5	-0.5	-0.5	-0.5	-2.1
3. Extend targeted jobs tax credit (18 months)	7/1/92	(2)	-0.1	-0.2	-0.1	(2)	-0.5
PROMOTE LONG-TERM ECONOMIC GROWTH THROUGH:							
1. Increased savings - Restoration of the fully-deductible IRAs and creation of Special IRAs	(3)	(2)	1.9	-1.1	-1.9	-3.9	-5.0
2. Improved educational opportunities:							
a. Self-reliance loans (4)	--	(2)	-0.1	-0.1	-0.1	-0.1	-0.2
b. Permit deduction/credit for student loan interest	1/1/92	(2)	-0.1	-0.2	-0.2	-0.2	-0.7
c. Youth training program (LEAP)	2/1/92	(2)	(2)	(2)	-0.1	-0.1	-0.2
d. Penalty-free IRA withdrawals for education (includes interaction with withdrawals for first-time homebuyers)	1/1/92	-0.1	-0.1	-0.1	-0.1	-0.1	-0.6
e. Extend employer-provided educational assistance (18 months)	7/1/92	-0.1	-0.2	-0.2	--	--	-0.5
f. Expand exclusion for education savings bonds	1/1/92	(2)	(2)	(2)	(2)	(2)	(2)
g. Extend access to tax information by the Department of Veterans Affairs (9/30/98) (4)	--	--	(1)	0.1	0.1	0.1	0.2
3. Better access to affordable health care:							
a. Extend 100% deduction for health insurance premiums of self-employed (25% in 1992; 100% in 1993 and 1994)	7/1/92	-0.1	-0.6	-1.7	-1.2	--	-3.6

Item	Effective	1992	1993	1994	1995	1996	1992-96
b. Adopt small-employer health insurance market reforms; eliminate loss of health insurance resulting from pre-existing condition exclusions	(5)	(6)	(6)	(6)	(6)	(6)	(6)
c. Medicare prevention benefits (4)	1/1/93	--	-0.1	-0.1	-0.1	-0.1	-0.3
d. Penalty-free IRA withdrawals for serious medical expenses	1/1/92	(2)	(2)	(2)	(2)	(2)	(2)
e. Increase excise tax on ozone-depleting chemicals (7)	7/1/92	(1)	0.1	0.5	0.7	0.1	1.4
f. Extend orphan drug tax credit (18 months)	7/1/92	(2)	(2)	(2)	--	--	(2)
4. Investment in real estate:							
a. Penalty-free IRA withdrawals for first-home purchase (8)	1/1/92	-0.2	-0.4	-0.4	-0.3	-0.2	-1.7
b. UBIT changes to promote increased pension investment in real estate (8)	1/1/92	--	-0.1	-0.1	-0.1	-0.1	-0.4
c. $5,000 credit for first-home purchase (through 12/31/93, new homes only) (8)	2/1/92	-0.1	-0.7	-0.6	-0.1	(2)	-1.5
d. Allow passive losses for active real estate developers (existing properties) (8)	1/1/92	-0.1	-0.4	-0.4	-0.4	-0.5	-1.9
e. Extend depreciation period for nonresidential real estate from 31.5 to 40 years	2/12/92	(1)	0.1	0.3	0.6	0.9	1.9
f. Extend and modify low-income housing tax credit (18 months)	7/1/92	(2)	-0.1	-0.2	-0.3	-0.3	-0.9
g. Extend mortgage revenue bonds and mortgage credit certificates (18 months)	7/1/92	(2)	(2)	-0.1	-0.1	-0.1	-0.3
5. Other incentives to promote long-term investment and improve competitiveness:							
a. 10% investment tax allowance (through 12/31/92) (8)	2/1/92	-4.3	-2.4	1.8	1.3	0.9	-2.7
b. Alternative minimum tax relief:							
(1.) Gifts of appreciated property to charitable organizations (18 months)	7/1/92	(2)	(2)	-0.1	(1)	(2)	-0.1
(2.) Modify treatment of IDCs in minimum tax	tyba 12/31/91	-0.1	-0.2	-0.2	-0.2	-0.1	-0.8
(3.) Repeal ACE depreciation adjustment (8)	2/1/92	-0.2	-0.3	-0.3	-0.3	-0.2	-1.4
c. Extend research and experimentation tax credit (18 months)	7/1/92	-0.2	-0.8	-0.5	-0.1	-0.1	-1.7
d. Progressive capital gains relief; 2-year holding period; depreciation recapture at 31%; and 50% exclusion for gains from venture capital investments (8)	D/o/E	-0.1	-1.3	-3.2	-2.1	-0.9	-7.7
e. Extend small-issue bonds (18 months)	7/1/92	(2)	(2)	-0.1	-0.1	-0.1	-0.3
f. Extend business energy credits (solar and geothermal) (18 months)	7/1/92	(2)	(2)	(2)	(2)	(2)	-0.1
g. Modify import category for certain vehicles (4)	4/1/92	0.1	0.2	0.2	0.2	0.2	1.0
h. Cap deduction for regular tax and AMT purposes for executive compensation at $1 million	1/1/92	0.1	0.3	0.4	0.4	0.4	1.5

