91st Congress }
1st Session }
COMMITTEE PRINT

TAX REFORM ACT OF 1969

COMPILATION OF DECISIONS REACHED IN EXECUTIVE SESSION

COMMITTEE ON FINANCE
UNITED STATES SENATE
RUSSELL B. LONG, *Chairman*

OCTOBER 31, 1969

Printed for the use of the Committee on Finance

U.S. GOVERNMENT PRINTING OFFICE
35-876 O
WASHINGTON : 1969

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*This press release is referred to in the Oct. 10, 1969 press release.

Introduction

This document contains the day-by-day press announcements of the committee decisions with respect to the Tax Reform Act of 1969. Generally, the announcements contained herein indicate those areas of the House bill which were amended by the Committee on Finance. In the event any feature of the House bill is not mentioned in these announcements, it is likely that the provision involved was not amended by the committee, but was agreed to without change, or with only necessary technical changes. This list of announcements is not intended to indicate the substance of all the provisions of the House bill.

PRESS RELEASE

FOR IMMEDIATE RELEASE
October 9, 1969

COMMITTEE ON FINANCE
UNITED STATES SENATE
2227 New Senate Office Building

STATE AND LOCAL BOND INTEREST AND TAX REFORM

Senator Russell B. Long (D., La.), Chairman of the Committee on Finance, announced today that the Committee had agreed that it would not subject State and local bond interest to Federal income tax. This was the first decision reached by the Committee in their deliberation on the tax reform bill of 1969. The Committee also agreed to delete that provision in the House bill which would provide a subsidy for States and local governments which choose to issue their bonds on a taxable basis and pay competitive market rates of interest on them.

The Committee decided to retain the provision in the House tax reform bill which subjects interest earned on so-called arbitrage bonds to Federal income tax. Arbitrage bonds are those which are sold by the State and local government, the proceeds of which are reinvested in higher yield Federal or corporate securities. The Committee felt that these bonds served no useful governmental purpose but were an unhealthy consequence of the record-high interest rates existing in the Country today.

Finally, the Committee added to the bill a provision which will require in the future that State and local bond interest be reported on the tax return for statistical purposes only.

The Chairman indicated that because of the gap in knowledge as to who the recipients of this interest are there had been considerable speculation that these bonds are purchased primarily for their tax avoidance potential. He stated that this attitude overlooked the more obvious point that the purchaser of State and local governmental bonds had already borne a tax in the form of a return for his investment.

The full text of Senator Long's statement is attached.

TEXT OF STATEMENT MADE BY HONORABLE RUSSELL B. LONG, CHAIRMAN, COMMITTEE ON FINANCE, ANNOUNCING THE COMMITTEE DECISIONS WITH RESPECT TO THE TAX TREATMENT OF INTEREST PAID ON STATE AND LOCAL GOVERNMENT BONDS

The Finance Committee acted this morning to delete those provisions of the House tax reform bill which would indirectly tax the interest earned on State and local government bonds. Under this action the limit on tax preferences and the allocation of deduction provisions of the House-passed tax reform bill will not apply to this bond interest. The provision extending a Federal subsidy to State and local governments which choose to issue their bonds on a taxable basis was also deleted.

The Committee felt that if there was ever a time for ending the tax exemption on this interest income, 1969 is not the year to do it. Interest rates are at the highest level in over 100 years.

Because of this, taxable investment opportunities have attracted money away from the State and local government bond market. This in turn has caused interest rates on some State and local bonds in recent months to rise three times as swiftly than interest rates generally. On the other hand, provisions in many State Constitutions severely limit the interest that State or local governments may pay on their obligations. These factors have made it very difficult for States and municipalities to raise the funds they need to finance the improvements they desire for their citizens.

The tax bill has added to this difficulty by further reducing the net income a purchaser of these bonds might earn. This causes a widening of the gap between the net yield on taxable corporate and Federal securities on the one hand and tax-exempt State and local governmental securities on the other.

Good tax policy considerations and public policy considerations alike demand that the total tax structure -- Federal, State and local, combined -- be explored in determining the advisability of tax reform aimed at a Federal tax on State and local bond interest.

The Committee on Finance did explore these aspects.

During the hearing before the Finance Committee, a distinguished panel of Governors representing the National Governors' Conference was followed to the witness table by a distinguished panel of Mayors which, in turn, were followed by a distinguished panel of County officers. These dedicated officials presented irrefutable evidence of the impact the House tax reform bill has already had on their functions.

Their capital improvement programs cannot be initiated. Their bond issues have been authorized but the bonds cannot be sold. Bonds they have already issued are rapidly depreciating in value, causing considerable losses to their holders.

These witnesses reminded the Committee that the House tax reform bill would raise only $80 million annually in revenues for the Federal Treasury through the tax on their bond interest. Then they carefully demonstrated that State and local taxes would have to go up by $200 million a year to pay for it.

State and local tax structures generally are regressive -- they fall more heavily on the poor than on the rich. Sales taxes, property taxes, gasoline taxes -- these are the levies that would need to be hiked at State and local levels to pay the higher yields demanded by purchasers in anticipation of a Federal tax on their bond interest. These are the taxes that hit hardest at the poor.

Based on the testimony we received, the Committee on Finance concluded this morning that the provisions of the House bill taxing State and local bond interest constituted a very inefficient tax reform and should not be enacted. The Committee is hopeful that the action it has taken on this subject will restore confidence to the tax-exempt bond market and enable State and local governments to get on with the important work of improving services and facilities for their own citizens.

ARBITRAGE BONDS

The Committee agreed to retain that provision in the House Tax Reform bill which would tax the interest earned on so-called "arbitrage bonds." However, the provision was modified to make it somewhat more objective.

Arbitrage bonds are bonds issued by a State or local government, the proceeds of which are reinvested in higher yield Federal or corporate securities.

The Committee felt that State and local governments should not use their tax exempt privilege for the purpose of gaining a higher return on other investments in this day of record-breaking interest rates.

The Committee action consists primarily of the addition to the bill of a definition of the type of bond to which the House bill referred but did not identify. It is made clear in this definition that bonds issued by a State and local government to provide funds for the financing of residential housing, sports facilities, airports, docks, warfs, mass commuting facilities and park facilities, air and water pollution control facilities, sewage or solid waste disposal facilities, or for facilities of the local furnishing of electric energy, gas or water would not be treated as arbitrage bonds, and the interest on bonds issued for these purposes would remain tax-exempt. These are the purposes for which an exception was provided when Congress acted last year to tax the interest earned on industrial development bonds.

REPORTING OF TAX-EXEMPT INTEREST

The Committee also agreed to a provision which in the future would require that individuals and corporations receiving tax-exempt State and local bond interest must report their bond interest on their tax returns for statistical purposes only

This will provide information as to where, in the income classes, interest on these bonds is received. This will indicate whether there are individuals with large amounts of this income who are avoiding the payment of any Federal taxes.

Today this interest is not reported on tax returns for any purpose. No one knows who receives this interest at the present time and this gap in our knowledge has led to considerable speculation that these bonds are purchased primarily for their tax exemption.

The statistical knowledge gained by requiring that tax-exempt interest be identified on the tax return will permit a more rational discussion of the question of whether these bonds are used primarily as a tax-avoidance device.

It is certainly true -- although tax-purists are unwilling to concede it -- that the purchaser of State and local bonds have already borne a tax, a tax in the form of a lower return on their money.

P.R. #25

PRESS RELEASE

FOR IMMEDIATE RELEASE
October 10, 1969

COMMITTEE ON FINANCE
UNITED STATES SENATE
2227 New Senate Office Bldg.

COMMITTEE DECISIONS
TAX REFORM ACT OF 1969

Senator Russell B. Long (D., La.), Chairman of the Committee on Finance, announced today that the Committee had taken the following action in executive session on H. R. 13270, the Tax Reform Act of 1969.

50 Percent Maximum Tax on Earned Income. -- The Committee agreed to delete Section 802 of the House-passed tax reform bill. This provision would have reduced the maximum tax on earned income from 70 percent (77 percent with the surtax) to 50 percent.

This action removes the distinction created by the House bill, based on the source of income, and increases the revenue to be gained by the bill by $200 million in 1970.

Deduction for Gasoline Tax. -- The Committee decided not to approve an administration suggestion that the Federal income tax deduction be disallowed in the case of State and local gasoline taxes. Before the Committee acted, the Treasury Department modified its original suggestion so that those who commute not more than 10 miles per day could continue to deduct the State and local tax paid on the gasoline they purchase to travel to and from work. As already reported, the Committee rejected this suggestion.

Capital Gains Holding Period. -- The Committee agreed that it would retain the provision in present law which requires taxpayers to hold a capital asset for 6 months if the gain from the sale of the asset is to qualify for favorable capital gains tax treatment. In taking this action, which was recommended by the Treasury Department, the Committee rejected the feature which would have extended the holding period to one year. The Committee did not act on the provision to repeal the maximum capital gains rate of 25 percent.

The Treasury Department indicated that there was some question as to whether the extension of the holding period would increase revenues by the $150 million they had previously estimated. They indicated that on reconsideration they felt the revenue increase estimated under the House bill might not be nearly so large.

Deferred Compensation. -- The Committee agreed to delete the provision of the House bill (Sec. 331) which would have imposed a tax on amounts received as deferred compensation based on the rates which would have been applied if the deferred amount had been received in the year in which earned. This action carried out a recommendation made by the Treasury Department.

Investment Tax Credit. -- The Committee agreed that the rules in the House bill for repealing the 7 percent investment tax credit would be modified to conform to the Committee's previously announced decisions (of September 19, 1969)* with respect to the repeal of the credit. In addition, the Committee made one change in its September 19 decisions.

This single change related to the special transitional exception for railroad rolling stock. Under the prior announcement this exception was to apply to all "rolling stock." Under the Committee's decision of today, this exception is not to apply to locomotives (other than passenger train locomotives), flat cars, or railroad cars for the hauling of automobiles.

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* This press release is reproduced on page 7.

PRESS RELEASE

FOR IMMEDIATE RELEASE
September 19, 1969

COMMITTEE ON FINANCE
UNITED STATES SENATE
2227 New Senate Office Bldg.

REPEAL OF INVESTMENT TAX CREDIT

Senator Russell B. Long (D., La.), Chairman of the Committee on Finance, announced today that the Committee on Finance had taken the following action in executive session.

Investment Tax Credit Repeal. -- It ordered that H. R. 7311, a bill to reduce the import duties on stethoscope parts, be reported with a Committee amendment to repeal the 7 percent Investment Tax Credit.

Explanation of Amendment. -- The Committee amendment generally adds to the bill the language previously approved by the House of Representatives (and reported to the Senate by the Committee on Finance) as part of H. R. 12290. (Among other features that bill would have extended the income tax surcharge through June 30, 1970).

Under the Committee amendment, the 7 percent investment tax credit generally would be repealed as of April 18, 1969. The Committee, however, did revise several features of the repeal provision. These revisions are as follows:

Railroad Rolling Stock. --The Committee provided that railroad rolling stock ordered under binding contracts prior to January 1, 1971, and placed in service prior to January 1, 1975, is to qualify for a progressively smaller tax credit computed as of the time the rolling stock actually is placed in service. This declining credit would be calculated under a schedule identical to the "phase-out" rules contained in H. R. 12290.

Phase Out - Unused Tax Credits. --The Committee provided that for property eligible for the credit after April 18, 1969, the "phase-out" rules in H. R. 12290 would not apply and this property would qualify for the full 7 percent credit if it is placed in service not later than December 31, 1978. (Under H. R. 12290 the credit would be reduced by one-tenth of one percentage point per month beginning in 1971 and it would be finally repealed as of January 1, 1975.)

The Committee also provided an additional 3-year carryover for unused tax credits which cannot be utilized because of the special 20 percent limitation on tax credits included in prior versions of H. R. 12290.

New Design Products. -- The Committee agreed to extend the so-called Lockheed amendment to McDonnell-Douglas, enabling both of these aircraft manufacturers to qualify for the credit with respect to property they must acquire to produce the air buses which they have committed themselves to build. Specifically, it would reduce from 60 percent to 50 percent the test on the number of aircraft which it has contracted (as of April 18, 1969) to deliver by 1973, and would permit price changes where materials costs fluctuate as well as where wage rates fluctuate.

Sale and Leaseback. -- The Committee agreed to add to the bill a provision included in the 1966 Suspension Act to insure that the investment tax credit will not be recaptured if the property subject to the lease should be returned to the lessor. (The very narrow leaseback exception which the House included in H. R. 12290 as a substitute for the 1966 rule would be retained with respect to the situation for which it was designed by the House.)

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Purchase of Corporate Assets. --The Committee agreed to continue the tax credit where all the assets of a business (including binding contracts to lease property eligible for the credit) are acquired by another corporation. (This makes the treatment under the bill consistent with the treatment which would occur if the acquiring corporation purchased the stock of the other corporation and then liquidated it, thus ending up with its assets.)

Performance Contracts. --The Committee agreed to allow the tax credit to be taken by a taxpayer who was required by a binding contract in effect on April 18, to acquire property specified in the contract to be used to produce products substantially all of which are to be sold to the other party to the contract. Special restrictions in the case of extractive property would require the property involved to be placed in service by January 1, 1973, and that the contract of sale must not have included escalation clauses to protect against loss of the tax credit. Where the extractive property which must be acquired is not specified in the contract, it must be readily ascertainable from the location and characteristics of the material involved in the sales contract. Except for these features applicable only to extractive property, this provision is similar to one contained in the 1966 Act suspending the investment tax credit.

Certain Leaseback Arrangements. --Under H. R. 12290 a taxpayer may transfer his rights in property to a leasing company in a leaseback arrangement qualifying the lessor for the credit only if the transaction involves the transfer of a binding contract in effect on April 18, 1969. The Committee agreed to extend this favorable feature to property eligible for the tax credit under other provisions as well, such as, for example, the machinery and equipment rule.

Non-subsidized Shipping Lines. --The Committee would treat non-subsidized shipping lines in the same manner as subsidized shipping lines with respect to bar[illegible] necessary to the planned use of ocean-going vessels designed to carry barges and contracted for on April 18, 1969. The amendment would allow non-subsidized lines the benefit of the investment tax credit if more than 50 percent of the barges necessary to the planned use of the vessel are acquired on or before April 18, 1969, or are subject to binding contracts in effect on that date.

Estimated Tax. -- The Committee would provide rules to protect taxpayers who filed declarations of estimated tax claiming the benefit of the tax credit with respect to property contracted for after April 18, 1969. Under such rules, taxpayers would be protected from the assertion of penalties until they have had an opportunity to revise their estimates to reflect the repeal of the credit.

Recapture Rules. -- The Committee adopted rules preventing the recapture of the investment tax credit where property for which the credit was allowed is held for only a short time and then is disposed of and is shortly replaced with other property of a like kind.

EXTENSION OF INTEREST EQUALIZATION TAX

Extension. -- The Committee agreed to report H. R. 12829, which would extend the interest equalization tax through March 31, 1971, with technical amendments, and with a single amendment relating to another matter. This other amendment, described below, would repeal the ammunition registration requirements of the Gun Co[illegible]l Act of 1968.

Technical Amendment. -- An amendment was adopted which provides that leases are to be treated as giving rise to debt obligations for interest equalization tax purposes in cases where the lease is principally a financing transaction. The financing company provision was broadened to allow the financing of export leases and an exemption was provided for export leases which is similar to the existing export sales exemption.

Two modifications of the financing company provision of the bill also were adopted. A financing company is to be permitted to loan out amounts represented by accrued foreign taxes which are payable within three years, rather than one year as under the House bill. Also, a financing company is to be allowed to own debt obligations acquired in the course of carrying on its financing business (such as loans to employees) in addition to the other types of debt obligations the company is allowed to own under the House bill.

Ammunition Registration. -- The Committee approved as an amendment to H. R. 12829 the text of S. 2718, introduced by Senator Bennett of Utah and co-sponsored by 46 Senators. This amendment would modify the Gun Control Act of 1968, to repeal the registration requirements concerning persons purchasing .22 caliber rimfire ammunition or ammunition for shotguns or rifles. The amendment would also repeal the registration requirements for component parts of the same types of ammunition. At present the registration provision requires the purchaser of ammunition to give his name, address, and date of birth; the date of purchase; the manufacturer, caliber, gauge or type of component, and the quantity of the ammunition purchased; and the purchaser's driver's license number or other type of personal identification.

F. R. #23

PRESS RELEASE

FOR IMMEDIATE RELEASE
October 13, 1969

COMMITTEE ON FINANCE
UNITED STATES SENATE
2227 New Senate Office Bldg.

Tax Reform Act of 1969
Charitable Contributions
Actions in Executive Sessions

Honorable Albert Gore (D., Tenn.), who presided during the afternoon session of the Committee on Finance announced today that in considering the Tax Reform Act of 1969 the tax treatment of charitable contributions was taken up by the Committee. In deliberation on this portion of the bill, he reported that the Committee had taken action with respect to the different categories of transactions that are set forth below:

50 Percent Limitation. -- The Committee agreed to the provision in the House bill which would increase the overall limitation on the deduction of charitable contributions from 30 to 50 percent for gifts to "public" charities. In accepting the House provision the Committee also approved a Treasury Department suggestion that a taxpayer's basis for property contributed to public charities be eligible for the 50 percent limitation, and that only the appreciation element in the donated property be limited to 30 percent. (Under the House bill the entire value of the gift of appreciated property would have been limited to 30 percent.)

The Committee also agreed to modify the House provision (and the existing law) to allow contributions to private operating foundations, and private non-operating foundations which distribute the contributions they receive to public charities within one year, to qualify for the 30 percent and 50 percent limitations. This action involved approval of a suggestion made by the Treasury Department.