Item	Effective	1992	1993	1994	1995	1996	1992-96
i. Expand exclusion for transit passes to $60 per month; extend exclusion to vanpooling and park-and-ride benefits; limit exclusion for employer-provided parking to $160 per month	(9)	(1)	(1)	(1)	(2)	(2)	(2)
j. Repeal luxury tax on boats, airplanes, jewelry, and furs; index threshold for automobiles; and impose diesel excise tax on motor boats	(10)	(2)	(2)	-0.1	-0.1	-0.1	-0.3
k. Extension of other expiring provisions (11)	--	--	--	--	--	--	---
6. Simplification of the Internal Revenue Code	--	0.4	(2)	-0.6	-0.6	0.3	-0.5
7. Taxpayer Bill of Rights	(12)	(2)	-0.1	-0.1	-0.1	-0.1	-0.4
SUBTOTALS		**-6.0**	**-14.4**	**-15.2**	**-13.1**	**-11.8**	**-60.5**
CBO Revenue Surplus		**3.0**					**3.5**
TOTALS: Fairness and Long-Term Economic Growth		**-3.0**	**-14.4**	**-15.2**	**-13.1**	**-11.8**	**-57.0**
PROPOSALS TO ENSURE HIGH-INCOME TAXPAYERS PAY THEIR FAIR SHARE							
1. Add fourth individual rate bracket of 36% beginning at taxable income of $150,000 (single), $175,000 (joint), and $162,500 (head of household)	tyba 12/31/91	3.4	10.2	9.5	10.0	9.9	43.0
2. Impose 10% surtax on tax attributable to taxable income in excess of $1 million	tyba 12/31/91	0.6	1.9	1.9	2.0	2.1	8.5
3. Extend permanently the personal exemption phaseout and the itemized deduction limitation	tyba 12/31/95	--	--	--	--	3.7	3.7
4. Conform book and tax accounting for securities inventories	tyeo/a 12/31/93	--	0.1	0.4	0.5	0.5	1.5
5. Make corporate and individual estimated tax changes permanent	--	--	--	--	--	--	---
6. Extend 45-day processing rule to all taxes and refunds (4)	7/1/92	--	0.1	0.1	0.1	0.1	0.2
SUBTOTALS		**4.1**	**12.3**	**11.8**	**12.6**	**16.3**	**57.0**
GRAND TOTALS		**1.1**	**-2.1**	**-3.4**	**-0.5**	**4.5**	**0.0**

Joint Committee on Taxation

NOTES: Details may not add to totals due to rounding.

[Legend and Footnotes appear on the following page.]

Item	Effective	1992	1993	1994	1995	1996	1992-96

Legend and Footnotes for JCX-8-92:

Legend for Effective column: D/o/E = Date of enactment
tyba = taxable years beginning after
tyeo/a = taxable years ending on or after

(1) Gain of less than $50 million.
(2) Loss of less than $50 million.
(3) Generally effective 1/1/93; provision for transfers to special IRAs effective 1/1/92.
(4) Estimate for this provision provided by the Congressional Budget Office (CBO).
(5) Effective dates: Small market reform = plans offered, issued, or renewed on or after 1/1/94; pre-existing conditions = plan years beginning after 12/31/92.
(6) Gain or loss of less than $50 million.
(7) Tax is $1.85 in 1992 (effective 7/1/92), $2.75 in 1993, $3.65 in 1994, $4.55 in 1995, and (as scheduled under present law) increased by $0.45 per year thereafter.
(8) A similar or related proposal was included in the President's 7-point plan.
(9) Effective dates: Transit passes = 1/1/92; Parking cap = D/o/E.
(10) Net of income tax offsets. Effective dates: Luxury tax = 1/1/92; Diesel tax = 7/1/92.
(11) Other expiring provisions to be extended: excise tax on certain vaccines for the Vaccine Injury Compensation Fund for two years and Railroad Retirement Tier II transfers. (NOTE: Extension of the vaccine excise taxes is assumed in the CBO baseline; therefore, an extension of the Vaccine Injury Compensation Fund has no revenue effect.)
(12) Effective dates: For sections 201, 204, 501, 703, 704, 802, 803, and 902 = date of enactment; for sections 202 and 401 = six months after the date of enactment; for sections 303, 502, and 905 = taxable years beginning after 12/31/92.

<u>FICA TIP CREDIT WITH CLUB DUES OFFSET</u>

* Since 1988, employers in industries with tip income have been required to treat all employee tip income as employer-provided wages for FICA tax purposes.

* This is despite the fact that employers do not control tips, cannot plan for them, and are <u>prohibited</u> from considering most tips as wages elsewhere under federal law (i.e., the tip credit provisions of the Fair Labor Standards Act).

* This federal double-standard towards tip income is confusing and costly to hundreds of thousands of small businesses. It is a mistake we must correct.

* I have introduced S.765 which would repeal this Reagan Administration budget proposal outright. S.765 has been cosponsored by 46 Senators, including a majority of the members of this Committee.

* Recognizing the concerns of some members about any proposal -- no matter how sensible -- which serves to reduce the flow of revenues into the Social Security Trust Fund, I offer today a compromise measure which fully protects the Social Security Trust Fund while addressing the fundamental financial inequity highlighted in S.765.

* My amendment would create a new income tax credit for employers for certain FICA taxes paid on employee tip income.

* Under this amendment, employers would continue to pay FICA taxes on all employee tip income throughout the year. At year's end, they would calculate the amount of FICA taxes they paid on tips which could not be considered wages under the Fair Labor Standards Act. They would receive a tax credit for this amount.