Unlimited Charitable Contribution Deduction. -- The Committee agreed to repeal the unlimited charitable contribution over a 5-year period. This is the same period provided for by the House bill.

The Committee did modify the 5-year phase-out rule, however, so that the following features of the House bill would not apply in the case of the unlimited charitable contribution deduction:

(a) The inclusion of appreciated charitable gifts as tax preferences within the limit on tax preferences and allocation of deduction rule,

(b) the allocation of the charitable deduction,

(c) the 30 percent limit on gifts of appreciated property,

(d) the appreciated property rule in the case of property which would give rise to a long-term capital gain if sold.

The Committee was advised that these rules (if applied) would often render the special phase-out for the unlimited charitable deduction meaningless, in effect causing the immediate repeal of this deduction rather than a phase-out.

Gifts of Appreciated Property . -- The Committee generally agreed to the provisions of the House bill which require that the amount of appreciation in value of property donated for charitable objectives be taken into account for Federal income tax purposes. However, the Committee modified the House rules in a number of respects, as follows:

(1) In the case of gifts of capital gain property to private foundations, the Committee adopted a simplified rule for taking the appreciation into account. Under this rule, the donor would be allowed a charitable deduction equal to his cost or other basis for the property, plus one-half of the appreciation. This rule is a substitute for the dual House rule which involved either deducting only the cost of the property or retroactively deducting the value of the property by including the appreciation in income. The Committee's rule achieves substantially the same net effect as if the donor had included the appreciation in income and claimed a charitable deduction for the fair market value of the property.

(2) The Committee removed gifts of future interest in property (which is not tangible personal property or ordinary income property) from the types of property to which the appreciation rules of the House bill apply. The Committee felt the inclusion of future interest within the appreciation rules could have a substantial adverse effect on charitable giving to public charities and schools, since future interest gifts are a common form of charitable giving.

(3) The bargain sale provision of the House bill was deleted. Under this action, sales to charity of appreciated property for less than its fair market value would not give rise to any allocation of basis between the portion of the property sold and the portion given away. Stated differently, under this Committee decision, no gain would be recognized for tax purposes because of the making of the bargain sale.

With these changes, the Committee approved the appreciated property rules of the House bill. Specifically, it approved the amendments which require that appreciation in value of gifts of tangible personal property (such as art works and books) be subject to the appreciation rules.

2-Year Charitable Trusts . -- The Committee approved the House provision without change.

Charitable Contributions by Estates and Trusts. -- The Committee adopted the House provision which would eliminate the deduction for amounts set aside for charity, which is presently allowed non-exempt trusts, subject to certain modifications.

(a) Set-Aside Deduction. -- First, the Committee restored the set-aside deduction in the case of estates, since it may often be impractical or contrary to probate law for an estate to make current distributions. The Committee also restored the set-aside deduction in the case of pool arrangements under which a person transfers property to a public charity which places it in an investment pool and pays the donor the income attributable to the property for life. This set-aside deduction, however, would be limited to the amount of the pool's capital gain income. The Committee took this action in order to prevent a significant adverse effect on the use of these arrangements which have been increasingly relied on by public charities.

(b) Irrevocable Trusts; Wills. --The Committee also restored the set-aside deduction in the case of certain types of existing arrangements which were established in contemplation that the deduction would be available. The set-aside deduction will continue to be available under the Committee action in the case of existing irrevocable trusts (established before August 1, 1969). The deduction also would continue to be available, as recommended by the Treasury, for trusts established pursuant to a will in existence on August 1, 1969, which cannot be changed under State law prior to the person's death because of his incompetency or other disability. In the case of trusts provided for in wills in existence on August 1, 1969, the set-aside deduction will continue to be available if the person dies within three years.

(c) Effective Date. --The Committee also adopted the Treasury recommendation that the elimination of the set-aside deduction apply only with respect to taxable years beginning after 1969.

Gifts of the Use of Property. -- The Committee adopted the provision of the House bill which denies a deduction for gifts of the use of property with a modification to insure that this provision does not have unintended effects such as denying a deduction for an outright gift of a fractional interest in property. Generally, the Committee's action would restrict this provision to gifts of terminable interests in property or future interests in property.

Charitable Remainder Trusts. -- The House bill provided that the charitable contribution deduction (for income, estate, and gift tax purposes) would be allowed for a charitable gift of a remainder interest in trust only where the trust was an annuity trust (i.e., it specified the annual amount to be paid the noncharitable income beneficiary in dollar terms) or was a unitrust (i.e., the specified amount was expressed as a fixed percentage of the value of the trust's assets).

The Committee, in general, accepted this provision of the House bill but adopted a series of modifications of the provision to provide persons with greater flexibility in making this type of gift and to reduce the potential adverse effect of the provision on established forms of giving, while at the same time protecting against the abuses to which the provision is directed.

(a) Pooled Arrangements; Gifts of Real Property . -- First, the charitable deduction would continue to be allowed in the case of gifts to pool arrangements even though the annuity trust or unitrust requirement was not met. In this case, however, the amount of the charitable deduction would be determined with reference to the highest rate of return from the particular pool or fund during the three years prior to the contribution. A similar situation in which the Committee decided to allow a charitable deduction, even though the annuity trust or unitrust requirements are not met, is in the case of gifts of real property to charity where the donor and/or his spouse reserve the right to live on, or receive the income from, the property for life. Where appropriate, straight-line depreciation or cost depletion would be taken into account in valuing the charitable gift.

(b) Unitrusts and Annuity Trusts. - The Committee also adopted a modification of the unitrust rule in order to provide greater flexibility with regard to this type of gift. Under this modification, a unitrust would be required to pay the noncharitable income beneficiary only the amount of the trust income where this is less than the percentage amount stated in the trust. In addition, deficiencies in income distributions (i.e., where the trust income was less than the stated percentage amount) could be made up in later years when the trust income exceeded the stated percentage amount. As under the House provision, however, the percentage amount would continue to be used in determining the amount of the deduction allowed for the charitable remainder.

The Committee also modified the definitions of an annuity trust and a unitrust to permit these trusts to have more than one noncharitable income beneficiary.

(c) Effective Dates . -- The Committee also adopted certain modifications of the effective date provisions of the charitable remainder trust rules. For purposes of the income tax charitable deduction, the new rules are to be applicable only to transfers in trust after October 9, 1969. For estate tax purposes, the new rules are not to apply in the case of trusts created before October 9, 1969, which provide an irrevocable gift to charity. In addition, the new rules are not to apply with respect to trusts created by wills in existence on October 9, 1969, if the person dies within three years. Finally, the new rules are not to apply with respect to trusts established in wills in existence on October 9, 1969, which may not be changed under State law prior to the person's death because of his incompetency or other disability. The Committee took these actions since they involved situations where the new rules could not have been taken into account and, therefore, the Committee felt it inappropriate to deny a charitable contribution deduction in these cases.

Charitable Income Trust with Noncharitable Remainders. -- The Committee adopted the House provision regarding the allowance of a charitable deduction for a gift of an income interest to charity in trust with minor modifications. Generally, under the House provision a deduction would not be allowed in these cases except where the grantor is taxable on the trust income. The purpose of this rule is to prevent the taxpayer from receiving a double benefit (i.e., a charitable deduction and also an exclusion from his tax base of the trust income). Since the possibility of this double benefit is present in the case of the income tax charitable deduction but not the estate and gift tax charitable deductions, the Committee decided to make the new rules (other than the requirement of an annuity trust or unitrust format) inapplicable for estate and gift tax purposes.

The Committee also decided to make the new rules for purposes of the income tax charitable deduction applicable to transfers in trust after October 9, 1969.

Repeal of 7 Percent Investment Tax Credit. -- As previously announced by the Committee (on October 10, 1969) the provisions of the tax reform bill repealing the 7 percent investment tax credit were modified to conform to the actions taken on September 19 when it considered this matter. In its announcement of October 10, the Committee reported a single modification of the earlier decisions -- a modification narrowing the type of equipment eligible for the credit under the special transitional exception for "rolling stock" of railroads.

Today the Committee gave final approval to one further modification urged by Senator Goodell of New York. Under this modification a contract between members of an affiliated group entered into before April 18, 1969 (which under the House bill would not be treated as a binding contract) will be treated as a binding contract where the affiliation between the parties to the contract is ended before June 30, 1969.

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PRESS RELEASE

FOR IMMEDIATE RELEASE
October 14, 1969

COMMITTEE ON FINANCE
UNITED STATES SENATE
2227 New Senate Office Bldg.

Tax Reform Act of 1969
Actions in Executive Session

Honorable Russell B. Long (D., La.) announced today that the Committee on Finance was continuing to make considerable progress in its work on the Tax Reform Act of 1969. He reported that in executive session the Committee had made decisions with respect to several provisions of the House-passed bill as described below. He noted that these actions preserved many of the important tax reform features contained in the House bill with only minor changes.

Restricted Property. -- The Committee agreed to the provision in the House bill which provides that a person who receives compensation in the form of property, such as stock, will be subject to ordinary income tax on the value of the property at the time of the receipt unless his interest is subject to a substantial risk of forfeiture, in which case tax would be imposed at the time the interest becomes non-forfeitable.

The Committee, however, adopted a series of relatively minor modifications, the most important of which are explained below:

(a) The House bill requires the recognition of income to an employee upon transfer even though the property remains subject to forfeiture. The Committee approved a a Treasury suggestion that in such a case, the employee would not be treated as realizing income merely because he donated his forfeitable interest to another person, if the other person is also subject to the forfeitable condition. However, the employee would be taxed at the time the rights become non-forfeitable.

(b) The Committee also adopted a provision which provides that an interest in property is not to be considered forfeitable unless the employer can compel the employee or other holder to return the identical property upon the happening of the events which caused the forfeiture. However, where the property is forfeitable, the employee would be treated as realizing income when he sells the property if this event occurs before the property becomes non-forfeitable. This provision was also recommended by the Treasury Department.

(c) The Committee adopted a provision which will permit employees the option of reporting the original receipt of restricted property as if the restriction did not exist. Stated otherwise, the employee could treat the receipt of restricted property as a receipt of unrestricted compensation and pay tax on it at that time. However, an employee who exercises this option, will not be entitled to a refund if subsequently his right to the property proves to have been forfeitable.

(d) The Committee also added provisions which provide that restricted property rules would not apply to premiums paid by an employer under non-trustee annuity plans for an employee which meet the qualification requirements of Internal Revenue Code Sec. 401(a). Also, the restricted property rules would not apply to any amount excluded from gross income (under Sec. 403(b)) in the case of annuities purchased for an employee by an educational or charitable (Sec. 501(c)(3)) organization. These provisions had been recommended by the Treasury Department.

(e) The Committee also adopted provisions to make it clear that in the case of non-exempt trusts and non-qualified annuities, the amount subject to tax when the employee's interest becomes non-forfeitable is the value at that time of his interest in the trust (or the value of the annuity contract). The value of the amount subsequently contributed by the employer to the trust (or premiums subsequently paid) would be included in the income of the employee when contributed or paid to the trust (or insurer). The Treasury Department had also recommended the adoption of these provisions.

(f) The Committee modified the effective date provision of the section. The general effective date included in the House bill provided that the section would not apply to property transferred after June 30, 1969, if the property was transferred before February 1, 1970, pursuant to a written plan adopted and approved before July 1, 1969. The Committee agreed to the July 1 date but at the suggestion of the Treasury Department, the Committee decided to allow more time for the actual transfer. Thus the February 1, 1970, cutoff date was extended until May 1, 1970.

The Committee also agreed that in the case of a company which has a binding contract prior to April 22, 1969, with third parties to pay key employees a determinable amount of stock each year, the property could continue to be transferred before December 31, 1972, under the rules of existing law.

Income Averaging. -- The Committee generally agreed to the provision in the House bill enlarging the class of taxpayers eligible for income averaging. Under the bill a person whose income for the year exceeds his average income for the prior four years by more than 20 percent may utilize the favorable averaging device. (Under existing law his current income must be one-third greater). However, the Committee was not willing to permit wagering income, capital gains, and income from gifts to be eligible for averaging, and so it deleted the provisions of the House bill which would have extended averaging to these types of income. This action reduced the revenue loss from this feature of the House bill from $300 million to $110 million on an annual basis.

Moving Expenses. -- The Committee agreed to the provision in the House bill which would liberalize the types of items which may be deducted by an employee who moves to accept employment at a new location. However, the Committee decided not to approve the feature of the House bill which would have denied the deduction unless the move covered more than 50 miles. Thus it retained the provision in existing law which allows the deduction for those moving more than 20 miles.

The Committee further agreed that the limitation of $2,500 should apply on a family basis. Stated otherwise, if a family made a move, then the family could only deduct up to $2,500 even though both the husband and the wife were employed.

The Committee also agreed that the deduction for moving expenses should be available to self-employed individuals. However, self-employed individuals would have to remain at the new location for a 78-week period instead of the 39-week period presently required for employed individuals.

Collection of Letters, Memorandums, etc. -- The Chairman reported that the Committee on Finance had also approved--at its Monday meeting--the provisions in the House bill which treat gain on the sale of letters, memorandums, and other papers by a person whose efforts created the property(or for whom it was prepared produced) as ordinary income rather than as capital gain.

By treating them as ordinary income assets, other provisions of the bill require that any appreciation in value of the papers, memorandums, etc., should be taken into account by the taxpayer in the event he chooses to contribute these documents to a library, university, or other charitable institution. However, the Committee modified the effective date so that the provisions of the House bill would apply to sales or other dispositions of these papers occurring on or after January 1, 1969, rather than after July 25, 1969.

Total Distributions from Qualified Pension and Other Plans. --The Committee agreed to the provision in the House bill which would limit the extent to which capital gains treatment would be allowed for lump-sum distributions from qualified employees' trust made within one taxable year. Thus, amounts attributable to employer contributions made during plan years beginning after 1969 will be treated as ordinary income. However, the Committee simplified the tax computation required under the House bill. Generally one-fifth of the employer contribution would be added to the taxpayer's other income, except that wages and salary received by the taxpayer during the year in which the lump-sum distribution is made and the capital gains portion of the lump-sum distribution would be omitted from the computation. Tax would be calculated in the usual manner for this one-fifth and the resulting amount would be multiplied by 5 to arrive at the tax due on the employer portion.

Subchapter "S" Corporations. -- The Committee agreed to the provision in the House bill which provides limitations similar to those contained in H. R. 10 plans with respect to contributions made by Subchapter "S" corporations to a retirement plan for those individuals who are "shareholder-employees." Under this provision, a shareholder-employee must include in his income the contributions made by the corporation under a qualified plan to the extent contributions on his behalf exceed 10 percent of his salary or $2,500-- whichever is less.

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PRESS RELEASE

FOR IMMEDIATE RELEASE
October 15, 1969

COMMITTEE ON FINANCE
UNITED STATES SENATE
2227 New Senate Office Building

TAX REFORM ACT OF 1969
ACTIONS IN EXECUTIVE SESSION

The Honorable Russell B. Long, (D., La.) Chairman of the Senate Committee on Finance announced today that the Committee was continuing to make good progress in its effort to complete action on the Tax Reform Act of 1969 by October 31. He reported that in executive session the Committee had reached decisions on a number of important tax reform provisions contained in the House bill, and had corrected defects in several of them. The complete action of the Committee is described in the following paragraphs:

Multiple Trusts; Accumulation Trusts. -- The Committee generally approved the provisions of the House bill which tax the beneficiary of accumulation trusts (including multiple trusts) in substantially the same manner as if the income had been distributed to the beneficiary when it was earned by the trust. However, it approved a series of amendments to correct certain defects in the House language.

(a) The definition of "distributable net income" was modified to include capital gains and dividends allocated by the trustee to the corpus of the trust, thereby preventing the use of trusts to accumulate these items at low rates to be distributed later to high-bracket taxpayers.

(b) The Committee agreed to apply an interest charge to the tax payments deferred by the use of accumulation trusts. This charge would be 6 percent of the tax involved for the period for which it is deferred, and would be assessed against the beneficiary who receives the accumulated income of the trust.

(c) The Committee decided to make the new rules for accumulation trusts applicable with respect to income accumulated in taxable years beginning after December 31, 1968 (rather than in taxable years beginning after April 22, 1969). Income accumulated in prior years will continue to be subject to the law in effect at the time the income was accumulated, except that the $2,000 deminimis exemption will not apply.

(d) The Committee modified the so-called "short-cut" method for computing tax upon the distribution of accumulated income in a number of relatively minor respects, the most important of which was a Treasury Department recommendation to prevent the creation of multiple trusts with staggered accumulation distributions in order to take advantage of the short-cut rule. This is accomplished by making the "short-cut" method inapplicable if during any of the preceding taxable years in which an accumulation distribution is deemed to have been made, prior accumulation distributions were also deemed to have been made by two or more other trusts to the same taxpayer.

Multiple Corporations. -- The Committee approved provisions in the House bill tightening the rules under which large groups of commonly controlled corporations have been able to obtain substantial benefits intended primarily for small business. The principal benefits are the \$25,000 corporate surtax exemption, the \$100,000 exemption from the accumulated earnings tax and the special additional first-year depreciation allowance. In approving the objective of the House bill, the Committee made the following modifications to the language:

(a) Five-year Phase-out. -- The Committee rejected the eight-year phase-out of these special tax advantages contained in the House bill and substituted a five-year transition period instead. However, the Committee delayed the effective date of the phase-out so that it would not commence until 1970. (The House bill would have become operative in 1969.)