* Example -- Under current law, a waitress earns and reports $8.00 per hour in tips. The employer is allowed to consider up to $2.12 per hour in tips as wages. The employer pays a cash wage of $2.13 per hour and takes a tip credit of $2.12 per hour to ensure the $4.25 minimum wage obligation is fulfilled. The waitress's total income is $10.13 per hour. Despite the fact that only $2.12 per hour in tips are allowed here as wages, the employer pays FICA on all tips. His tax liability on that employee is 77 cents per hour ($10.13 x 7.65%). Under my proposal, the employer's tax credit would be equal to the amount of FICA he must pay on tips above $2.12 per hour. In this example, his credit would be 45 cents per hour for this employee. This financial relief equalizes the tipped employer's payroll tax liability with that of other industries -- taxes are owed only on wages under the control of the employer. The FICA funds remain protected.

* Reducing the cost of labor will help create jobs. According to the Employment Policies Institute, my bill would create more than 39,000 new jobs and would be a "cost-effective job creation program to deal with the current recession."

* The debate surrounding this tax bill has centered on tax fairness, job creation, and economic growth. This proposal contains all three, and I urge its adoption.

Elimination of Business Deduction for Club Dues

* While regular working people cannot deduct membership dues for local health fitness clubs or other clubs that offer cultural, educational, athletic or entertainment value, their corporate counterparts and businessmen are able to reduce their taxes by deducting dues paid to posh clubs.

* Current law enables a limited class of high income people to entertain themselves and their friends under the cloak of "business" while wage earners, journeymen, and other middle income people, are not able to put on such airs and get a tax break.

* In times like these, we cannot afford to subsidize executives who get to use such clubs, while middle and low income families are able to participate only with their own hard earned after-tax dollars, if at all.

* Because membership dues have been deductible, the price of joining has been artificially elevated. Corporate money has bid up the cost of belonging. This has made it even more difficult for the average person who is not in a position to write it off to be able to join a club in which he or she seeks membership. By removing the deduction, executives would be less inclined to spend shareholders' dollars on multiple high-priced club memberships. They would be more choosy about which and how many clubs they would join. This would stop the price escalation and leave more room for greater middle class anticipation.

* Let us be clear, this measure does not interrupt the existing deduction for fees connected to each use of club owned facilities. Thus, for example, if a salesman were to take three customers golfing with him to get a chance to tell them about a new product line, then so long as the business purpose of the event is established, the green fees for that round of golf would still be deductible. It is just the underlying memberships dues that would not be.

* While the way I wish to invest this recovered revenue loss will clearly create tens of thousands of jobs, I do not believe that this amendment will cost jobs. In fact, I think it could increase employment among clubs. When the XYZ Corporation buys membership in four golf clubs, for example, that does not produce a recurring employment opportunity for greens keepers, caddies, etc. It is the actual use or the rounds of golf that do that. Under current law, many who would like to belong to the club and play the club on a regular basis are frozen out by the high membership fee which was bid up by the all the XYZ Corporations. By removing the tax subsidy of membership dues for the privileged few, we will increase access to the club for the average person. It is their use, their rounds of golf, for example, who will create the need for more employees at the clubs.

* The way this amendment is structured recognizes that legitimate business is often conducted in connection with the utilization of clubs since it leaves intact the case by case deduction for each use. But it also recognizes that merely belonging to a club does not prove a business purpose.

* Furthermore, in offering this amendment, we are recognizing that only the privileged few are in a position to try to broadly claim a business purpose deduction for membership dues, while the existing deduction for specific use is open to anyone who can show that each expenditure was, in fact, in pursuit of a business purpose.

Congress of the United States

JOINT COMMITTEE ON TAXATION
1015 LONGWORTH HOUSE OFFICE BUILDING
WASHINGTON, DC 20515-6453
(202) 225-3621

Honorable John B. Breaux
United States Senate
Washington, DC 20510

Dear Senator Breaux:

This letter is in response to your request dated February 28, 1992, for an estimate of the revenue effects of a two-part proposal.

The first part of the proposal would provide employers with a Federal income tax credit in an amount equal to the FICA tax obligation they pay on cash tips paid each year. The credit would apply to that portion of tip income that is in excess of the amounts that are considered wages for purposes of minimum wage requirements.

The second part of the proposal would deny the deductibility from taxable income of club dues paid to social, athletic, luncheon, and sporting clubs.

The following estimate assumes that these proposals would become effective upon enactment (assumed to be April 1, 1992).

	Fiscal Years [Billions of Dollars]						
Item	1992	1993	1994	1995	1996	1997	1992-97
Credit for tips.......	-0.1	-0.3	-0.3	-0.3	-0.3	-0.3	-1.5
Deny deductibility of club dues...........	0.1	0.3	0.3	0.3	0.3	0.3	1.5

I hope this information is helpful to you. If we can be of further assistance, please let me know.