(b) The Committee also approved a Treasury-suggested modification to prevent any part of a preconsolidation loss incurred by one member of a controlled group from being used to offset income of other members of the group until after the 5-year transition period referred to in paragraph (a). The House bill would have "phased-in" the allowance for these losses as it "phased-out" the other advantages. It also deleted references to controlled groups of mutual insurance companies in accordance with advice received from the Treasury that no such groups were in existence.

(c) The Committee also modified the bill to permit corporations which used surtax exemptions in the past to elect to shift immediately to a consolidated returns basis of tax reporting and to use loss carryovers within the group without reduction, if the group agreed to give up the multiple surtax exemptions it had claimed for the year the loss was sustained.

Treble Damages; S. 2631. -- On the Chairman's motion, the Committee approved the text of S. 2631 as an amendment to the tax reform bill. This bill would disallow a tax deduction for two-thirds of amounts paid as treble damages growing out of criminal violations of the antitrust laws. The disallowance would apply in the case of a conviction after December 31, 1969 in a criminal proceeding or in the case of a guilty plea or plea of nolo contendere entered after that date. The amendment also makes it clear that no deduction is allowable because of the payment to another person of bribes and other illegal kickbacks.

Foreign Tax Credits. -- The Committee deleted those provisions of the House bill (Sections 431 and 432) which would have reduced the foreign tax credits available to taxpayers with income from foreign sources.

However, the Committee did agree to add an amendment to the bill making it clear that for Federal tax purposes, the continental shelf of the United States is to be treated as part of the United States.

Stock Dividends. -- The Committee approved the portion of the House bill which taxes the recipients of stock dividends in those instances where one group of shareholders receives a distribution in cash and there is an increase in the proportionate interest of the group receiving the stock dividend. Before approving it, however, the Committee adopted an amendment to prevent avoidance of the House provision where a company had two classes of stock outstanding before the effective date of the provision but had not used them in a way which would give rise to a tax under the new rules. It amended the effective date provision in another respect also. Under this latter amendment a corporation which had two classes of stock outstanding on the effective date of the provision would be permitted to issue additional shares of stock of whichever class is the larger.

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PRESS RELEASE

FOR IMMEDIATE RELEASE
October 16, 1969

COMMITTEE ON FINANCE
UNITED STATES SENATE
2227 New Senate Office Bldg.

COMMITTEE DECISIONS
TAX REFORM ACT OF 1969
Five Percent Surtax Extension -- Financial Institutions

The Honorable Russell B. Long (D., La.), Chairman of the Senate Committee on Finance, announced today that the Committee was nearly a full day ahead of schedule in its effort to complete action on the Tax Reform Act of 1969 and order the bill reported to the Senate by October 31, 1969. By completing action on the portions of the bill which revise the tax treatment of financial institutions and by acting to extend the income tax surcharge at a 5 percent rate through June 30, 1970, the Chairman observed that some of the most difficult work of the Committee was now done. He expressed confidence that the Committee would finish its work in executive session and order the tax reform legislation reported by the agreed-upon date.

The full description of the Committee's decisions follows:

5 Percent Surtax. -- The Committee agreed with the House of Representatives and with the administration that the income tax surcharge should be extended for an additional 6-month period -- through the first half of 1970 -- at a 5 percent rate. Provisions to accomplish this result are already contained in the House bill. The extension of this surtax through June 30, 1970 involves $3.1 billion in additional revenue.

Financial Institutions. -- The Committee agreed with the House of Representatives that the tax benefits presently available to banks, savings and loan associations and mutual savings banks should be scaled down. However, the Committee concluded that rather than fix permanent rules for the future, as the House bill would do, it would be preferable to scale down the tax advantages in such a way that the matter can be reviewed again in a few years in the light of conditions as they exist at that time.

Commercial Banks. -- Under present law commercial banks are allowed to make tax-deductible additions to bad debt reserves up to 2.4 percent of their outstanding loans. The House bill would have substituted for this bad debt reserve treatment a new system under which future additions would have been based on the bank's actual loss experience calculated over a six-year period. The Committee on Finance decided that in lieu of the approach taken by the House it would be preferable to reduce the 2.4 percent ceiling on bad debt reserves to 1.8 percent. Banks with current reserves in excess of 1.8 percent would begin paying greater taxes in 1970 just as they would have under the House bill.

Savings and Loan Associations; Mutual Savings Banks . -- The Committee approved the provisions of the House bill repealing the so-called "three percent" method for computing additions to bad debt reserves of mutual thrift institutions.

It also agreed to reduce the special deduction of 60 percent of taxable income (for amounts added to bad debt reserves) to 50 percent over a four-year period. (The House bill would have reduced the 60 percent deduction to 30 percent over a ten-year period.) Under the Committee decision, the 60 percent limitation would be reduced to 57 percent in 1970, 54 percent in 1971, 51 percent in 1972 and finally to 50 percent in 1973.

The Committee also agreed that mutual savings banks and savings and loan associations in the future must allocate their dividend-received deduction between their taxable income and their additions to bad debt reserves. This action will reduce the incentive presently available to these institutions to invest in corporate stocks, report only 15 percent of their dividend income for tax purposes (since they are allowed an 85 percent deduction for the dividends they receive) and then deduct the entire amount either as interest paid to depositors or as additions to bad debt reserves.

Bonds Held by Financial Institutions . -- The Committee agreed to the provisions of the House bill which subject the gain realized on the sale of securities held by financial institutions (banks and mutual thrift institutions alike) to ordinary income tax rather than to the more favorable capital gains treatment. Losses on these bonds are presently deductible from ordinary income. However, the Committee provided a special transitional rule under which gain from bonds owned by the institution on July 11, 1969 (the same effective date as provided by the House bill) may continue to receive capital gains treatment if the gain is realized within five years. The House bill would have applied ordinary income tax to gain on bonds disposed of in taxable years beginning after July 11, 1969.

Foreign Deposits in U. S. Banks . -- The Committee agreed to the House provision extending until 1975 the period during which foreign persons may deposit non-business funds in U. S. banks without being taxed on the interest earned on these deposits. However, it also approved an amendment limiting the exemption where the foreign person deposits his money in a U. S. branch of a foreign bank to situations where the deposits were not "effectively connected" with a trade or business carried on in the United States.

P. R. #30

PRESS RELEASE

FOR IMMEDIATE RELEASE
October 17, 1969

COMMITTEE ON FINANCE
UNITED STATES SENATE
2227 New Senate Office Bldg.

TAX REFORM ACT OF 1969
Actions in Executive Session

Honorable Russell B. Long (D., La.), Chairman of the Senate Finance Committee, announced today that the Committee had reached further major decisions with respect to the Tax Reform Act of 1969. The important subjects before the Committee at today's executive session concerned the treatment of farm cooperatives and farm losses.

A complete explanation of the actions taken by the Committee follows:

Farm Cooperatives. -- The Committee deleted from the House bill the provisions which would have required farm cooperatives (1) to pay out in cash 50 percent (instead of 20 percent, as provided by existing law) of patronage dividends if they are to qualify for deduction, and (2) to redeem the patronage dividend within 15 years. The Committee noted that the House provisions would not have produced any additional revenue for the Federal Treasury.

However, in a related move, the Committee directed the staff to explore the possibility of taxing cooperative organizations on their income which is not related to the purpose for which the cooperative was created. This would enable the Committee to determine whether the competitive advantage available to cooperatives which engage in a profit-making business enterprise can be removed without jeopardizing the purposes for which cooperatives were granted a tax advantage.

A technical amendment was also approved to allow cooperatives 8-1/2 months after the close of the year to make cash payments of per-unit retain allocations and deduct them, thus conforming to the period presently allowable in the case of non-cash allocations.

In addition the Committee agreed to provide a 10-year carryback with respect to bad debts of the banks for cooperatives.

Rural Electric Cooperatives. -- The Committee also added to the bill an amendment which would require rural electric cooperatives to pay tax on the interest income they receive on Federal government obligations they own if they also have borrowed from the Federal government loans bearing a special low rate of interest.

Federal Land Banks. -- The Committee approved an amendment to terminate the Federal income tax exemption (first enacted in 1916) for Federal Land Banks over a 5-year transition period. This action should add approximately $12 million to Federal reserves.

Farm Losses. -- The Committee agreed with the House that the tax treatment of farm losses should be brought under greater control. However, it felt that the approach taken by the House was unnecessarily complicated. Accordingly, the Committee agreed to a substitute for the House provision. Under this substitute, an individual who has more than $50,000 of non-farm income and who incurs a loss from his farm operation of more than $25,000 (these are the same tests provided in the House bill) will be allowed to deduct currently only one-half of his farm losses in excess of $25,000 against his non-farm income. The remaining portion of his farm loss which would not be allowed as a deduction in the year it is incurred could be carried over for an indefinite period but could be used only to offset future farm income.

Under the Committee substitute, farm losses up to $25,000 could continue to be deducted in full against non-farm income but deductions in excess of $25,000 (where the taxpayer has non-farm income of more than $50,000) could be subject to an initial 50% disallowance.

Initially, the Committee substitute would produce more revenue for the Federal government than the House bill. This is so because the House bill allowed a full current deduction of farm losses but then recaptured at ordinary income tax rates the amount previously deducted when the farm property is sold at a capital gain.

Crop Insurance Proceeds. -- The Committee added an amendment to the bill (Amendment No. 243, Senator Miller (R., Iowa)) to provide that at his election a farmer whose crops have been destroyed and who receives crop insurance proceeds in compensation for his loss may elect to defer the immediate reporting of those proceeds for Federal income tax purposes until the year following the year of destruction, provided that is the year in which he would normally have reported the income from the sale of the crop if it had not been destroyed.

Holding Period for Livestock. --Under existing law livestock must be held for one year in order for the gain on its sale to qualify for favorable capital gains treatment. The House bill would have changed the holding period so that livestock must be held for at least one year after the animal would ordinarily have been used for draft breeding and dairy purposes. Because this test was difficult to apply in the case of many types of livestock the Committee approved an amendment under which horses and cattle must be held for at least two years in order to qualify for capital gains treatment. Other types of livestock would remain subject to the one-year holding period presently in existing law.

Livestock Depreciation Recapture. -- The Committee adopted the House bill provision which provides for the recapture of ordinary income tax rates of gain on the sale of livestock to the extent depreciation deductions had previously been taken with respect to purchase livestock and deduct it against ordinary income. Under present law, all the gain on the sale of livestock is treated as a capital gain.

Hobby Losses. -- Under the House bill, the hobby loss provision in existing law would be replaced with a rule which disallows the deduction of losses from an activity which is not carried on with a "reasonable expectation of profit."

The House bill presumed the activity to be carried on without an expectation of profit where the losses from the activity were greater than $25,000 in three out of five years. The Committee agreed with the House as to the desirability of tightening up on the deduction for hobby losses. However, testimony presented at the hearings indicated considerable difficulty could be expected from the subjective nature of the test applied by the House bill. For this reason, the Committee modified the House bill in such a way as to disallow losses with respect to an activity which the taxpayer is "not engaged in for profit."

The Committee also provided that if the taxpayer has profits in two out of five years from the activity in which he is engaged, he would be presumed to have engaged in that activity for profit and the Internal Revenue Service would be under a burden to rebut this presumption.

The Committee also approved technical amendments, the most important of which would assure the continued deductibility for items which would be deductible without regard to a trade or business. Items referred to include deductions for interest, State and local taxes, and long-term capital gains. In this same vein, the Committee agreed that even in the case of a hobby loss the expenses involved would be deductible to the extent of the income received from the activity.

Because concern has been expressed as to whether there would be a reasonable administration of this provision, the Committee expressed its intent that the Treasury should establish two advisory groups drawn from the cattle and horse industries to assist the Commissioner of Internal Revenue by examining the reasonableness of cases which agents would contemplate bringing under the new hobby loss provision. One advisory-agreed group would be concerned with livestock operations and the other with horse raising, breeding and racing operations. These advisory groups would be composed of industry experts and would examine and recommend action to the Service with respect to cases involving their industries. This action would precede the disallowance by the Internal Revenue Service of deductions of losses under this provision. This would assure taxpayers of a high level review of their cases by responsible representatives of their industry. This intent will be repeated in the Committee reports and the tax reform bill.

Medical Insurance; Medicare. -- The Committee approved an amendment which will be added to the bill to require that payments made under the Medicare and Medicaid programs and payments made by private medical insurance carriers must be reported to the Federal tax collector if they aggregate $600 or more during the year. This amendment would also require that the Department of Health, Education, and Welfare record transactions with respect to these programs on the basis of the individual's social security number. The payments which must be reported include those made directly to the health care practitioner who accepts an assignment from his patient and those for which a patient submits bills and is paid for services rendered by the health care practitioner. The amendment also requires that the Secretary of Health, Education, and Welfare submit an annual report to the Finance Committee and to the Ways and Means Committee, identifying each person paying a total of $25,000 or more under Medicare and Medicaid.

F.R. #31

PRESS RELEASE

FOR IMMEDIATE RELEASE
October 20, 1969

COMMITTEE ON FINANCE
UNITED STATES SENATE
2227 New Senate Office Bldg.

TAX REFORM ACT OF 1969
Accelerated Depreciation
Committee Decisions

The Honorable Russell B. Long, (D., La.), Chairman of the Committee on Finance announced today that the Committee had concluded its executive consideration of the portions of the House-passed tax reform bill dealing with the use of accelerated depreciation. He reported that the Committee was generally in agreement with the objectives of the House provisions and had approved the provisions restricting the use of accelerated depreciation in the case of real property to new residential property. However, in recognition of the goals fixed by the Housing Act of 1968, it had amended the bill to continue the present recapture rules for low and moderate income rental housing.

The full details of the Committee's actions are described in the following paragraphs:

Recapture of Excess Depreciation. -- The Committee adopted a suggestion by the Treasury Department that in the case of new residential housing the recapture rules of the House bill be relaxed. Under this suggestion gain, up to the entire amount of accelerated depreciation in excess of straight-line depreciation, would be recaptured at ordinary income tax rates if the property should be sold within 10 years. Thereafter, the amount recaptured at ordinary income tax rates would be reduced by one percentage point for each month the property is held beyond ten years. If the property is held for 18 years and 4 months all gain realized on its sale would be taxed as capital gains. (Under the House bill, the recapture rules would apply to the gain reflecting the full amount of the difference between accelerated depreciation and straight-line depreciation.)

Recapture on Sales of Low and Medium Income Housing. -- The Committee agreed to another Treasury Department suggestion under which the recapture rules of existing law would be retained without change for certain federally assisted projects such as the so-called FHA 221 (d)(3) and FHA 236 programs and for other publicly assisted housing programs under which the return to the investor is tightly limited. Under present law the gain, up to the full amount of the difference between accelerated depreciation and straight-line depreciation, would be recaptured at ordinary income tax rates if the property is sold within 20 months; thereafter the amount subject to recapture would be reduced by one percentage point for each additional month the property is held beyond 20 months.)

Recapture on Certain Dispositions. -- The Committee also agreed to an amendment which would retain the application of the existing recapture rules

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where the sale of the property was subject to a binding contract in existence prior to October 9, 1969, but where the transfer takes place after this date.

Foreign Real Estate. -- The Committee agreed to another amendment, also suggested by the Treasury Department, (but modified by the Committee), under which accelerated depreciation would be available in the case of construction of residential housing in foreign countries only to the extent that the foreign country allows accelerated depreciation on that housing.

Rehabilitation Expenditures. -- The Committee agreed to the provisions in the House bill which allow 5-year amortization of the costs of rehabilitating buildings for low-cost housing. However, it agreed to limit this amortization to expenditures made prior to January 1, 1975. This will provide time for the Congress to evaluate the effectiveness, and the cost, of this new incentive.

Depreciation Allowed Regulated Industries. -- The Committee adopted the sections of the House-passed bill which would enact new provisions relating to the use of accelerated depreciation by regulated industries. These provisions generally provide that as to existing property, if straight-line depreciation is presently being taken, then no faster depreciation may be used. However, if the taxpayer is taking accelerated depreciation and is normalizing, then accelerated depreciation can continue to be taken but only if the taxpayer continues to normalize. (The utility retains the current tax reductions resulting from the use of accelerated depreciation and uses this money in lieu of capital that would otherwise have to be obtained from equity investments or borrowing.) No change in the method of depreciation would be required if the taxpayer is now on flow-through. (Where the utility is earning the maximum allowed by law or regulations, the utility "flows through" the tax reduction resulting from the use of accelerated depreciation to the utility's current customers in the form of lower rates.) As to new property, a taxpayer presently on straight-line or presently on accelerated depreciation with normalization will be permitted to take accelerated depreciation on the new property only if the tax benefits are normalized. However, the taxpayer may continue to use flow-through on new property, if the taxpayer is now on flow-through insofar as the same kind of property is involved. The bill does not change the power of a regulatory agency, in the case of normalization, to exclude the normalized tax reduction from the base upon which the agency computes the company's maximum permitted profits.

The Committee made certain changes in the House-passed bill. The more important of these changes follow.

The Committee adopted a provision which will permit regulated taxpayers to elect within 180 days after the date of enactment of the bill to shift from a flow-through to the straight-line method. The regulated taxpayer could also shift to a normalization method if he is so permitted by the appropriate regulatory agency.

The Committee also deleted oil pipelines from the category of companies covered by the bill. Oil pipeline companies compete with non-regulated forms of transportation and are not guaranteed any specific rate of return. However, regulated steam producers were included within the provisions of the bill as well as Comsat.

The Committee also adopted a definition of normalization which provides that a regulated utility must not only normalize on their regulated books of account, but that these books of account must also be used as the basic source of information in setting the current rates to be charged to their consumers. Further, the Committee adopted a provision which provides that a taxpayer would not be treated as normalizing unless the entire deferral of taxes resulting from the difference between the depreciation expenses reflected in the regulated books of account and the accelerated depreciation deducted on their return is normalized.