Sincerely,

Harry L. Gutman

ITEM 1 OF 1 IN SET 1 *** 102ND CONGRESS ***
ALL
S.765 DATE INTRODUCED: 03/21/91

SPONSOR: Breaux

REFERRED TO: Senate Committee on Finance
COSPONSOR(S): CURRENT (45) WITHDRAWN (1)
Durenberger; Johnston; Gorton; Bryan; Kasten; Reid; Harkin; Shelby; Exon; Helms; Grassley; Burns; Lott (A-04/09/91); Inouye (A-04/09/91); Cochran (A-04/09/91); Thurmond (A-04/23/91); Smith (W-05/15/91); Levin (A-05/23/91); McCain (A-06/04/91); Mack (A-06/06/91); Boren (A-06/06/91); Pressler (A-06/13/91); Seymour (A-06/28/91); Akaka (A-07/17/91); D'Amato (A-07/23/91); Heflin (A-07/30/91); Symms (A-07/30/91); Brown (A-07/30/91); Craig (A-09/11/91); Nickles (A-09/12/91); Hatch (A-09/12/91); Smith (A-09/12/91); Hollings (A-09/12/91); Baucus (A-09/18/91); Conrad (A-09/26/91); Burdick (A-09/26/91); Hatfield (A-09/26/91); Murkowski (A-10/07/91); Mikulski (A-10/07/91); Wirth (A-10/15/91); Pryor (A-11/06/91); Bumpers (A-11/13/91); Packwood (A-11/26/91); Dixon (A-01/31/92); Coats (A-02/25/92); Rockefeller (A-02/25/92):
LATEST OFFICIAL TITLE:
OFFICIAL TITLE AS INTRODUCED AS OF 03/21/91:
A bill to amend the Internal Revenue Code of 1986 to exclude the imposition of employer social security taxes on cash tips.
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HOUSE CO-SPONSORS CURRENT 255

* DP – This is the ~~self~~-employed amendment we are working on with Chairman Bentsen. He is prepared to do this colloquy with you if you want. [signature]

SENATOR PRYOR: Mr. Chairman, as I believe you know, I have been working on an amendment to extend your important "job-lock" and other insurance market reform protections to people who want to start their own self-employed business but do not do so for fear of losing their current employer-provided insurance. Particularly during a time of economic downturn, we do not want people to not start businesses simply out of fear of losing health insurance.

Since there are outstanding issues that have yet to be resolved on this amendment, I will not offer it today. I do strongly believe, Mr. Chairman, that we should do everything possible to get this self-employed protection enacted into law. Because I know you share my concerns for the self-employed, I am confident we can do just that.

LIKELY LLOYD BENTSEN RESPONSE: Senator Pryor, Marina and the staff have indeed advised me of your hard work on this important matter. As you know, I share your commitment to addressing this self-employed issue. I commend you on your work and share your hope to work out any bugs in this amendment before we vote on final passage of this bill.

END OF HEALTH CARE SECTION BEFORE MRS WEISS WRAPS UP

PROPOSAL OF SENATOR ROCKEFELLER
REGARDING COAL MINER HEALTH BENEFITS

Purpose: To stabilize the funding of health care for retired coal miners, including especially "orphan" retirees whose former employers are out of business.

Background: Health benefits of retired coal miners and their families have been provided by multi-employer trust funds under successive bagaining agreements. With fewer and fewer coal companies making contributions, the funds are facing severe financial difficulties. Many employers stopped making contributions because they went out of business; others remain in business but simply stopped making contributions.

Proposal: The proposal is based on S. 1989. Under S. 1989, each company with beneficiaries in the trust funds will be responsible for its own retirees and will also participate with the rest of the industry in paying for the retirees whose companies are out of business.

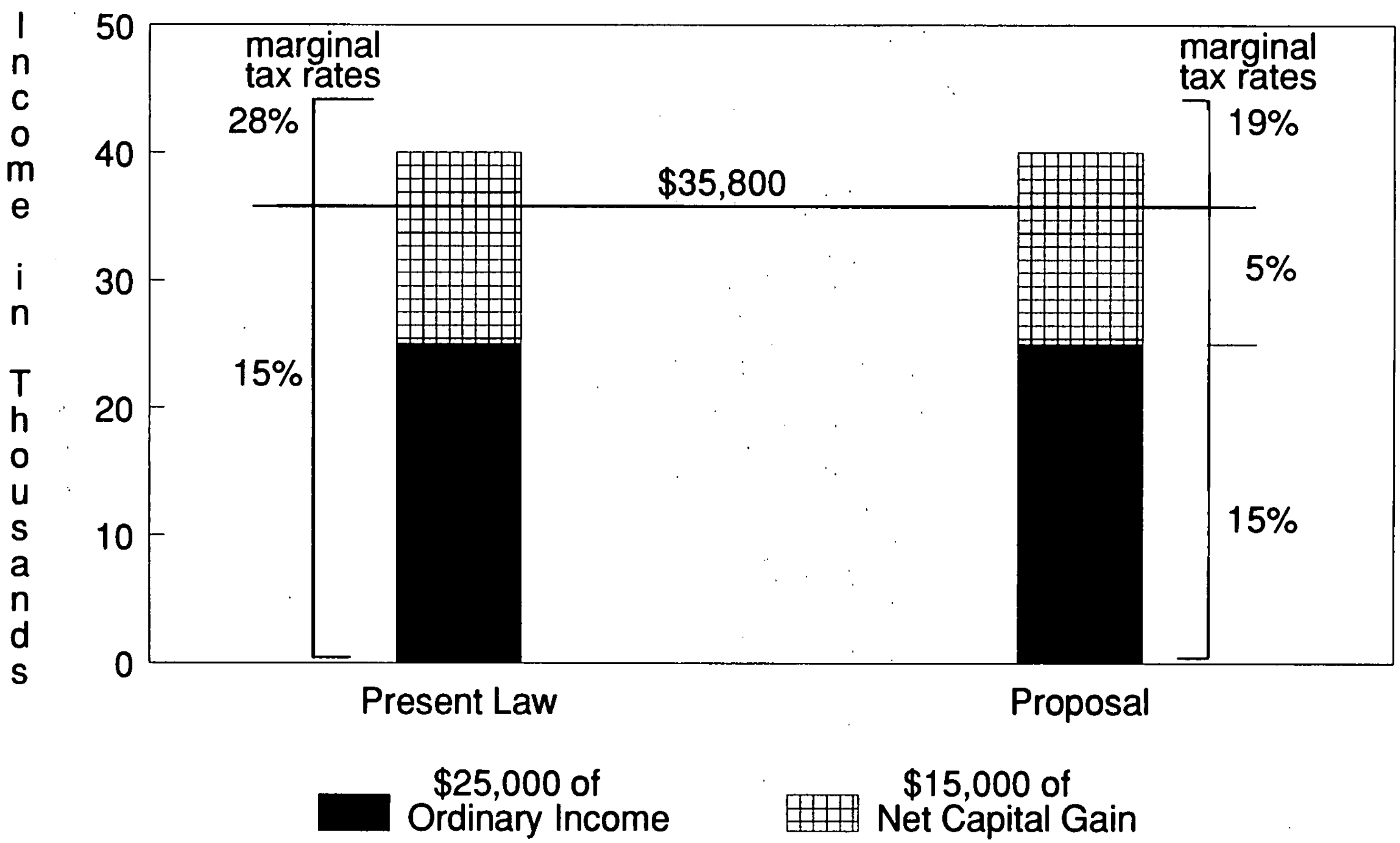
The bill creates two new entities to replace the old trust funds. One of the new entities is a government corporation called the Coal Industry Retiree Health Benefit Corporation. The other is a new multi-employer benefit fund.