The Committee also changed the date for determining the status of a company under the bill from July 22, 1969, to August 1, 1969 (the date the bill was introduced in the House and its specific provisions were made public). Further, the Committee adopted a provision which provides that the status of a company will be determined in the first instance by what was done on its income tax return for its most recent taxable year. In addition, regulated companies which have used accelerated depreciation (with flow-through) in computing their tax expenses on their regulated books of account for the latest monthly period ending on or before August 1, 1969, would be permitted to elect accelerated depreciation (with flow-through) for future acquisitions. Also, a utility which had filed a request before August 1, 1969, with the Internal Revenue Service, or with the appropriate utility commission, for permission to change from straight-line to accelerated depreciation would be permitted to make that change for such property and future acquisitions.

Earnings and Profits. -- The Committee adopted the provision of the House-passed tax bill which provides that for purposes of computing its earnings and profits, a corporation must deduct depreciation on the straight-line method, or on a similar method which provides for a ratable deduction of depreciation over the useful life of an asset. The provision would not affect the amount of depreciation that could be deducted in determining the corporation's income tax. However, the Committee adopted a change which would make it clear that this new rule would not affect foreign tax credits. The amount of the foreign tax credit which would be allowed a company would be computed as under existing law and would not be affected by this provision of the House-passed tax bill.

P. R. #32

PRESS RELEASE

FOR IMMEDIATE RELEASE
October 21, 1969

COMMITTEE ON FINANCE
UNITED STATES SENATE
2227 New Senate Office Bldg.

TAX REFORM ACT OF 1969
Capital Gains
Committee Decisions

The Honorable Russell B. Long, (D., La.), announced today that the Committee on Finance had concluded its work on that portion of the House tax reform bill dealing with the treatment of capital gains and losses. He reported that the Committee had substantially approved the restrictions contained in the House bill. However, he recalled that on October 10, the Committee had agreed to retain the 6-month holding period required before gain on the sale of the property could qualify for favorable capital gains treatment. (The House bill would have extended the holding period to one year.)

Senator Long also reported that Secretary George Romney of the Department of Housing and Urban Development had prevailed upon the Committee to consider further a suggestion he had made to encourage investments in low and moderate housing. The suggestion had been explored, but not approved, at Monday's meeting of the Committee. Following the Secretary's presentation, the Committee approved his suggestion.

A complete description of the actions taken at today's meeting follows:

Low and Moderate Income Housing

Tax-Free Reinvestment. -- As noted above, the Committee approved an amendment to the provisions of the House bill relating to the real estate industry. This amendment, recommended by the Department of Housing and Urban Development would permit a taxpayer who invests in low-or medium-income housing to sell the property and pay no current tax on the gain involved, provided (1) he sells the property to the occupants or to a tax-exempt organization which manages the property, and (2) the full proceeds from the sale are reinvested in other government-assisted housing. In such a case the taxpayer's basis for the old property, to the extent the proceeds are re-invested in similar property, will be carried forward and become a part of his basis for the new property.

CAPITAL GAINS

25 Percent Maximum Rate. -- The Committee generally agreed with the objective of the House bill in repealing the present 25 percent maximum rate on capital gains. However, it felt that taxpayers with relatively small amounts of capital gain should continue to be eligible for the 25 percent maximum rate. Accordingly, it provided that married couples could continue to apply this rate in the case of gains up to $140,000 ($85,000 for single persons), provided they did not have "preference" income of more than $10,000. (The Committee has not yet taken up that part of the House bill concerned with the limit on tax preference, and for this reason, no announcement as to the items constituting "preference" income is being made at this time).

The Committee further agreed to move the effective date for the higher capital gains rate to December 31, 1969 (it was July 25, 1969 under the House bill), and to phase it in over a three-year period. While the exact amount of the increase will not be finally determined until the Committee has reviewed the rate reduction provisions, based upon the rate structure contained in the House bill the phase-in would be as follows:

1969 - 27.5% (including the surtax),
1970 - 29.5%,
1971 - 31%,
1972 - 32.5%

Alternative Tax for Corporations. -- The Committee agreed to adopt the provision of the House-passed tax bill which would increase the alternative tax rate for a corporation's net long-term capital gains from 25 percent to 30 percent. The effective date of this change will also be December 31, 1969 and, as in the case of the alternative 25 percent tax rate for individuals, this higher tax will also be phased-in. However, the phase-in in the case of corporations will involve only 2 years. The rates applicable during this period are:

1969 - 27.5%
1970 - 29.0%
1971 - 30%

Transitional Rules. -- In addition to the date change and the phase-in, described above, the Committee agreed to adopt several transitional rules which will apply both to the alternative tax for individuals and the alternative tax for corporations. The Committee agreed to a transitional provision which provides that capital gains arising from sales or other dispositions under binding contracts that were in effect on or before October 9, 1969, would be taxed under present law. This binding contract rule would not apply, however, in certain cases of gain from timber, coal, or domestic iron ore which is taxed as a capital gain under section 631 of the Internal Revenue Code. Further, the Committee adopted a provision which would except a capital, or liquidating, distribution from a corporation which was made under a plan adopted prior to October 9, 1969.

The Committee further adopted a provision which clarifies the status of installment payments received after 1969 but which relate to sales made on or before October 9, 1969. This new provision provides that such installment payments would be taxed at the maximum alternative rate of 25 percent until the sale price is paid off.

Capital Losses of Individuals. -- The Committee adopted the provisions of the House-passed tax bill relating to capital losses of individuals. This provision provides that only 50 percent of an individual's long-term capital losses may be offset against his ordinary income. In addition, the deduction of capital losses against ordinary income for married persons filing separate returns would be limited to $500 for each spouse. The Committee did, however, change the effective date of this provision. Under the Senate version, this provision would be effective for taxable years beginning after December 31, 1969 (the House bill would have applied to taxable years beginning after July 25, 1969).

Sales of Life Estates. -- The Committee also adopted the provision of the House-passed tax bill which relates to the sales of life estates. In general, this provision provides that the entire amount received on the sale or other disposition of a life (or term of years) interest in property, or income interest in trust (whether acquired by gift, bequest, inheritance, or by a transfer in trust), is to be taxable without any reduction for the taxpayer's basis. Presently, only the excess of the amount received over the seller's basis is taxed. The Committee, however, did change the effective date for the provision. Under the Senate version, this provision would become effective as to sales or other dispositions after October 9, 1969 (the House bill would have applied with respect to sales or other distributions after July 25, 1969).

Casualty Losses Under Section 1231. -- The Committee further adopted the provisions of the House-passed tax bill which change the tax treatment of certain casualty losses. The Committee did provide that the provision would include casualty gains and losses on personal capital assets. Personal capital gains and losses were not included within the House bill. Further, the Committee changed the effective date of this provision to years beginning after December 31, 1969 (the House bill would have applied with respect to taxable years beginning after July 25, 1969).

Transfer of Franchises. -- The Committee adopted the provisions of the House-passed tax bill relating to transfers of franchises. However, the Committee added additional rules to the provisions to help distinguish between those cases when the transfer of the franchise is to be treated as a sale as contrasted with when the transfer is to be treated as a license. In addition, the Committee adopted rules for the tax treatment of the franchisee which would be consistent with that treatment given to the franchisor. Further, the Committee provided that the section would apply to trademarks and trade-names as well as franchises. Under the Committee version this section would apply to transfers made after December 31, 1969. However, present franchisees who are otherwise eligible for the more liberal rules included in this provision could elect to come under this new provision, rather than continuing to be taxed in accordance with present law. Finally, the Committee agreed to exclude professional sports from the application of these new rules.

Collections of Letters, Memorandums, etc. . -- This matter was dealt with by the Committee on October 13, 1969. See press announcement of October 14, 1969.

Holding Period of Capital Assets. -- This matter was dealt with by the Committee on October 10, 1969. See press announcement of that date.

Total Distributions from Qualified Pension and other Plans. -- This matter was dealt with by the Committee on October 14, 1969. See press announcement of that date.

PR #33

PRESS RELEASE

FOR IMMEDIATE RELEASE
October 23, 1969

COMMITTEE ON FINANCE
UNITED STATES SENATE
2227 New Senate Office Bldg.

TAX REFORM ACT OF 1969
Natural Resources
Committee Decisions

The Honorable Russell B. Long (D., La.), Chairman of the Committee on Finance, announced today that the Committee on Finance had concluded its work on that portion of the House tax reform bill dealing with the treatment of natural resources. The important question in this area concerned the 27-1/2 percent allowance for depletion of oil and gas wells. The Chairman reported that the Committee had resolved this matter by reducing the allowance to 23 percent.

A complete description of the actions taken at today's meeting follows:

Oil and Gas. -- The Committee agreed to reduce the percentage depletion rate for oil and gas from the present rate of 27-1/2 percent to 23 percent, with respect to both domestically and foreign produced minerals. The House-passed bill would have reduced the percentage depletion rate for oil and gas produced in the United States to 20 percent, and would have repealed it entirely for oil and gas produced in foreign countries.

The Committee also agreed that in the case of oil and gas producers with less than $3 million of gross income from oil and gas production the present limitation on the allowance for depletion -- 50 percent of the net income from the property -- will be increased to 65 percent. The House bill did not deal with this matter.

Other Minerals. -- The Committee agreed that in the case of all other minerals, the provisions of the House bill, which would have reduced the applicable depletion allowances by approximately one-fourth, should be deleted. This action had the effect of retaining the depletion allowances provided by present law. These allowances range from 5 percent for sand and gravel to 23 percent for uranium and sulphur and for certain strategic minerals.

Special Limitation on Depletion for Gold, Silver and Copper. -- Under present law the allowance for percentage depletion is based upon a specified percent of gross income from the mineral property, except that the deduction could not exceed 50 percent of the net income from that mineral property. In addition to the change described above in the case of small oil and gas producers, the Committee agreed that with respect to gold, silver and copper, the 50 percent limitation should be increased to 70 percent.

Great Salt Lake. -- The Committee further agreed to an amendment clarifying the treatment, for percentage depletion purposes, of minerals extracted from saline lakes within the United States. Under present law, percentage depletion is not allowed with respect to minerals extracted from sea water or from "similar inexhaustible sources." This latter phrase has been interpreted to prevent a depletion allowance for minerals extracted from the Great Salt Lake. The Committee amendment provides that except for salt and water the regular allowances will be provided for minerals extracted from the Great Salt Lake and other saline lakes in the United States.

Mineral Production Payments. -- The Committee approved the provisions of the House bill which restrict the tax benefits of carved-out production payments and so-called ABC transactions. However, it moved the effective date from April 22, 1969 to October 9, 1969 and provided two transitional rules. The first of these would permit a taxpayer who had sold a production payment in 1968 to elect to treat that transaction as a loan in the same manner as a production payment sold after the effective date. Under the second transitional rule the Committee provided that except for percentage depletion and foreign tax credit purposes, the new provision would not apply to carved-out production payments sold during that part of the taxpayer's taxable year which occurs after October 9, 1969, to the extent that the production payments offset a net operating loss which would otherwise occur in the taxable year in the absence of the carve-out. In this latter case, however, the amount of the carved-out payments qualifying for this treatment would not be allowed to exceed the amount of carved-out payments sold by the taxpayer during his preceding taxable year.

Mining Exploration Expenditures. -- The Committee agreed to adopt the provisions of the House-passed tax bill relating to mining exploration expenditures. This provision amends present law to provide that insofar as future mining exploration expenditures are concerned, the general recapture rules will apply in all cases. However, the Committee provided that this provision would be applicable only to mining exploration expenditures made after December 31, 1969. The House bill would have applied to mining exploration expenditures made after July 22, 1969.

Further, the Committee provided that taxpayers who have elected to deduct mining exploration expenditures under the limited provision of present law will be deemed to have made an election, with respect to expenditures made after December 31, 1969, to deduct the expenditures under the unlimited provision, unless the taxpayer notifies the Treasury that he does not desire to be so treated. The Committee also agreed that it would clarify the treatment of expenditures which are incurred during the development or producing stage of a mine. The intention of the Committee was that a taxpayer should deduct all expenditures incurred in bringing a mine into production, either as exploration expenditures during the exploration stage, or as development expenditures or operating expenses during the development and production stage. The Internal Revenue Service has at times taken the view that these expenditures are not to be treated as development or operating expenses, but rather, they are to be treated as exploration expenditures which must be capitalized, since they are incurred after the development stage of the mine has been reached. The Committee will make it clear that this is not the position it intended in enacting the law.

Oil Shale. -- The Committee also agreed to adopt the provisions of the House-passed tax bill relating to treatment processes in the case of oil shale. The effect of the House bill generally is to extend the point at which percentage depletion is computed in the case of this mineral to the point at which the oil is extracted from the rock. (Under present law percentage depletion is computed generally on the basis of the value of the shale as it comes from the mine.)

P.R. #34

PRESS RELEASE

FOR IMMEDIATE RELEASE
October 24, 1969

COMMITTEE ON FINANCE
UNITED STATES SENATE
2227 New Senate Office Bldg.

TAX REFORM ACT OF 1969
Minimum Tax
Committee Decisions

The Honorable Russell B. Long (D., La.), Chairman of the Committee on Finance, announced today that the Committee had adopted a new comprehensive minimum tax to apply to both individuals and corporations with tax preference income which now escapes Federal tax. He reported that the new provision replaces the limit on tax preferences and the allocation of deductions features of the House-passed Tax Reform Act. The Chairman noted that these House provisions were unusually complex in their operation and had been sharply criticized during the month-long hearings on the tax reform bill. He stated that the Finance Committee substitute not only was far simpler than the House provisions but also produced more revenue, in large part because of its extension to corporations.

Senator Long also reported that the Committee had approved the House language extending the 7 percent excise tax on passenger automobiles, and the 10 percent excise tax on telephone services for another year. He noted that the Committee had previously taken identical action when it reported H. R. 12290 to the Senate in July. The full description of the Committee's action follows:

5 Percent Minimum Tax. -- The Committee approved a substitute for the Allocation of Deduction Rule and the Limit on Tax Preferences provision of the House bill. The substitute involves the imposition of a 5 percent tax on preference income in excess of $30,000.

Under the Finance Committee provision, individuals and corporations would total their tax preference income, subtract an exemption of $30,000 and apply a 5 percent rate to find the minimum tax. (For married couples filing separate returns the exemption would be $15,000.) This minimum tax would be in addition to the regular individual income tax, and the regular corporation income tax.

Tax Preference Income. -- The minimum tax under the Finance Committee provision applies to a total of twelve tax preference items. The covered tax preference items are as follows:

(1) Capital Gain. -- One-half of long-term capital gains of individuals. In the case of corporations, the tax preference is three-eighths of long-term capital gains (based on the difference between the 30 percent rate that would apply to long-term capital gains and the 48 percent corporate tax rate.)

(2) Accelerated Depreciation. -- The excess of accelerated depreciation (or amortization) over straight-line depreciation on:

a) Real property;
b) Section 1245 property (equipment and machinery) where the property is leased on a net lease basis;
c) Property receiving 5-year amortization for rehabilitation expenses;
d) Anti-pollution facilities which would qualify for 5-year amortization under section 704 of the bill; 1/
e) Railroad rolling stock which would qualify for rapid amortization under section 705 of the bill. 1/

(3) Intangible Drilling and Development Expenses. -- The excess of intangible drilling expenses over the amount that would be recovered through straight line depreciation and cost depletion.

(4) Percentage Depletion. -- The excess of percentage depletion over cost depletion.

(5) Western-Hemisphere Trade Corporations. -- The tax savings received by Western Hemisphere corporations because their income is taxed at 34 percent instead of the 48 percent regular corporate income tax rate.

1/ The Committee has not yet taken up that part of the Tax Reform Act which provides for this amortization. The final decision on the inclusion of these items in the minimum tax will depend on the Committee's decision with respect to the sections providing the amortization.

(6) Financial Institutions; Bad Debt Reserves. -- Bad debt deductions of financial institutions in excess of actual loss experience.

(7) Investment Interest. -- Interest on indebtedness incurred to purchase, or carry investment property to the extent that such interest exceeds the net investment income received and reported as ordinary income during the year.

(8) Stock Options. -- The difference between the option price and the fair market value of qualified stock options at the time the option is exercised.

Exceptions From Tax Preference Income. -- The 5 percent minimum tax does not apply to tax exempt interest on State and local bonds, unrealized appreciation in the value of property deducted as a charitable contribution, and farm losses.

Treatment of Losses. -- If a taxpayer sustains a loss or has loss carryovers or carrybacks to the taxable year, then he may elect to offset the loss against the preference income used in the minimum income tax computation. However, to the extent he uses the loss to offset preference income then the loss may not later be used in the regular tax computation.

Revenue Effect. -- This new minimum tax would increase revenues by an estimated $700 million a year with about half the additional revenue coming from individuals and half from corporations.

Excise Tax on Autos and Communications. -- The Committee also approved a provision to continue the 7 percent manufacturers automobile excise tax until January 1, 1971. In addition, the reductions in the automobile excise tax scheduled under present law for future years are postponed for one additional year in each case. Similarly, the Finance Committee's action provided for the continuation of the communication services tax on local and toll telephone, and teletype writer exchange services. The present 10 percent tax on these items will be continued until January 1, 1971, and future scheduled reductions will occur one year later than provided under present law.

P R E S S   R E L E A S E

FOR IMMEDIATE RELEASE
October 27, 1969

COMMITTEE ON FINANCE
UNITED STATES SENATE
2227 New Senate Office Bldg.

TAX REFORM ACT OF 1969
Private Foundations
Committee Decisions

The Honorable Russell B. Long (D., La.), Chairman of the Committee on Finance, announced today that the Committee had reached further major decisions with respect to the Tax Reform Act of 1969. The subject before the Committee at today's executive session concerned the treatment of private foundations. The Chairman stated that the principal decision reached by the Committee would p'ace a time limitation on the life of private foundations, which are not operating foundations. Under this action private foundations would have to dispose of their assets for charitable purposes, or to a public charity, and terminate existence within forty years. For foundations currently in existence, this new rule would require that they terminate not later than the year 2009.

A complete explanation of the actions taken by the Committee follows:

Limitation on Life of Foundations. -- The Committee adopted an amendment to limit the life of a private non-operating foundation to forty years. (Existing foundations could continue in existence forty years from the date of enactment of the bill.) By the end of the forty-year period, the foundation must either become a public charity or an operating foundation or it must distribute all its assets to a public charity or an operating foundation.

Tax on Investment Income. -- The Committee agreed to delete the portion of the House bill which provides for a 7-1/2 % tax on private foundations' net investment income, and to assert in its stead a tax of 1/5 of 1% based on the fair market value of the assets held by the foundation, or $100, whichever is greater. In doing so, the Committee indicated that the tax generally was intended as a supervisory fee to provide funds for proper administration of the Internal Revenue Code provisions relating to exempt foundations.

Prohibition on Self-dealing. --The Committee generally adopted the provisions of the House bill relating to self-dealing between a private foundation and "disqualified persons."

Substantial Contributor. -However, it amended the House bill by changing the definition of a "substantial contributor" to a person who contributes $5,000 or more than 2% of the total contributions previously made to the foundation, whichever is higher. In the case of a husband and wife their contributions would be treated as one unit.

Transitional Rules; Leases and Loans; Shared Facilities. -- The Committee also adopted a transition rule in the case of leases and loans outstanding on October 9, 1969. Where the terms of the lease or loan is at least as favorable to the private foundation as it would be in an arms-length transaction, then the self-dealing rules would not be applicable for ten years from the date of the enactment of the bill. The Committee further agreed that where goods, services, or facilities are shared by disqualified persons and a private foundation under an arrangement in existence on October 9, 1969, which is beneficial to the private foundation, such an arrangement will not be subject to the self-dealing rules .

for a period of ten years from the effective date of the bill. This period will allow time for foundations to revise existing arrangements.

<u>Sales Commissions</u>. -- In cases where a private foundation is permitted to sell stock to a disqualified person in order to comply with the divestiture rules the Committee indicated that this would not be self-dealing even if the sale price is reduced by the amount of the sales commissions which would have to be paid if the stock were sold in the open market.

<u>Attribution Rules; Brothers, Sisters, Partners</u>. -- The Committee decided to remove brothers and sisters of substantial contributors and their decendents from the category of disqualified persons. It also agreed to remove partners of substantial contributors from the disqualified persons category unless their profits interest was 20% or more.

<u>Penalties.</u> -- The Committee agreed to change the treatment of foundation managers who "knowingly" violate the self-dealing requirements of the House bill so that (1) the Internal Revenue Service would be permitted to waive the penalty where it finds that the foundation manager's violation is not wilful and is due to reasonable cause, and (2) the burden of proving the "knowing" violation would be upon the Internal Revenue Service to the same extent as in the case of civil fraud under present law.

<u>State Litigation, Abatement of Federal Tax.</u> -- The Internal Revenue Service would be authorized to abate Federal taxes imposed on private foundation (except the 1/5 of one percent supervisory tax), where it finds that the action by a State Attorney General to correct the violations satisfies the requirements of the bill.

<u>Stock Transactions</u>. -- The Committee also agreed that it should be made clear that self-dealing may occur without the transfer of money or property between the private foundation and the disqualified person. For example, it would be self-dealing where stock is bought and sold by the Foundation in order to manipulate the stock's price for the benefit of the disqualified person.

<u>Distribution of Income</u>. -- The Committee generally approved the rules in the House bill relating to the distribution of income. However, it agreed to the modifications listed below:

<u>Phase-in of Five Percent Payout</u>. -- The Committee accepted the 5% payout requirement contained in the House bill, but allowed a transition period by providing that only 3-1/2% need be paid for 1972, 4% for 1973, 4-1/2% for 1974 and 5% for 1975 and following years. In taking this action the Committee noted further that the payout requirement could be satisfied by distributions of cash or other assets.

Distributions of Income. -- (Continued)

Deficiency Distributions. -- The Committee decided to permit foundations to make deficiency distributions where they have not met the 5 percent pay-out requirement because of an incorrect valuation of assets that is not willful and is due to reasonable causes. This would avoid the payment of penalties in situations where the action was inadvertent.

Twelve-Month Pass-Through. -- The Committee adopted a recommendation to amend the House bill by treating as a qualifying distribution a payment made by a private foundation to a private operating foundation or to another private foundation (even though controlled by the distributing foundation), if the money is spent or used for charitable purposes within one year of its receipt by the controlled organization. The donee organization would not be permitted, however, to pass the grant through to another private, non-operating foundation.

Expenses. -- The Committee adopted a proposal which would treat as a qualifying distribution the supervisory tax imposed on investment income and the unrelated business income tax. This would reduce the amount that the foundation would otherwise have to distribute currently for charitable purposes. The Committee also provided that it should be made clear that the administrative expenses of operating a foundation should also be treated as a qualifying distribution.

Controlled Organization. -- The Committee agreed to make it clear that a recipient organization is considered as "controlled" when disqualified persons of the granting foundations can, by aggregating their votes or positions of authority, require the organization to make a distribution or prevent it from making such a distribution. In adopting this rule, the Committee pointed out that if an organization has been created by several private foundations, all of which are independent of one another, none of the creating foundations would be said to control the other organizations, if each creating foundation has an equal vote on the Board of Trustees of the new foundation and the Board proceeds to operate the organization by majority vote.

Repayments of Prior Distributions. -- The Committee adopted a rule that where a private foundation receives money or assets as a result of previous expenditures made by the foundation that were treated as qualifying distributions (e. g., student loans), such monies or assets will be considered income for minimum distribution purposes.

Transition Rule for Commitments. -- The Committee agreed that where a private foundation had made a written commitment by October 9, 1969, that is binding upon it to make a grant to a non-controlled, non-operating private foundation, it will be allowed to treat the grant as a qualifying distribution if it is made to carry out the charitable, educational, or other purpose for which the organization is exempt. This rule would not operate to allow grants to be treated in this manner for a period any longer than five years from the date of the enactment of the bill.

Limitation on Use of Assets. -- The Committee approved those provisions in the House bill forbidding a private foundation from investing its corpus in such a manner as to jeopardize the carrying out of its exempt purposes. However, it made the following modifications in these provisions of the House bill:

Sanctions. -- The Committee decided to adopt an initial sanction on private foundations of five percent of the amount involved and an initial tax on the foundation manager, where he knowingly jeopardizes the carrying out of the foundation's exempt purposes, of

Sanctions . -- (Continued)

five percent (up to a maximum of $5,000). It also agreed to a second level sanction, where the jeopardy situation is not corrected, of 25 percent on the foundation and five percent on the foundation manager who refuses to take action to correct the situation. (In the case of the foundation manager, the sanction cannot exceed more than $10,000.) In adopting these rules for the tax on the foundation and the manager, the Committee provided that, before the second-stage sanction is imposed, the State Attorney General should be given an opportunity to intervene in the case to exercise whatever powers he has to correct the situation. Where the situation is corrected, the second-level sanctions would not be imposed.

Program-Related Investment . -- The Committee made it clear that a program-related investment -- such as low-interest or interest-free loans to needy students, high-risk investments in low-income housing, and loans to small business where commercial sources of funds were unavailable -- should be considered as being charitable expenditures and not investments which might jeopardize the foundation's carrying out of its exempt purposes. However, in order to qualify as a program-related investment treated in this way, the investment must be for charitable purposes and not for any major purpose of making profit for the foundation.

Limitation on Foundation Activities . -- The Committee accepted the provisions of the House bill with certain modifications.

Voter Registration Drives . -- It decided to delete that portion of the bill which would allow private foundation funds to be used for voter registration drives.

Lobbying . -- It also adopted a recommendation which, in effect, would use the tests applied under the present law respecting the influencing of legislation, except that it would drop the test of "substantiality," now in use. Hence, lobbying activities -- both grassroots lobbying and the buttonholing of Government officials -- would be prohibited. However, examination of broad problems that the Government would ultimately be expected to deal with would not be prohibited, although lobbying on matters that have been proposed for legislative action would still be forbidden. Also, the Committee's decision would permit the offering of advice and technical assistance in response to written governmental requests.

Educational Broadcasting . -- The Committee noted that in establishing the rules respecting attempts to influence legislation, where non-commercial educational television and radio stations are involved, adherence to the FCC regulations and the "fairness doctrine" (which require balanced, fair, and objective presentations of issues and which forbid editorializing by such broadcasting stations), will constitute compliance with the provisions of the bill. Under this rule a private foundation would be able to make grants to non-commercial educational television and radio without any sanctions being applied under this provision.

Expenditure Responsibility . -- The Committee accepted a recommendation that the provision of the House bill which places "expenditure responsibility" on private foundations be clarified so that it will not be interpreted as making the granting foundation an insurer of the activities of the recipient organization, so long as the private foundation making the grant uses reasonable efforts and establishes adequate procedures so that the funds will be used for proper charitable purposes.

<u>Sanctions</u>. -- With respect to the sanctions imposed in the House bill on certain prohibited activities, the Committee agreed to provide an initial tax on the foundation of ten percent of the amount improperly spent and a second tax of 100 percent if the foundation failed to correct the earlier improper action. The Committee also decided that the initial tax on a foundation manager who knowingly made the improper expenditure should be 2-1/2 percent, up to a maximum of $5,000, and the second tax should be 50 percent of the amount involved, if the manager refused to correct the earlier action.

<u>Prizes and Awards</u>. -- The Committee decided to allow private foundations to make a grant to an individual in the form of a prize or award if the individual is selected from the general public on the basis of merit or unusual achievement. Under the House bill, awards could only be made to individuals in the form of scholarship or fellowship grants, or where the purpose of the grant is to achieve certain objectives such as the production of a report or improvement of certain skills.

<u>Individual Grants</u>. -- The Committee decided to add to the provisions of the House bill permitting individual grants for various purposes an additional category of "teaching skills." It did not change the rule that the grant procedure must be approved in advance by the Internal Revenue Service.

<u>Influencing the Outcome of Any Public Election</u>. -- The Committee decided to amend the language of the House bill which would prohibit expenditures "to influence the outcome of any public election." The Committee limited the language to any <u>specific</u> public election because it recognized that almost any statement or study or general educational activity might become an issue in an election at some future time. Under the Committee action, preparation of any materials designed to favor or hinder any particular candidate for public office or any particular viewpoint in the case of referendum would still be prohibited.

<u>CHARITABLE CONTRIBUTIONS</u>

<u>Appreciated Gifts -- Tangible Personal Property</u>. -- The Committee reconsidered an earlier vote with respect to charitable contribution deductions for gifts of appreciated tangible personal property (see press announcement of October 13, 1969). Upon reconsideration, the Committee removed gifts of tangible personal property -- art objects, paintings, etc. -- from the types of property the appreciation in value of which would have to be taken into account by the donor in computing his charitable contribution deduction. (Under the House bill, the donor of such property must either (a) reduce his charitable contribution deduction to the amount of his tax basis for the gift property, or (b) claim a charitable contribution deduction for the full fair market value of the property and include the amount of appreciation in value in his gross income for tax purposes.) This Committee amendment would not apply, however, unless gain from the sale of the appreciated asset would have been taxed as a long-term capital gain. This rule would allow a donor to continue to contribute works of art to museums, educational institutions, etc., and compute his deduction under the rules of present law.

P. R. #26

PRESS RELEASE

FOR IMMEDIATE RELEASE
October 28, 1969

COMMITTEE ON FINANCE
UNITED STATES SENATE
2227 New Senate Office Bldg.

TAX REFORM ACT OF 1969
Private Foundations - Part II
Committee Decisions

The Honorable Russell B. Long (D., La.), Chairman of the Committee on Finance, announced today that the Committee on Finance had concluded its work on that portion of the House tax reform bill dealing with the treatment of private foundations and other tax-exempt organizations. He reported that the Committee had generally approved the provisions of the House bill with respect to tax exempt organizations, but made some important changes in defining "private foundations" and "private operating foundations" and also in the Excess Business Holdings provisions.

A complete description of the actions taken at today's meeting follows:

PRIVATE FOUNDATIONS

Disclosure and Publicity Requirements.--The Committee generally adopted the provisions of the House bill which recognize the need for more current information, from more organizations which could be made readily available to the public, including State officials. It did amend the rules in some respects, however, as set forth below:

Filing Requirement - Churches and Smaller Organizations.--The Committee agreed to exempt churches from the requirement of filing annual information returns in view of the traditional separation of church and state. However, where the church is engaged in an unrelated business, it would still be required to file an unrelated business income tax return. Also exempted from the filing requirements were organizations that have gross income of $5,000 or less, where the organization is not required to file an information return under present law. These include local chapters and smaller "public-type" organizations, such as the Boy Scouts, garden clubs, etc. In addition to the two categories mentioned above, the Secretary could exempt other organizations from the filing requirements if he concluded that the information which would be obtained was not of sufficient value to require filing.

Public Disclosure.--The Committee adopted a recommendation that the names of substantial contributors not be disclosed to the public in the case of exempt organizations other than private foundations.

Such organizations would still be required to disclose these names to the Internal Revenue Service.

Change of Status. -- The Committee adopted the provisions of the House bill which relate to notification to the Treasury by new exempt organizations and the treatment of existing private foundations, with the following changes:

Exceptions. -- It agreed that churches would not be required to apply for exempt status in order to be tax exempt, nor would they be required to file with the Internal Revenue Service to avoid classification as a private foundation. It also decided that public educational or charitable organizations need not obtain exemption certificates or file for status as a non-private foundation where their gross income is $5,000 or less. Under the House bill, the Treasury Department may exercise its discretion in exempting other classes or organizations, where this could be done without interfering with efficient administration.

Operation as a Public Charity. -- Under the House bill a private foundation may change its status after five years if it distributes all of its property to a public charity or itself acts as a public charity for at least five consecutive years. The Committee adopted a recommendation that would treat a private foundation as a public charity during the entire five-year period involved, if it indicated that it would operate as a public charity for all five consecutive years. It provided that if the organization failed to act as a public charity any time during the five-year period it would then lose its status as a public charity.

Definition of Private Foundation. -- In adopting the provisions of the House bill respecting the definition of a private foundation, the Committee made several important changes:

Support. -- Because the definition of a private foundation contained in the House bill depends, in whole or in part upon the proportion of support received from public sources, the Committee believed that a definition of "support" should be added. It adopted the definition contained in the current regulations modified to include amounts received from the exercise or performance by an organization of its exempt purpose or functions. The present regulations indicate that support means all forms of support, including contributions, investment income, and net income from an unrelated trade or business.

In defining the one-third of the organization's support which must come from the public, the bill specifies that amounts received from any "person" which are in excess of one percent of the organization's support will not be considered as coming from the public. The Committee decided to include the greater of one percent or $5,000 in public support. The term "person" as defined in the Internal Revenue Code does not include governmental units so that under the House bill an organization which has only one contributor whose support comes from government contract work might avoid classification as a private foundation. The Committee agreed that amounts received from Government contracts be included in the public support test, only to the extent that they do not exceed the one-percent or $5,000 test described above.

Foreign Foundations. -- The Committee agreed that an organization which is formed outside the United States that meets the definition of a private foundation will be considered as being subject to the rules applicable to private foundations and to private operating foundations.

Foundations Related to Certain Publicly-Supported Exempt Organizations. -- The Committee adopted the rule that a foundation operated in conjunction with a publicly-supported exempt organization (such as social welfare organizations, labor and agricultural organizations, business leagues, real estate boards, etc.), will be treated as meeting the public support test for purposes of being a public charity and would not be a private foundation.

Definition of Operating Foundation. -- The Committee generally approved the provisions of the House bill which define "operating foundation". (These are organizations to which qualifying distributions may be made by other private foundations. They are not subject to the 5 percent minimum pay-out requirement and are required to expend their entire income. In addition, they qualify for the 50 percent charitable contribution deduction.) One of the tests in the House bill (and in existing law) relating to operating foundations would require that substantially more than half of the assets of the foundation be devoted directly to the active conduct of the activities for which it is organized or to "functionally related" businesses. ("Substantially more than half" was described in the House Committee report as being 65 percent.) To provide relief for those types of organizations which could not meet this test because the type of activity is such as not to require large holdings of operating assets (as in the case of a research organization), the Committee adopted a rule which would permit an organization to qualify as an operating foundation where its endowment, based upon a 4 percent rate of return, is no more than adequate to meet its current operating expenses.

Hospitals. -- The Committee deleted that portion of the House bill which provides that hospitals are to have the same status as churches, educational institutions, and public charitable organizations for purposes of tax exemption, charitable contributions, and other matters. The Committee decided to reexamine this matter in connection with pending legislation on Medicare and Medicaid.

Effective Dates. -- The Committee adopted a series of changes with respect to effective date provisions contained in the House bill as follows:

(1) It determined that it would permit a private foundation to become a public educational or charitable organization without going through the procedures required by the change of status provision so long as the organization took such action with respect to its first year beginning after December 31, 1970. The date used in the House bill is May 27, 1969.