Companies honoring the current collective bargaining agreement with the United Mineworkers of America will pay for their own retirees from the old funds through the new multi-employer benefit fund. Companies that are in business but who stopped paying for their retirees will pay for them through the new corporation. All coal companies will pay a per hour premium to the corporation to provide benefits to the "orphaned" retirees whose last employer is no longer in business.

A transfer of excess assets from the over-funded UMWA Pension Plan is used to help eliminate the current deficit in the health trust funds. Benefits are subject to cost containment.

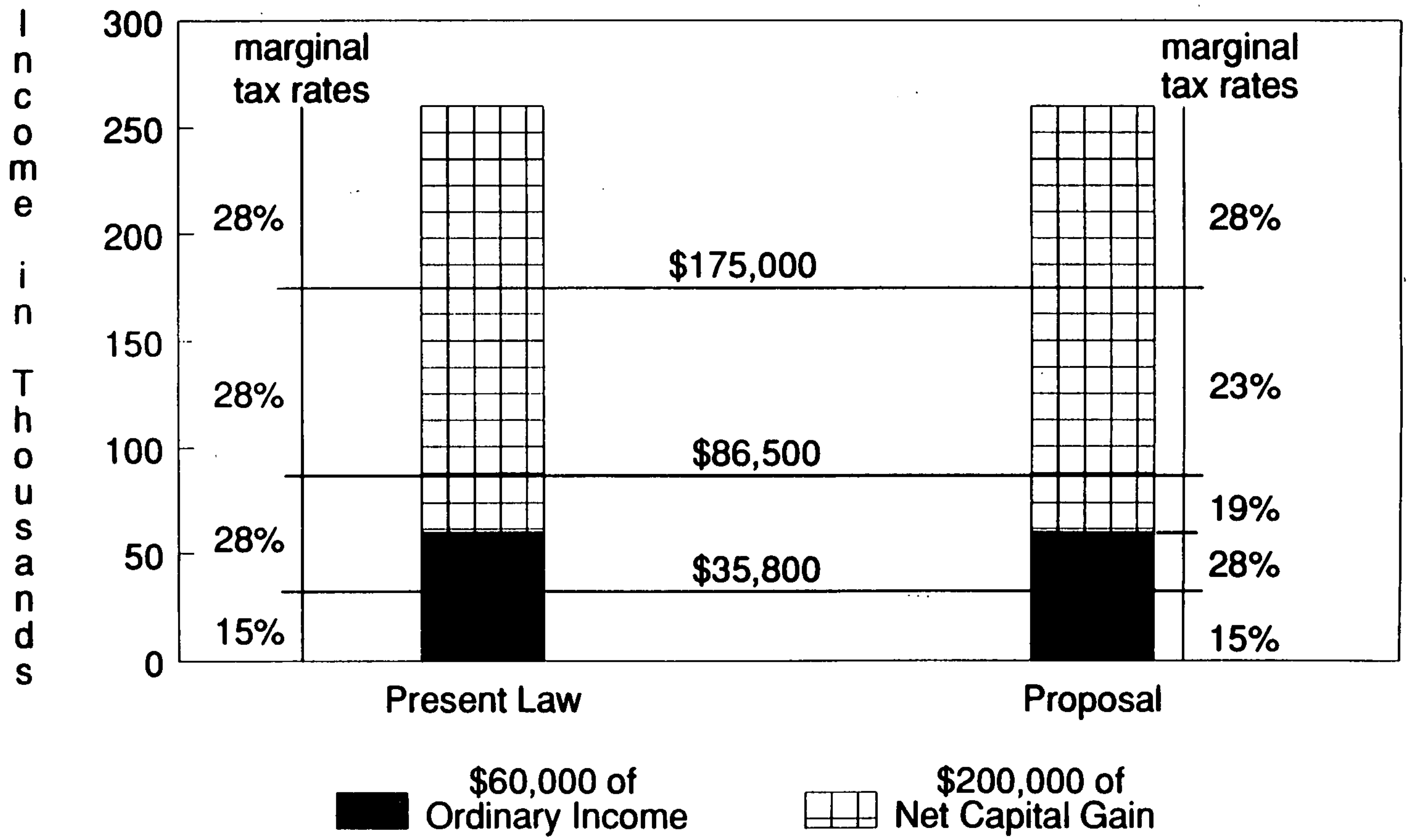
Modifications are made to S. 1989 to clarify the definition of coal production subject to the hourly fee and to define the category of companies still in business that have stopped contributing that will have a continuing obligation to contribute. The proposal does not include an exemption from budget limitations. Revisions are made in revenues to ensure deficit neutrality.

SFC Capital Gains Proposal
example 1



Under present law, the tax attributable to the $15,000 of net capital gain would be $2,445. Under the proposal, the tax attributable to the $15,000 of net capital gain would be $960.

SFC Capital Gains Proposal
example 2



Under present law, the tax attributable to the $200,000 of net capital gain would be $56,000. Under the proposal, the tax attributable to the $200,000 of net capital gain would be $49,190.

Progressive Capital Gains Proposal

The proposal applies an alternative tax rate schedule to net capital gain. In particular, the proposal would apply a marginal tax rate of 5 percent to net capital gain which otherwise would fall in the 15-percent tax bracket; a marginal tax rate of 19 percent to net capital gain which otherwise would fall in the 28-percent tax bracket; a marginal tax rate of 23 percent to net capital gain which would otherwise fall in the 31-percent tax bracket; and a marginal tax rate of 28 percent to net capital gain which otherwise would fall in the 36-percent tax bracket.

The effect of the alternative rate schedule is a reduction in the tax burden imposed on net capital gain, with the greatest tax reduction accruing to those taxpayers whose ordinary income is small. The attached pages provide detailed examples which show that a taxpayer with $100,000 of net capital gain but only $20,000 of ordinary income has his or her tax liability with respect to net gain income reduced 40 percent by the proposal (as compared to present law), while a taxpayer with $80,000 of net capital gain but whose ordinary income totals $60,000 has his or her tax liability with respect to net gain income reduced 29 percent. A taxpayer whose ordinary income totals $100,000 and who has $1 million of net capital gain receives a three percent reduction in tax liability with respect to net gain income under the proposal.

The computation of tax liability under the proposal is similar to the computation of tax liability under present law for those taxpayers subject to the maximum 28 percent tax rate on net capital gain.

In particular, the alternative rate schedule is applied to net capital gain by assuming that net capital gain is added last, after income from all other sources. The normal rate schedule is applied to taxable income less net capital gain. The alternative schedule of marginal tax rates is then separately applied to net capital gain. The attached pages provide detailed examples.

Progressive Capital Gains Proposal
Examples

For purposes of the examples, the following regular and alternative (capital gain) tax rate schedules are assumed. The regular schedule corresponds to the 1992 tax schedule for a married individual filing a joint return, as modified by the proposed 36-percent rate. These examples do not account for any potential alternative minimum tax liability.

Regular tax schedule

Taxable income	Tax liability
0 - $35,800	15%
35,800 - 86,500	$5,370 plus 28% of the excess over 35,800
86,500 - 175,000	$19,566 plus 31% of the excess over 86,500
175,000 and over	$47,001 plus 36% of the excess over 175,000

Alternative tax schedule (capital gains)

0 - $35,800	5%
35,800 - 86,500	$1,790 plus 19% of the excess over 35,800
86,500 - 175,000	$11,423 plus 23% of the excess over 86,500
175,000 and over	$31,778 plus 28% of the excess over 175,000

Example 1

Mr. A has $60,000 of ordinary income, $20,000 of qualifying net capital gain, and deductions of $30,000. Under present law, the first $5,800 of his net capital gain is taxed at 15 percent and the remaining $14,200 is taxed at 28 percent, for a total tax of $4,846 on net capital gain.

Under the proposal, the first $5,800 of his net capital gain would be taxed at five percent and the remaining $14,200 would be taxed at 19 percent, for a total tax of $2,988 on net capital gain.

Under the proposal, Mr. A has a $1,858 tax reduction on his $20,000 of net capital gain.

Example 2

Mr. B has $60,000 of ordinary income, $80,000 in qualifying net capital gain, and deductions of $30,000. Under present law, the first $5,800 of his net capital gain is taxed at 15 percent and the remaining $74,200 is taxed at 28 percent, for a total tax on net capital gain of $21,646.

Under the proposal, the first $5,800 of his net capital gain would be taxed at five percent, the next $50,700 would be taxed at 19 percent and the remaining $23,500 would be taxed at 23 percent, for a total tax on net capital gain income of $15,328.

Under the proposal, Mr. B has a $6,318 tax reduction on his $80,000 of net capital gain.