(2) The Committee postponed for one year the requirement that existing private foundations, operating foundations, and trusts with charitable interests must conform their governing instruments to the various limitations set forth in the bill by the start of the first year beginning after December 31, 1971. This date was extended to December 31, 1972. Foundations whose instruments could not be changed to comply with the income distribution rules or with the business ownership rules would not be affected by those rules until the instrument could be changed. Similar provisions already appear in the bill with regard to accumulations and with regard to the provision requiring existing private foundations to reform their governing instruments in accordance with the language of the bill.

(3) The House bill provides that self-dealing rules will not apply to fair price sales to disqualified persons of property held by the foundation on May 26, 1969, if the foundation is required to dispose of the property in order to meet the business holdings requirement. The Committee agreed to extend this treatment to exchanges and other dispositions where the foundation receives in return amounts equal to or in excess of the fair value of what was exchanged. The Committee also agreed that this rule as to sales of business holdings would also apply to later-acquired property received under wills executed before October 9, 1969, or where the property was received under the mandatory provisions of trusts or documents transferring property in the trusts if such provisions were irrevocable on October 9, 1969, and at all times thereafter.

Divestiture of Excess Business Holdings. -- The Committee decided to adopt largely the rules of the House bill regarding divestiture of business holdings acquired in the future. However, it made substantial changes with regard to the rules dealing with current business holdings of foundations. The following changes were adopted:

Future Purchases. -- The Committee adopted an amendment that would apply to future purchases of business holdings by private foundations. If a foundation buys voting stock of a business, it will not be permitted to cast votes for more than one-half of the stock acquired in this manner. This limitation will not apply to stock acquired by gift or bequest and will not apply to stock at present held by the foundation.

50-Percent Limitation. -- As to existing holdings, the Committee decided that the combined holdings of a private foundation and all disqualified persons in any one business must be reduced to 50 percent by 10 years from the date of the bill. Where the combined holdings now exceed 75 percent, an additional 5 years is allowed before the 50-percent limit must be reached. This test must be met both as to combined voting power and as to combined value of all classes of stock taken together.

Bequests and Trusts. -- Property acquired by the foundation in the future under the terms of a will executed before October 9, 1969, or under a trust which was irrevocable at all times since October 9, 1969, will be treated under the same rules as property now held by the foundation. However, in such a case, the 10-year and 15-year periods are to run from the date the foundation gets the stock from the trust or the estate.

Interim Disposition. -- The Committee eliminated the rules in the House bill requiring disposition of part of the excess stock within two years and another part within five years.

Sales, Etc., of Excess Business Holdings. -- The House bill permits fair-price sales of excess business holdings to be made by the foundation to disqualified persons. The Committee agreed that this was an appropriate way to facilitate the foundation's compliance with the excess business holdings rules. The Committee also provided that redemptions of stock by a closely-held corporation from a foundation to comply with these provisions would not trigger imposition of the accumulated earnings tax and it would not give rise to dividend treatment to other shareholders of the corporation. These rules will apply only in the case of stock already held by the foundation or acquired by the foundation under existing wills or trusts, as described above.

Program-Related Investments. -- The Committee made it clear that a program-related investment is not to be treated as a business holding that must be disposed of. This applies only to investments (such as small businesses in central cities and corporations to assist in neighborhood renovation) made for charitable purposes where the making of a profit for the foundation is not one of the major purposes.

Holding Companies. -- The Committee decided that if a foundation owns stock in a holding company, the foundation will be treated as owning the investments held by the holding company, in addition to any stock it holds separate from the holding company. If the total exceeds the limitation permitted under the bill, then either the holding company would dispose of some of its investments or the foundation would have to dispose of some of its stock in the holding company.

Passive Income. -- The Committee determined to make it clear that passive income sources need not be disposed of. For example, the holding of a bond issue would not be an excess business holding. Also, the holding of the stock of a company which itself derives essentially passive income in the nature of a royalty would not be treated as a business holding subject to the limitations of the bill.

Split Trusts. -- The Committee provided that a non-exempt trust that is subject, under the bill, to many of the limitations of private foundations would not be required to dispose of excess business holdings if the beneficial interest of charities in the trust is less than 60 percent of the value of the trust.

OTHER TAX-EXEMPT ORGANIZATIONS

The "Clay Brown" Provision or Debt-Financed Property. -- The Committee adopted those provisions in the House bill which would prevent a tax-exempt organization from in effect, selling its tax exemption in a transaction where it purchases a going business using little or no cash, liquidates it, leases it and pays the seller with the proceeds from the operation of the business.

Property Acquired Under Life-Income Contracts. -- The Committee agreed that property acquired under life-income contracts should not be treated as debt-financed property. This kind of contract is used in situations where, for example, a school will receive a charitable contribution of an asset and will agree to give the donor the income from the asset for his life.

Holding Companies. -- The Committee agreed that where a debt-financed building is operated by an exempt holding company for the benefit of its affiliated exempt organizations, the property of the holding company would not be considered as debt-financed property to the extent that it is used by the related exempt organizations in the performance of their exempt functions.

Use of Property. -- The House bill exempts from the definition of debt-financed property, property all of which is used for the exempt purpose. The Committee agreed instead that debt-financed property should not include property, substantially all of which is used for exempt purposes. In addition, if less than substantially all of the property's use is related, then it would not be debt-financed property to the extent that it was used for exempt purposes.

Extension of Unrelated Business Income Tax to All Exempt Organizations. -- The Committee adopted the provisions of the House bill which extend the unrelated business income tax to all exempt organizations. Under the present law certain classes of tax-exempt organizations are not subject to the tax. In adopting the House bill the Committee made the following changes:

Rents. -- The Committee adopted two rules to insure that an exempt organization pays the unrelated business income tax on income attributable to the active conduct of an unrelated business. First, it decided that rent from personal property is to be excluded from unrelated business income only when the lease of the personal property is incidental to the lease of the realty; where the rent from personalty is 50 percent or more of the total rent, all would be subject to tax. Thus, only "passive" rental income would be excluded from unrelated business income. Secondly, the Committee agreed to tax real property rentals as unrelated business income where the rentals are measured by reference to the net income from the property. It would exclude rentals based upon a percentage of gross receipts, however.

Related Income. -- The Committee clarified the House bill by providing that related income includes income received from members for providing goods, facilities, or services not only to guests but also to the members' dependents.

Specific Deduction. -- The Committee agreed that the $1,000 specific deduction allowed in the present law in computing the unrelated business income tax will be available for each parish, individual church, district, or other local units in the case of a diocese, province of a religious order, or convention, or association of churches. This rule would be applicable to the extent that the parish, district, etc., realized the income itself.

Voluntary Employees Beneficiary Associations. -- Since the House bill removes the 85% income test in the case of a voluntary employees beneficiary association generally (section 501 (c)(9))such an association is for all practical purposes identical to voluntary employees beneficiary associations whose members are U. S. Government employees (section 501 (c)(10)). Under present law the 85% income test is not applicable with respect to this latter category. Consequently, the Committee combined both types of organizations into one category. In addition, the Committee also provided that those voluntary employees beneficiary associations who have pension and retirement plans for their members but who do not satisfy the 85% income requirement (which is removed by the House bill) will be placed back in an exempt category and would be subject to the unrelated business income tax.

Religious Organizations. --The Committee decided not to extend the unrelated business income tax to those religious organizations that have held certain properties 10 years or more if they pay out no less than 90 percent of their earnings each year and it is established to the satisfaction of the Secretary or his delegate that their rates or other charges and services are competitive with similar businesses.

Consolidated Returns - Holding Companies. -- The Committee agreed that when an exempt holding company and a tax-exempt organization to which it is related file a consolidated return, the holding company will be treated as organized and operated for the same purposes as an exempt-organization. Consequently, if the business activities of the holding company are related to the exempt purpose of the exempt organization, the income would be related business income and not subject to tax.

Taxation of Investment Income of Social, Fraternal, and Similar Organizations. -- The Committee generally agreed to the House provisions related to the taxation of the investment income of these membership organizations with the following modifications:

Cost of Administration. -- The Committee agreed that income will be treated as set aside for the specified benefits where it is used for the reasonable costs of administration of the benefit program as well as the payment of the benefits themselves.

Gain on Sale of Assets. --The Committee also adopted a recommendation which would exclude from the tax on investment income (to the extent the proceeds of the sale are reinvested in assets used for such purpose within a period of three years) the gain on a sale of assets used by the organizations in the performance of their exempt functions.

Masonic and Masonic-Related Organizations. -- Masonic and Masonic-related organizations which today are exempt from tax as a "fraternal beneficiary association" (section 501(c)(8)), in the future should be placed in a separate tax-exempt category. This category would exempt a domestic fraternal society, order, or association operating under the lodge system where the fraternal activities are largely religious, charitable, scientific, literary, or educational in nature and where there are no insurance activities. The tax on investment income would not apply.

Interest, Rent, and Royalties from Controlled Corporations. -- The House bill provides that where an exempt organization owns more than 80 percent of a taxable subsidiary the interest, annuities, royalties and rents are to be treated as "unrelated business income" and subject to tax. Where the operation of the controlled corporation is "functionally related" to the exempt purposes of the controlling exempt organization, these types of income would be "related" income and would not be subject to tax. The Committee also adopted a recommendation which would provide a special rule where the controlled corporation is also an exempt organization. Under the rule, the payment received from the controlled corporation would not be subject to tax to the extent that the facilities rented or the money borrowed is used by the controlled corporation in the performance of its exempt function.

Limitation on Deductions of Nonexempt Membership Organizations. -- The Committee adopted the provision in the House bill which would deny the deduction for expenses incurred in supplying services, facilities or goods to members of a taxable membership organization to the extent that such expenses were not related to income received from the members. Under this provision, no membership organization is permitted to escape the tax on business or investment income by using the income to serve its members at less than cost and then deducting the book "loss". In adopting the provision the Committee made the following modifications:

American Automobile Association. -- Because certain membership organizations (such as the American Automobile Association) must compete with profit-making organizations that provide the same type of services at a loss, they must set their dues at the same loss level. These organizations offset the losses against income received from non-members (such as income from the sale of advertisements). In order to meet this problem, the Committee agreed that it will provide a special rule in cases of this type where the business practice is to provide comparable services at a loss.

Carryovers. -- The Committee agreed that in cases where the deduction for furnishing services, insurance, goods, etc., to members exceeds the income from members the excess deductions can be carried over into succeeding years.

Effective Date. -- The Committee adopted a recommendation that the provisions of the House bill relating to non-exempt membership organizations be effective as of December 31, 1970.

Income from Advertising. -- The Committee adopted the language of the House bill which would provide that the income from advertising and similar activities would be included in unrelated business income even though the advertising is carried on in connection with activities related to the exempt purpose. The Committee adopted the approach of the House bill and instructed the staff to review the language to limit it to the matter specifically covered in the Treasury regulations.

Social Clubs - National Fraternaties and Sororities. -- The Committee agreed that the investment income of social clubs, particularly the national organizations of college fraternaties and sororities (as distinguished from their local chapters) should be exempt from the tax on investment income to the extent that such income is set aside for charitable, educational or religious purposes.

Thrift Shops, etc. -- Under present law, an organization operated primarily to carry on a trade or business for profit is not exempt even though all its profits are payable to one or more exempt organizations. The Committee decided to allow an exemption for such an organization where substantially all the work in carrying on the trade or business is performed for exempt charitable organizations without compensation.

PENSION PLAN CONTRIBUTIONS

Professional Service Corporations. -- The bill does not presently deal with the limits of pension plans except to provide that small business corporations (so-called Subchapter S corporations) must in the future follow in general the limitations of "H. R. 10 plans." In general, those plans limit current distributions to pension and profit-sharing plans to no more than 10 percent of the self-employed person's earnings from the business up to a maximum of $2,500 in any one year. The Committee decided to impose essentially the same limitations upon pension plans of professional service corporations (generally, corporations under special State laws relating to attorneys and doctors).

P. R. #37

PRESS RELEASE

FOR IMMEDIATE RELEASE
October 29, 1969

COMMITTEE ON FINANCE
UNITED STATES SENATE
2227 New Senate Office Bldg.

TAX REFORM ACT OF 1969
Amortization Provisions and Taxation of Single Persons
Committee Decisions

The Honorable Russell B. Long (D., La.), Chairman of the Committee on Finance, announced today that the Committee on Finance had concluded its work on that portion of the House tax reform bill dealing with the amortization of air and water pollution control devices and railroad rolling stock, and with the income tax treatment of single individuals.

A complete description of the actions taken at today's meeting follows:

Amortization of Pollution Control Facilities. -- The Committee agreed to the concept of the House bill of allowing a taxpayer to amortize over sixty months certain certified air or water pollution control facilities. The amortization deduction would be in place of the regular depreciation deduction (but the additional first-year 20 percent depreciation allowance would be available).

The Committee further adopted a recommendation by the Treasury Department that the benefits of this provision be limited to pollution control facilities added after December 31, 1968, to plants which were in operation on that date. The special amortization provision would not be available in the case of facilities included in new plants built in the future. In addition, the Committee adopted a Treasury recommendation that the five-year amortization would be limited to the cost of property with the normal useful life of fifteen years, or less. If the property had a normal useful life of more than fifteen years, the taxpayer would, in effect, treat his facility as if it were two separate facilities. One facility would receive the five-year amortization and the other facility would receive normal depreciation based on the normal useful life of the property. The taxpayer would write off the two facilities concurrently.

The Committee further agreed to a Treasury recommendation that the definition of an eligible pollution control facility would be limited to exclude facilities which serve any function other than pollution abatement. No amortization would be permitted on facilities that only diffuse the pollution and which did not serve to abate the pollution. The Committee also agreed to adopt a Treasury recommendation to make it clear that the amortization provision would apply only to installations which prevent or minimize the direct release of pollutants into air or water in the course of manufacturing operations. Facilities which remove certain elements from fuel (for example, sulphur) that are released as pollutants when the fuel is burned would not be eligible for the amortization.

Further, the Committee adopted a provision which provides that the amortization deduction could only apply to air and water pollution control facilities completed or acquired before January 1, 1975. The Committee also deleted the features which authorize the Secretary of Interior and the Secretary of Health, Education and Welfare to establish effluent standards for water and emissions standards for air. Under this amendment (which conforms to the pattern set by Congress in the Air Quality Act of 1967) the Federal government could set general guidelines which had to be maintained, but in general, the specific standards which would be required would be fixed by the States pursuant to the Air Quality Act of 1967 and the Water Quality Act of 1965.

Amortization of Railroad Rolling Stock. -- In connection with the consideration of the provisions of the House bill extending special 7-year amortization treatment to railroad rolling stock, the Committee also reconsidered the action it had previously taken (see Committee announcements of September 19 and October 10) to provide a special transitional exception to the repeal of the 7 percent investment tax credit for certain railroad rolling stock. As a result of its study, the Committee agreed to delete all these provisions from the bill and substitute instead a new incentive plan suggested by the Treasury Department. The principal features of this plan are:

1. 5-year amortization on new rolling stock, including locomotives, acquired after January 1, 1970 available to all railroads and their lessors.

2. 4-year amortization of 1969 equipment acquisition unrecovered costs (rolling stock including locomotives) as of January 1, 1970.

3. Pretermination property eligible for the 7 percent investment credit placed in service in 1970 will be eligible for the amortization write-off.

4. The investment credit life will be determined by the actual useful life of the property and not by the elective amortization period as presently required.

5. On January 1, 1973, the Secretary of the Treasury after consultation with the Secretary of Transportation will promulgate regulations prescribing the particular class of cars which are not in short supply. This determination will preclude that class of car from the amortization write-off.

6. The cost of repairs to existing rolling stock will be allowed as an expense without question where such cost does not exceed 20 percent of the original cost of the unit.

7. Elective amortization of grading and tunnel bores on a 50-year life.

After agreeing to this plan, the Committee further agreed to limit the amortization privilege to property placed in service before January 1, 1975. In addition, it agreed to permit certain railroad equipment acquired pursuant to the Korean War amortization provision (which the House bill would repeal) to continue to qualify for the amortization authorized by that law.

Single Person; Head of Household . -- The Committee also agreed to adopt two proposals recommended by the Treasury Department relating to the tax treatment provided for single persons. First, the Committee deleted the House-passed provision which would have extended joint return privileges for widows with dependent children beyond the two years now in existing law. Thus, under the Committee's decision existing law which provides that a widow with a dependent child may file a joint return for two years after the date of the spouse would be retained.

Second, the Committee adopted the Treasury recommendation which would provide a new tax rate schedule for single persons. This new schedule, which replaces the provisions of the House bill, would not distinguish between single persons based on whether their age is over or under 35. Instead, it would provide a tax liability for single persons which would not exceed 120 percent of joint return tax liability. Under the Committee's decision, a head-of-household (this is generally a single person who maintains a household which is the principal residence for himself and a dependent) would continue to receive the same tax treatment that he now enjoys under present law. Under the House-passed tax bill, widows and widowers, regardless of age, and unmarried individuals age 35 and over would have been taxed at rates halfway between those available to married couples and those applicable to other single persons.

Fraternal Beneficiary Societies . -- At Tuesday's meeting, the Committee established a separate category (in the provisions defining organizations exempt from income tax) for organizations such as the Masons which operate under the lodge system and which are primarily religious, educational or charitable in nature. A condition to classification in this new category is that the organization not engage in the furnishing of insurance protection to its members. Organizations in this new category were made subject to tax on their unrelated business income but were not brought under the new tax (imposed by the House bill) on investment income of certain categories of organizations.

At today's meeting the Committee agreed to also exclude from the new tax on investment income, other fraternal organizations operating under the lodge system which do provide insurance protection for their members.

Manufacturers Excise Tax. -- The Committee also agreed to a technical amendment (substantially incorporating the text of S. 2510) which relates to the calculation of the manufacturers excise tax in situations where a "constructive sales price" must be determined.