Example 3

Mr. C has $100,000 of ordinary income, $1,000,000 in qualifying net capital gain, and deductions of $50,000. Under present law, the entire $1 million gain is taxed at 28 percent, for a total tax on net capital gain of $280,000.

Under the proposal, the first $36,500 of his net capital gain would be taxed at 19 percent, the next $88,500 would be taxed at 23 percent and the remaining $875,000 would be taxed at 28 percent, for a total tax on net gain income of $272,290.

Under the proposal Mr. C has a $7,710 tax reduction on his $1,000,000 of net capital gain.

Example 4

Mr. D has $20,000 of ordinary income, $100,000 in qualifying net capital gain, and deductions of $30,000. Under present law, the first $10,000 of his net capital gain is taxed at zero percent, the next $35,800 is taxed at 15 percent, and the remaining $54,200 is taxed at 28 percent, for a total tax on net capital gain of $20,546.

Under the proposal, the first $10,000 of his net capital gain would be taxed at zero percent, the next $35,800 would be taxed at five percent, the next $50,700 would be taxed at 19 percent and the remaining $3,500 would be taxed at 23 percent, for a total tax on net capital gain of $12,228.

Under the proposal, Mr. D has a $8,318 tax reduction on his $100,000 of net capital gain.

ITEM 1 OF 1 IN SET 1

*** 102ND CONGRESS ***
ALL
DATE INTRODUCED: 03/21/91

S.765

SPONSOR: Breaux

REFERRED TO: Senate Committee on Finance
COSPONSOR(S): CURRENT (45) WITHDRAWN (1)
Durenberger; Johnston; Gorton; Bryan; Kasten; Reid; Harkin;
Shelby; Exon; Helms; Grassley; Burns; Lott (A-04/09/91);
Inouye (A-04/09/91); Cochran (A-04/09/91);
Thurmond (A-04/23/91); Smith (W-05/15/91); Levin (A-05/23/91);
McCain (A-06/04/91); Mack (A-06/06/91); Boren (A-06/06/91);
Pressler (A-06/13/91); Seymour (A-06/28/91);
Akaka (A-07/17/91); D'Amato (A-07/23/91); Heflin (A-07/30/91);
Symms (A-07/30/91); Brown (A-07/30/91); Craig (A-09/11/91);
Nickles (A-09/12/91); Hatch (A-09/12/91); Smith (A-09/12/91);
Hollings (A-09/12/91); Baucus (A-09/18/91);
Conrad (A-09/26/91); Burdick (A-09/26/91);
Hatfield (A-09/26/91); Murkowski (A-10/07/91);
Mikulski (A-10/07/91); Wirth (A-10/15/91); Pryor (A-11/06/91);
Bumpers (A-11/13/91); Packwood (A-11/26/91);
Dixon (A-01/31/92); Coats (A-02/25/92);
Rockefeller (A-02/25/92):

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HOUSE CO-SPONSORS CURRENT 255

<u>FICA TIP CREDIT WITH CLUB DUES OFFSET</u>

* Since 1988, employers in industries with tip income have been required to treat all employee tip income as employer-provided wages for FICA tax purposes.

* This is despite the fact that employers do not control tips, cannot plan for them, and are <u>prohibited</u> from considering most tips as wages elsewhere under federal law (i.e., the tip credit provisions of the Fair Labor Standards Act).

* This federal double-standard towards tip income is confusing and costly to hundreds of thousands of small businesses. It is a mistake we must correct.

* I have introduced S.765 which would repeal this Reagan Administration budget proposal outright. S.765 has been cosponsored by 46 Senators, including a majority of the members of this Committee.

* Recognizing the concerns of some members about any proposal -- no matter how sensible -- which serves to reduce the flow of revenues into the Social Security Trust Fund, I offer today a compromise measure which fully protects the Social Security Trust Fund while addressing the fundamental financial inequity highlighted in S.765.

* My amendment would create a new income tax credit for employers for certain FICA taxes paid on employee tip income.

* Under this amendment, employers would continue to pay FICA taxes on all employee tip income throughout the year. At year's end, they would calculate the amount of FICA taxes they paid on tips which could not be considered wages under the Fair Labor Standards Act. They would receive a tax credit for this amount.

* Example -- Under current law, a waitress earns and reports $8.00 per hour in tips. The employer is allowed to consider up to $2.12 per hour in tips as wages. The employer pays a cash wage of $2.13 per hour and takes a tip credit of $2.12 per hour to ensure the $4.25 minimum wage obligation is fulfilled. The waitress's total income is $10.13 per hour. Despite the fact that only $2.12 per hour in tips are allowed here as wages, the employer pays FICA on all tips. His tax liability on that employee is 77 cents per hour ($10.13 x 7.65%). Under my proposal, the employer's tax credit would be equal to the amount of FICA he must pay on tips above $2.12 per hour. In this example, his credit would be 45 cents per hour for this employee. This financial relief equalizes the tipped employer's payroll tax liability with that of other industries -- taxes are owed only on wages under the control of the employer. The FICA funds remain protected.

* Reducing the cost of labor will help create jobs. According to the Employment Policies Institute, my bill would create more than 39,000 new jobs and would be a "cost-effective job creation program to deal with the current recession."

* The debate surrounding this tax bill has centered on tax fairness, job creation, and economic growth. This proposal contains all three, and I urge its adoption.