RELATED BUSINESS INCOME OF CHURCHES

At Tuesday's meeting the Committee agreed that the operation and maintenance of cemeteries, the conduct of charitable institutions, the sale of religious articles, and the printing, distribution and sale of religious pamphlets, tracts, calendars, books and magazines with substantial religious content done in connection with a church would be treated as related business income of the church and would not be subjected to the tax on unrelated business income even though the document might produce some advertising income.

P. R. #38

PRESS RELEASE

FOR IMMEDIATE RELEASE
October 30, 1969

COMMITTEE ON FINANCE
UNITED STATES SENATE
2227 New Senate Office Bldg.

TAX REFORM ACT OF 1969
Committee Decisions

The Honorable Russell B. Long (D., La.), Chairman of the Committee on Finance announced today that the Committee on Finance had reached agreement on several additional parts of the House-passed tax reform bill.

A large part of today's executive session was devoted to consideration of amendments offered by Senators Albert Gore (D., Tenn.) and Vance Hartke (D., Ind.) to increase the $600 personal exemption and an alternative approach by Senator Jack Miller (R., Iowa) to provide tax reduction through the use of additional tax credits. The Chairman reported that following a number of record votes on these matters the Committee decided that it would concentrate its attention at tomorrow's meeting on tax cuts worked out through reductions in the tax rate schedules. This is the same approach taken by the House bill.

During the remainder of today's session, the Committee acted on a series of amendments, the substance of which are described in the following paragraphs.

Income of American Employees Abroad. -- Under present law, an American citizen who resides in a foreign country for 17 out of 18 consecutive months may exclude from his gross income for Federal tax purposes amounts paid to him from foreign sources up to $20,000 a year. If he is a bona fide resident of a foreign country he may exclude $20,000 a year for the first three years, and thereafter exclude $25,000 a year. At today's meeting, the Committee decided that these $20,000 and $25,000 exclusions should be limited to $6,000. Accordingly, the earned income limitation in existing law in these cases for the future will be limited to $6,000.

Federal Land Banks; Amendment Reconsidered. -- The Committee reconsidered the amendment it had added to the bill earlier in its sessions which would have subjected Federal land banks to Federal income tax. (See Committee announcement of October 17, 1969.) Following this reconsideration the Committee decided to omit the provision from its bill.

REA Cooperatives; Amendment Reconsidered. -- The Committee also reconsidered the action taken at an earlier session by which rural electrification cooperatives were subjected to tax on income earned on U. S. government bonds purchased with the proceeds of low interest bearing loans which these organizations are authorized to obtain from the Federal government. (See Committee announcement of October 17, 1969.) Following this reconsideration, the Committee decided to omit this provision from its bill.

Recapture of Soil and Water Conservation Expenses. -- The Committee agreed to a provision to recapture soil and water conservation expenditures and land clearing expenditures made with respect to farm land. Under the provision, the gain on the sale of land would be treated as ordinary income, rather than as a capital gain, to the extent of the previous specified expenditures with respect to the land. However, there would be no recapture after the land had been held for ten years from the time of the expenditures. For land sold within 10 years there would be a sliding scale of recapture. Where the land was sold prior to the end of the fifth taxable year after the year in which the expenditure was made, there would be a 100 percent recapture; for sales in the sixth through the tenth years the amount would be recaptured as follows:

YEAR	PERCENT RECAPTURE
6	80
7	60
8	40
9	20
10	0

Medical Insurance; Medicare Amendment Reconsidered. -- On October 17, 1969, the Committee approved an amendment to require that payments made under the Medicare and Medicaid programs and payments made by private medical insurance carriers must be reported to the Federal tax collector if they aggregate $600 or more during the year. The payments to be reported include those made directly to the health care practitioner who accepts an assignment from his patient and those for which a patient submits bills and is paid for services rendered by the health care practitioner.

At today's meeting the Committee reconsidered this amendment and agreed that the new provisions with respect to private insurance would not be applicable until 1971. Reporting of payments under the Medicare and Medicaid programs, however, will be required beginning in 1970.

Real Estate Depreciation; Binding Contracts. -- Under the House bill the use of accelerated depreciation is protected where the taxpayer acquires new real property pursuant to a binding contract in effect on July 25, 1969. No comparable provision protects the purchaser of used real estate where the acquisition occurs after July 25, 1969 pursuant to a binding contract in effect prior to that date. The committee added an amendment to allow a purchaser to use 150% of straight line depreciation with respect to used real property acquired pursuant to a binding contract in effect on July 25, 1969. Thus, under the Committee's action today, a taxpayer may claim fast appreciation with respect to a building, whether new or used, if he had entered into binding contracts prior to July 25, 1969, for the purchase of the building.

Another amendment was agreed to providing for accelerated depreciation with respect to a building for which the necessary land had been acquired and building plans had been completed before July 25, 1969, but for which the local authorities had failed to grant the necessary approval to permit construction to commence before July 25, 1969, even though application to build had been filed before that date. Under the Committee amendment, accelerated depreciation will be available provided construction commences within one year from the date of filing of the application for the building permit.

Insurance Companies. -- The Committee agreed to four amendments with respect to the tax treatment of insurance companies. The first two of these had previously been approved by the Committee and passed by the Senate (H.R. 2767 of the 90th Congress). The substance of the four amendments follows:

Losses. -- This amendment provides for loss carryovers where one type of insurance company is converted into another type (for example, where a stock casualty insurance company becomes a mutual company, or a life insurance company, or vice versa). The amount of the loss deduction generally would be limited to the lower of the amount for which the company would qualify before or after the shift.

Spin-off Phase III Tax. -- This amendment provides that the so-called "phase three" tax applicable to life insurance companies is not to apply in certain cases merely because a life insurance company distributes to its holding company parent the stock of a subsidiary which it holds. However, in such a case the so-called "phase three" tax is to apply to distributions by the subsidiary, whose stock was distributed, in the same manner as it would apply to distributions by the life insurance company itself.

Contingency Reserves. -- This amendment clarifies the deductibility of interest credited to special reserves under contracts of group term life insurance or group health and accident insurance established and maintained for insurance on the lives of retired workers, or for premium stabilization. On approving this legislation the Committee observed that the amendment reiterated its intent, expressed during consideration of the Life Insurance Company Income Tax Act of 1959, that this interest was deductible.

Tax-Free Exchanges of Securities. -- This amendment deals with the situation where insurance companies with large holdings of appreciated securities in their investment portfolios have been able to exchange these securities for their own stock without payment of tax on the gain included in the securities surrendered. Under this amendment this sort of exchange in the future will give rise to taxable gain.

Interest on Tax Deficiencies and Refunds . -- The Committee agreed to adopt a new provision (recommended by the Internal Revenue Service) which provides a penalty on taxpayers who fail to pay the tax required to be shown on the return at the time they file their return. In general, present law imposes a five percent per month penalty, up to a maximum of 25 percent, in the case of failure to file a return on the date it is due. This provision does not apply if the failure is due to reasonable cause and not due to wilful neglect. Under the Committee provision, this penalty would be expanded to apply if the taxpayer fails to pay the tax due at the same time he files his return. As in the case of the failure to file the return at the time it is due, however, the addition to the tax would not apply if the failure is due to reasonable cause and not due to wilful neglect.

Further, the Committee agreed to increase the penalty for failure to make required deposits of withholding taxes. Under this decision the present penalty of one percent per month (up to a maximum of six percent) would be raised to five percent of the amount due to the Government. This penalty would be added to any deposit of withholding taxes which are not paid at the time they are due. However, it would not apply where the failure to deposit on time is due to reasonable cause and not due to wilful neglect.

Mutual Funds; Unit Investment Trusts . -- The Committee approved an amendment to prevent participants in a periodic payment plan to purchase mutual fund shares from being treated as an association taxable as a corporation. However, the Committee included a proviso that its amendment would not apply with respect to an association of persons investing in variable annuity contracts with a life insurance company.

Subpart F Income . -- The Committee agreed to an amendment which would make technical corrections in the computation of "subpart F" income, which is taxed to the parent corporation of a foreign subsidiary. Under existing law, foreign base company income (a part of Subpart F Income) does not include any item of income received by a controlled foreign corporation if it is established to the satisfaction of the Secretary or his delegate, with respect to the item, that the creation or organization of the foreign corporation does not have the effect of substantial reduction of income, or similar taxes. The provision adopted by the Committee would clarify this section of existing law by providing that foreign base company income would not include any item of income received by such a foreign controlled corporation if the transaction giving rise to the item of income did not have as one of its significant purposes a substantial reduction of income, or similar taxes.

Private Foundations . -- The Committee also agreed to a new provision relating to existing private foundations which would make the divestiture requirement inapplicable if the following conditions are present:

(1) The stock in the company was acquired by the foundation by gift, device or bequest,

(2) The foundation owns ninety-five percent or more of the voting stock of the corporation;

(3) The majority of the governing body of the foundation consists of persons other than the donor or members of his immediate family, taking into account the attribution rules in the bill;

(4) The current business of the corporation is substantially of the same character as the business conducted at the time of the gifts of the stock by the donor;

(5) The corporation does not purchase any stock in another business enterprise which would represent an excess business holding;

(6) The corporation annually, distributes to its shareholders 40 percent of its income after taxes; and

(7) The foundation must distribute (or use) for its tax-exempt purpose substantially all of its income.

Mutual Savings Banks; Savings and Loan Associations. -- The Committee considered and approved several modifications of the rules relating to investment restrictions applicable, to mutual savings banks and savings and loan associations. Under these modifications the following investments would qualify for purposes of meeting the tests (82 percent of total assets in the case of savings and loan associations; 72 percent of total assets in the case of mutual savings banks) necessary to qualify for the special deduction for additions to bad debt reserves:

(1) Loans secured by redeemable ground rents;

(2) Loans secured by an interest in real property located in an urban renewal area if the urban renewal area is predominately residential; and

(3) Loans made to finance the acquisition or development of land which will become residential property if there is assurance that building will actually occur thereon within a period of three years (with retroactive disqualification of the loan if this does not occur).

The Committee also adopted a provision under which an apartment house with commercial establishments on the first floor would qualify as "residential real property" if 80 percent of the useable space in the building was residential space. It also modified the rules applicable during the transition period over which the 60 percent deduction for bad debts is reduced to 50 percent. (See Committee announcement of October 16, 1969.) During this period it would be permissible if only 50 percent (rather than 60 percent) of the investments of the institution are in qualifying assets. Thereafter, 60 percent of investments must be in qualifying assets just as the House bill would have required. Finally, a one percentage point reduction would be made in the 50 percent deduction for additions to bad debt reserves for each percentage point that qualifying assets fall below the 82 percent test in the case of savings and loan associations. In the case of mutual savings banks, a reduction of 1-1/2 percentage points in the bad debt deduction would be required for every percentage point that qualifying assets fall below the 72 percent test.

Supervisory Mergers of Savings and Loan Associations. -- The Committee agreed to an amendment, suggested by the Federal Home Loan Bank Board, clarifying the treatment of bad debt reserves of institutions participating in a tax-free merger under the supervision of the Federal Home Loan Bank Board. Under the amendment the amount in the bad debt reserves would not be restored to income at the time of the merger. The Committee was advised that its amendment reflected the law as the Internal Revenue Service had interpreted it, and in this respect it is merely declaratory of the law.

Charitable Remainder Trusts. -- The Committee decided to require a charitable remainder annuity trust or unitrust to distribute at least its current income (other than capital gains) to the income beneficiary, and to provide that in determining the amount of the charitable contribution deduction allowed in the case of a gift of remainder interest in trust, a 5 percent payout to the income beneficiary is to be assumed for valuation purposes if the 5 percent is higher than the payout otherwise determined under the annuity or unitrust rules. This rule strikes a balance between the harshness of imposing an inflexible 5 percent payout requirement which might unduly restrict the trust and the possibility of circumventing the restrictions contained in the private foundation provisions of the bill by providing for a very low income payout. The Committee action was made effective with respect to trusts created after October 9, 1969.

Limitation on Deduction of Interest. -- The Committee adopted the Treasury recommendation that the limitation on the interest deduction in the case of individual taxpayers contained in the House bill be deleted pending further study. Generally, this provision of the House bill would have disallowed the deduction of interest on indebtedness incurred to purchase investment assets to the extent the interest exceeded the taxpayer's net investment income and the amount of his long-term capital gains by more than $25,000.

Corporate Mergers--Disallowance of Interest Deduction in Certain Cases. -- The Committee generally adopted those provisions of the House bill dealing with the disallowance of the interest deduction on debt issued in connection with corporate mergers. However, it did make several important modifications in this provision. Under the House bill, the interest deduction would be denied for interest on bonds or debentures issued by a corporation to acquire stock in another corporation or to acquire at least two-thirds of the assets of another corporation. This rule, however, only would apply to bonds or debentures which (1) are subordinated to the corporation's trade creditors, (2) are convertible into stock, and (3) are issued by a corporation with a ratio of debt to equity which is greater than two to one, or with an annual interest expense on its indebtedness which is not covered at least three times over by its projected earnings.

First, the Committee adopted a provision authorizing the Internal Revenue Service to issue regulations providing tests for distinguishing generally whether bonds or debentures are in fact debt or equity. Since there is a great variety of situations in which this question can arise, the Committee believed it was appropriate to provide this authority to the Internal Revenue Service so it could develop rules to take account of the various characteristics of these situations.

The Committee also agreed that it would be appropriate to broaden the subordination test of the House bill so that it applies to obligations which by their terms are subordinated in right of payment to any substantial amount of the corporation's indebtedness. This action would provide for the case where although the obligation is not subordinated to trade creditors it is subordinated to substantial amounts of pre-existing debt.

The Committee also decided that the debt equity and interest coverage tests of the House bill should be revised so as to allow an issuing corporation to have a debt equity ratio of four to one, and to only require the annual interest expense of the corporation to be covered at least two times over by the corporation's projected earnings. The Committee believes these tests more appropriately reflect a reasonable capital structure for a corporation. The Committee further decided to clarify the application of these tests in the case of corporations engaged in the loan business by providing that the amount of the corporation's indebtedness should be reduced by amounts owed to it and the amount of the corporation's annual interest expense should be reduced by its annual interest income.

The Committee also agreed that where the interest deduction was disallowed because the debt equity test was not met or because the earnings of the corporation were not at least two times more than the annual interest expense, the disallowance of the interest deduction would be discontinued after the debt equity test and the earnings test had been met for a period of at least three years. The House bill provides for an exception from the disallowance rule of up to five million dollars a year of interest on obligations which meet the prescribed tests. This exemption is reduced by interest on obligations which do not meet one of the three specific tests in the bill. The Committee agreed that the reduction should be limited to interest on obligations issued after December 31, 1967.

In the case of corporate acquisitions the provisions of the House bill only apply where the acquiring corporation obtains at least two-thirds of the assets of another corporation. The Committee agreed to a Treasury recommendation that the two-thirds test should be applied to the operating assets (excluding cash) of the acquired company rather than to the total assets. This would prevent the two-thirds test from being avoided where the acquired company has a large amount of its assets in cash and non-operating properties.

The Committee also decided to make this provision of the House bill inapplicable in the case of an acquisition of a corporation's stock where the total interest of the acquiring corporation in the other corporation does not exceed five percent. This would eliminate de minimus stock acquisitions from the scope of this provision.

The Committee also agreed that this provision of the House bill should be applicable to indebtedness incurred after October 9, 1969. (The date used in the House bill is May 27, 1969). The Committee also agreed that this provision would not apply to the acquisition of additional stock of a corporation where the taxpayer acquired at least 50 percent of the stock on or before October 9, 1969. This would enable a corporation which had achieved practical control of another corporation by this date to acquire the additional stock necessary to give it control for tax purposes. The Committee also agreed to make this provision of the bill inapplicable to the acquisition of stock or assets of a corporation pursuant to a binding contract entered into before October 9, 1969.

Corporate Mergers --Limitation on Installment Sales Provision. -- The Committee agreed to the provision of the House bill which provides that bonds with interest coupons attached, in registered form, or which are readily tradeable are, in effect, to be considered payments in the year of sale for purposes of the rule which denies the installment method where more than 30 percent of the sale's price is received in that year. In this connection, however, the Committee agreed to exclude from this treatment bonds or debentures in registered form which are non-transferable, except by operation of law.

The Committee also accepted the Treasury recommendation that the periodic payment requirement of the House bill be deleted, but that the installment method not be available where an obligation is payable on demand. Under the periodic payment requirement of the House bill the use of the installment method would be denied unless the payment of the loan principal, or the payment of the loan principal and interest together, were spread relatively evenly over the installment period.

The Committee also agreed to make these new rules regarding the installment method effective with respect to sales made after October 9, 1969, (the date used in the House bill is May 27, 1969). The Committee further agreed to make the new rules inapplicable in the case of installment sales which are made pursuant to a binding contract entered into before October 9, 1969.

Corporate Mergers--Original Issue Discount. -- The Committee accepted with minor modifications the provision of the House bill which provides that in the case of bonds issued at a discount the bondholder and the issuing corporation are to be treated consistently with respect to the original issue discount. Generally, under this provision of the bill, a bondholder is required to include original issue discount in income ratably over the life of the bond. This rule applies in the case of the original bondholder as well as to subsequent bondholders.

The Committee adopted a provision making the ratable inclusion of original issue discount requirement inapplicable in the case of life insurance companies which already accrue discount on a basis which produces essentially the same result as a ratable accrual. This will eliminate the necessity of life insurance companies shifting from one method of accruing original issue discount which has been regularly employed to another method (that prescribed by the bill) where the end result is essentially similar.