Elimination of Business Deduction for Club Dues

* While regular working people cannot deduct membership dues for local health fitness clubs or other clubs that offer cultural, educational, athletic or entertainment value, their corporate counterparts and businessmen are able to reduce their taxes by deducting dues paid to posh clubs.

* Current law enables a limited class of high income people to entertain themselves and their friends under the cloak of "business" while wage earners, journeymen, and other middle income people, are not able to put on such airs and get a tax break.

* In times like these, we cannot afford to subsidize executives who get to use such clubs, while middle and low income families are able to participate only with their own hard earned after-tax dollars, if at all.

* Because membership dues have been deductible, the price of joining has been artificially elevated. Corporate money has bid up the cost of belonging. This has made it even more difficult for the average person who is not in a position to write it off to be able to join a club in which he or she seeks membership. By removing the deduction, executives would be less inclined to spend shareholders' dollars on multiple high-priced club memberships. They would be more choosy about which and how many clubs they would join. This would stop the price escalation and leave more room for greater middle class anticipation.

* Let us be clear, this measure does not interrupt the existing deduction for fees connected to each use of club owned facilities. Thus, for example, if a salesman were to take three customers golfing with him to get a chance to tell them about a new product line, then so long as the business purpose of the event is established, the green fees for that round of golf would still be deductible. It is just the underlying memberships dues that would not be.

* While the way I wish to invest this recovered revenue loss will clearly create tens of thousands of jobs, I do not believe that this amendment will cost jobs. In fact, I think it could increase employment among clubs. When the XYZ Corporation buys membership in four golf clubs, for example, that does not produce a recurring employment opportunity for greens keepers, caddies, etc. It is the actual use or the rounds of golf that do that. Under current law, many who would like to belong to the club and play the club on a regular basis are frozen out by the high membership fee which was bid up by the all the XYZ Corporations. By removing the tax subsidy of membership dues for the privileged few, we will increase access to the club for the average person. It is their use, their rounds of golf, for example, who will create the need for more employees at the clubs.

* The way this amendment is structured recognizes that legitimate business is often conducted in connection with the utilization of clubs since it leaves intact the case by case deduction for each use. But it also recognizes that merely belonging to a club does not prove a business purpose.

* Furthermore, in offering this amendment, we are recognizing that only the privileged few are in a position to try to broadly claim a business purpose deduction for membership dues, while the existing deduction for specific use is open to anyone who can show that each expenditure was, in fact, in pursuit of a business purpose.

Congress of the United States

JOINT COMMITTEE ON TAXATION
1015 LONGWORTH HOUSE OFFICE BUILDING
WASHINGTON, DC 20515-6453
(202) 225-3621

Honorable John B. Bréaux
United States Senate
Washington, DC 20510

Dear Senator Breaux:

This letter is in response to your request dated February 28, 1992, for an estimate of the revenue effects of a two-part proposal.

The first part of the proposal would provide employers with a Federal income tax credit in an amount equal to the FICA tax obligation they pay on cash tips paid each year. The credit would apply to that portion of tip income that is in excess of the amounts that are considered wages for purposes of minimum wage requirements.

The second part of the proposal would deny the deductibility from taxable income of club dues paid to social, athletic, luncheon, and sporting clubs.

The following estimate assumes that these proposals would become effective upon enactment (assumed to be April 1, 1992).

	Fiscal Years [Billions of Dollars]						
Item	1992	1993	1994	1995	1996	1997	1992-97
Credit for tips.......	-0.1	-0.3	-0.3	-0.3	-0.3	-0.3	-1.5
Deny deductibility of club dues...........	0.1	0.3	0.3	0.3	0.3	0.3	1.5

I hope this information is helpful to you. If we can be of further assistance, please let me know.

Sincerely,

Harry L. Gutman

March 2, 1992

CONGRESS SHOULD RAISE THE PROPERTY/CASUALTY REINSURANCE EXCISE TAX

In passing the Tax Reform Act of 1986, Congress substantially increased the U.S. tax burden of domestic property and casualty reinsurance companies (by requiring the discounting of loss reserve deductions). However, Congress did not pass a corresponding increase in the excise tax applicable to foreign reinsurers who reinsure property and casualty risks located in the United States. For decades, this excise tax, currently at a rate of 1 percent of the premium paid to an offshore reinsurer, provided rough tax parity between domestic reinsurers subject to U.S. tax on their net income and foreign reinsurers not subject to U.S. income tax.

Congress should remedy the competitive disadvantage this situation causes domestic reinsurers, by increasing the reinsurance excise tax to 4 percent. This increase is necessary for the following reasons:

- Since 1986 the foreign share of the U.S. risk reinsurance market has increased from a 26 percent share to approximately 40 percent. This migration demonstrates the cost disadvantage faced by domestaic reinsurers in this tax-sensitive industry.

- Increasing the rate of tax will primarily affect tax haven reinsurers. The United States has treaties with most other major international insurance centers which waive the reinsurance excise tax. Existing treaty waivers of the tax will not be disrupted.

- Based on a study conducted by members of the Reinsurance Association of America, an increase in the tax to a 4 percent rate would be a conservative approach (the study indicated that the 1986 Act effect on domestic reinsurers translated into approximately a 7 percent premium tax). A 4 percent rate also is identical to the rate of excise tax imposed on <u>primary</u> insurance purchased from foreign insurers.

- Similar measures were passed by the Senate in 1984 and the House in 1985, but dropped in conferences pending further consideration.