The Committee agreed that this provision of the House bill should be applicable to debt obligations issued after October 9, 1969, (the date used in the House bill is May 27, 1969). The Committee also agreed that this provision of the bill should not apply to debt obligations which are issued pursuant to a binding commitment entered into prior to October 9, 1969.

Corporate Mergers--Convertible Indebtedness Repurchase Premiums. -- The Committee agreed to the provision of the House bill dealing with the deductability of convertible indebtedness repurchase premiums with a minor modification. This provision of the House bill provides that a corporation which repurchases its convertible indebtedness at a premium may deduct only that part of the premium which represents a cost of borrowing, rather than being attributable to the conversion feature.

The Committee agreed to make this provision applicable to repurchases of convertible indebtedness after October 9, 1969, (the date used in the House bill is April 22, 1969).

P. R. # 39

PRESS RELEASE

FOR IMMEDIATE RELEASE
October 31, 1969

COMMITTEE ON FINANCE
UNITED STATES SENATE
2227 New Senate Office Bldg.

TAX REFORM ACT OF 1969
Reported to Senate

The Honorable Russell B. Long (D., La.), Chairman of the Committee on Finance, announced today that the Committee on Finance had finished its work on the Tax Reform Act of 1969 and had ordered the bill reported to the Senate. He reported that the motion to report was approved by a voice vote with few Senators dissenting. He indicated this was the third most significant tax bill in the nation's history ranking behind only the original income tax act of 1913 and the massive tax cuts in the Revenue Act of 1964. He expressed hope that the technical work necessary to prepare the bill for Senate consideration could be finished within three weeks so that the bill could be acted on promptly by the Senate.

$9 Billions Tax Cuts. --Chairman Long reported that in large measure the $9 billion of individual income tax reductions recommended by the House of Representatives had been approved by the Committee on Finance. The most significant difference involved a transfer from 1971 to 1972 of a portion of the tax reductions the House bill would have provided in the earlier year. He indicated that this was done in order to prevent the bill from having an inflationary impact on the economy in 1971.

Planned Tax Reduction. -- Senator Long further indicated that the Senate bill reflected a program of planned tax reduction. He noted that on January 1, 1970, the 10 percent surtax would be reduced to 5 percent and that on July 1, 1970, it would be eliminated entirely. He also indicated that the standard deduction would be increased in 1970 and that the low income allowance --designed to remove 5 million tax returns from the tax rolls--would also become effective in 1970. The combination of these features, he said would involve tax reductions totaling $10.8 billion

In 1971 he reported the first step in the individual tax rate reductions would take place, and the second step in the increase of the standard deduction would occur. In addition, the so-called phase-out of the low income allowance would itself phase-out over a 2-year period. The combination of these changes plus the final elimination of the surtax and the planned reduction in auto and telephone excise tax rates, would result in further tax reductions for 1971 of $8.1 billion.

In 1972, the full tax rate reductions would become effective, and the final step in the increase of the standard deduction would be reached. In addition the "phase-out" of the low income allowance would be fully eliminated in 1972. Thus, in 1972 these planned tax reductions and another excise tax reduction would amount to a further $4.4 billion.

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Revenue Raising Tax Reform. --

In addition to these tax reductions, the Chairman emphasized that tax raising reform features of the bill would hike taxes by $6.5 billion from those who in the past have enjoyed substantial tax preferences. He observed that no industry in America would be left untouched by the bill and that the real estate industry, the oil and gas industry, financial institutions and private foundations had been singled out for particularly stringent treatment.

The Chairman stated his belief that at no time in his experience had the public interest been represented so well in a major tax bill. He praised the members of the Committee who had worked so long and so hard to reach agreement on a tax bill as complicated as the Tax Reform Act of 1969. He expressed confidence that if the full Senate would approach its work on the bill with the same diligence and dedication that the members of the Committee on Finance had displayed, the tax reductions provided by the bill could become the law of the land by Christmas.

A complete description of the day's decisions, with respect to other matter, follows:

Cement Mixers. -- The Committee approved an amendment (identical to an amendment which passed the Senate in 1968 too late for the House to act before adjournment) to clarify the excise tax status of cement mixers. Under the Committee amendment, cement mixers would not be subject to the 10 percent excise tax generally applicable to automobile tructs, although the tax would continue to apply to the truck in which the cement mixer is mounted. This amendment reverses a 1967 ruling in which the Internal Revenue Service administratively reversed its long-standing position and announced that cement mixers in the future would be subject to tax.

Vacation Pay. -- The Committee also adopted an amendment extending for an additional two years, for taxable years ending before January 1, 1971, the period within which vacation pay may be accrued by employers under rules in effect prior to 1960. The Committee was advised that the Treasury Department would be prepared to recommend permanent legislation within this two-year period to deal with the matter of vacation pay.

Filing of Income Tax Returns and Withholding. --The Committee adopted a number of provisions (all suggested by the Treasury Department) which will relieve many low income taxpayers from filing a tax return, permit more flexibility in the withholding system, and enable the Treasury to increase its assistance to taxpayers by computing their tax for them.

1. The first of these increases the income level at which filing a tax return is required from the present $600 ($1,200 for those age 65) to the new levels of nontaxable income provided by the low income allowance which the Committee also adopted. The filing requirement would be increased to $1,700 for single persons, $2,300 if married or age 65 or over, $2,900 if married and one spouse is age 65 or over, and $3,500 if married and both spouses are age 65 or over. The filing level would remain at $600 for a married couple filing separate returns.

2. The Committee adopted another recommendation that the problem of over-withholding for those with no tax liability (particularly those who work part-time such as students who work during the summer) be solved by eliminating withholding for such persons. This would be accomplished by an employee certifying to an employer that he estimates that he will have no Federal income tax liability for the current year and, in fact, had no income tax liability for the preceding year. This could relieve as many as 10 million persons from overwithholding.

3. The next recommendation was that the Internal Revenue Service be permitted to compute tax liability for taxpayers if they request, regardless of the amount or source of their income, their marital status, the type of tax credits claimed, or whether they itemize their deductions or take the standard deduction. Under present law, only taxpayers who have income less than $5,000, less than $100 of nonwage income, who use the optional tax table and do not use the retirement income credit, may elect to have their tax computed for them by the Internal Revenue Service.

4. The Committee also approved an amendment that the Internal Revenue Service be permitted to provide employers more flexibility in devising withholding systems which fit their particular needs and also match withholding and tax liability. In addition, employers will be permitted to annualize wage payments for withholding purposes to reduce overwithholding where wage payments are not made throughout the entire year as in the case, for example, of professional athletes. Under present law, withholding on wage payments is computed as if the same amount of wages is to be received each payroll period throughout the year.

Under the Treasury proposal, for example, if an employee is to receive wages for only 6 months of the year, his employer could multiply the amount of wages paid in the first month by 6, determine the withholding due on this amount as if it were the total wages for the year, and withhold one-sixth of the annual withholding in each of the six monthly payroll periods.

5. The next recommendation was that the Internal Revenue Service be permitted to prescribe rules for voluntary income tax withholding on payments for services which are not "wages" as defined in the law. Tax would be withheld on these payments only when the employee requests such withholding. This provision would reduce the amount of final tax payment (which may be burdensome) for retired persons (or their survivors) receiving pensions, farm and domestic workers, and others who receive payments not now subject to withholding.

6. The Committee also adopted a Treasury recommendation that supplemental unemployment benefits (SUB payments) be subject to withholding.

7. The Internal Revenue Service was authorized to permit rounding of withholding amounts to the nearest whole dollar. This will aid employers, particularly those whose withholding systems are computerized.

8. Employees who have itemized deductions in excess of the level of deductions on which the withholding tables are based may claim additional withholding allowances under existing law to prevent overwithholding in their cases. However, existing law requires that estimated itemized deductions for the year be no more than the taxpayer's itemized deductions for the preceding year. This effectively prevents the provision from operating for the first year in which the taxpayer has excess itemized deductions even though their existence is clear and need not be verified by similar experience in a prior year. The Committee adopted a recommendation that the prior year requirement be eliminated where the excess itemized deductions are substantiated by court order (such as alimony) or by other evidence which verifies their existence. Also, if the excess itemized deductions would result in a fractional additional withholding allowance, the Committee action would permit a full additional withholding allowance on account of such fractional amount, rather than none as under existing law.

Reimbursement of Certain Casualty Loss Expenditures. --The Committee approved an amendment (the substance of Amendment No. 242, Senator Jack Miller (R., Iowa)) which provides for the exclusion from gross income of amounts received under insurance contracts for increased living expenses necessitated by damage to or destruction of an individual's residence. However, under this amendment the taxpayer may exclude only actual extra living expenses resulting from the fire or other casualty which are over and above normal living expenses incurred by the taxpayer and members of his household.

Tax Court. -- On motion of the Chairman, the Committee added an amendment to the bill to create special procedures for the decision of small tax cases brought by taxpayers to the Tax Court and to change the status of the Tax Court to a legislative court under Article I of the Constitution. The amendment provides that where the taxes at issue are less than $1,000 for any one taxable year the taxpayer may request the court to review his case under a simplified procedure. Under this procedure the decisions will not be treated as precedents for deciding later cases. This provision, which is similar to proposals that had been introduced in both Houses of Congress in recent years, is expected to permit more rapid handling of many small tax cases. The amendment also changes the term of office of a tax court judge to fifteen years from the day he takes office. (Under present law it is twelve years, or the remainder of the term of the vacancy.) Modifications are provided in Tax Court retirement provisions, bringing them more in line with provisions for district court judges. Contempt and subpoena powers are made essentially the same as those of district court judges. The small claims provisions would take effect a year from the date of enactment; other provisions would generally apply as soon as the bill is enacted.

Arbitrage Bonds. --The Committee agreed to provide that State and local government bonds would not be treated as arbitrage bonds, which would cause the interest on the bonds to be taxable, where a portion of the proceeds of the bonds were placed in a reserve fund or a replacement fund. These are funds which are maintained to provide protection for bondholders and the proceeds of the funds generally are invested in Government or corporate securities. For this rule to be applicable, no more than fifteen percent of the proceeds of a bond issue could be placed in such a reserve or replacement fund. In addition, this treatment would not be available if the purpose of placing the proceeds in the fund was to obtain the benefits of arbitraging rather than to protect the bondholders. The Committee had previously dealt with the treatment of arbitrage bonds. (See Committee announcement of October 9, 1969).

Private Foundations. -- The Committee modified in some respects the provisions it had previously dealt with regarding requirements that private foundations dispose of excess business holdings. (See Committee announcement of October 28, 1969). In one case brought to the Committee's attention, it was decided to permit a foundation to receive certain securities which are now subject to both a will and a trust without violating the excess business holdings requirements.

In another case brought to the Committee's attention it was decided to require a foundation to dispose of its excess holdings in stages--10 percent of the excess holdings within two years, 25 percent within five years, 50 percent in 10 years, and the remainder by the 15th year--if those excess holdings are in a corporation which owns more than 10 percent of the land area of any major political subdivision in the United States, (a county or city with a population of more than 100,000).

Investment Tax Credit; Transition Rules. -- The Committee agreed to two additional transitional rules under which the investment credit will continue to be available in certain situations. The Committee previously had approved a transition rule which continues the availability of the credit in the case of property specified in a binding lease in effect on April 18, 1969 which obligates the lessor or lessee to construct under the terms of the lease. At today's meeting this rule was made applicable where the property is specified in a document filed with a local government authority prior to April 18, 1969. Thus, the investment credit will continue to be available for property which is specified in this manner and which is constructed pursuant to a pre-April 19, 1969, binding lease.

The Committee also agreed to continue the availability of the investment credit for property which would otherwise qualify for this treatment under the plant facility rule previously adopted by the Committee, except for the fact that construction had not commenced at the site of the plant facility. Generally, under this rule the credit will not be available unless the site for the plant facility was acquired prior to April 19, 1969, substantial expenditures were made prior to that date to prepare the site for its intended use (including the acquisition of access and transportation facilities related to the facility), and the taxpayer commences construction of the facility within one year from the time the site for the facility was acquired.

Capital Loss Carrybacks for Corporations. -- Under present law, corporations may carry capital losses forward for five taxable years. The Committee decided to allow corporations to carry back their capital losses three years (in addition to the 5-year carryover), conforming the treatment of net operating loss carrybacks and carryovers under present law.

Accumulated Earnings Tax. -- In its decisions regarding private foundations, the Committee had previously provided an exception from (1) the accumulated earnings tax (Internal Revenue Code section 531), and (2) the dividend rules (Internal Revenue Code section 303) in the case of redemptions of stock (owned by the foundation) by a closely-held corporation to comply with the new excess business holdings rules. (See Committee announcement of October 28, 1969.) An exception from the dividend rules appears in present law in the case of redemptions from an estate to pay death taxes. The Committee amended the bill to provide a similar exception from the accumulated earnings tax when a closely-held corporation redeems stock from an estate to pay death taxes.

Nonexempt Membership Organizations; Securities and Commodities Exchanges. -- The Committee previously adopted the provision in the House bill which would deny the deduction for expenses incurred in supplying services, facilities or goods to members of a taxable membership organization to the extent that such expenses were not related to income received from the members. In addition to the decisions previously made (see Committee announcement of October 28, 1969), the Committee adopted an amendment making this provision inapplicable to securities and commodities exchanges.

TABLE 1.—BALANCING OF TAX REFORM AND TAX RELIEF, CALENDAR YEAR LIABILITY

[In millions]

	1970	1971	1972	1973	1974	1979
Tax reform program	$1,395	$1,590	$1,805	$1,970	$2,315	$3,220
Repeal of investment credit	2,500	2,990	2,990	3,040	3,090	3,270
Tax reform and repeal of investment credit	3,895	4,580	4,795	5,010	5,405	6,490
Income tax relief:						
Low income allowance	−625	−625	−625	−625	−625	−625
Removal of phaseout on low income allowance		−1,522	−2,027	−2,027	−2,027	−2,027
Increase in standard deduction [1]	−867	−1,086	−1,373	−1,373	−1,373	−1,373
Rate reduction		−1,687	−4,498	−4,498	−4,498	−4,498
Tax treatment of single persons		−445	−445	−445	−445	−445
Total reductions	−1,492	−5,365	−8,968	−8,968	−8,968	−8,968
Balance between tax reform (+) and tax relief	−2,403	−785	−4,173	−3,958	−3,563	−2,478

[1] 1970: 13 percent, $1,400 ceiling; 1971: 14 percent, $1,700 ceiling; 1972: 15 percent, $2,000 ceiling.

Note: The tax surcharge extension ($3,100,000,000 liability for 1970) and the excise tax extension ($1,170,000,000, $800,000,000, $800,000,000 and $400,000,000, for 1970 through 1973, respectively) are not included above because of their impermanent character.

TABLE 2.—REVENUE ESTIMATES, TAX REFORM, CALENDAR YEAR LIABILITY [1]

[In millions of dollars]

	1970	1971	1972	1973	1974	1979
Corporate capital gains	140	175	175	175	175	175
Foundations	40	45	45	45	50	55
Unrelated business income	5	5	5	5	5	20
Contributions	5	10	20	20	20	20
Farm losses	10	10	10	15	15	20
Moving expenses	−110	−110	−110	−110	−110	−110
Railroad depreciation	−90	−135	−190	−255	−270	−170
Amortization of air and water pollution facilities	−15	−40	−70	−95	−115	−120
Corporate mergers, etc	([2])	([2])	([2])	([2])	([2])	([2])
Multiple corporations	30	70	120	170	235	235
Accumulation trusts	10	20	30	40	50	100
Income averaging	−110	−110	−110	−110	−110	−110
Deferred compensations:						
Restricted stock	([2])	([2])	([2])	([2])	([2])	([2])
Other deferred compensation						
Stock dividends	([2])	([2])	([2])	([2])	([2])	([2])
Subchapter S	([2])	([2])	([2])	([2])	([2])	([2])
Tax-free dividends					80	80
Financial institutions:						
Commercial banks:						
Reserve	225	150	125	100	100	100
Capital gain	([2])	5	5	5	10	50
Mutual thrift:						
Reserve—savings and loan associations	10	20	30	40	40	40
Mutual	20	25	30	30	35	35
Municipals tax-exempt interest						
Individual capital gains:						
Capital loss provisions	50	50	55	55	60	65
6 months-1 year holding						
Pension plans	([2])	5	10	15	25	50
Casualty loss	([2])	([2])	([2])	([2])	([2])	([2])
Sale of papers	([2])	([2])	([2])	([2])	([2])	([2])
Life estates	10	10	10	10	10	10
Franchises	([2])	([2])	([2])	([2])	([2])	([2])
Removal of alternate rate	200	265	330	330	330	330
Natural resources:						
Production payment	100	110	125	140	150	200
Percentage depletion	155	155	155	155	155	155
Foreign depletion						
Foreign income:						
Loss carryover						
Restriction on mineral credits						
Individual interest deduction						
Regulated utilities	60	140	185	225	260	310
Cooperatives	([2])	([2])	([2])	([2])	([2])	([2])
Limit on tax preference / Allocation } Minimum tax	650	655	665	675	690	700
Real estate:						
Used property	15	40	65	110	150	250
New nonhousing	([2])	60	170	300	435	960
Capital gain, recapture	([2])	10	20	30	40	100
Rehabilitation	−15	−50	−100	−150	−200	−330
Preliminary total	1,395	1,590	1,805	1,970	2,315	3,220
Plus investment credit	2,500	2,990	2,990	3,040	3,090	3,270
Total	3,895	4,580	4,795	5,010	5,405	6,490

[1] Except as indicated these estimates are all at current levels, the time differences being solely to show the phasein.
[2] Less than $2,500,000.

TABLE 3.—TAXABLE RETURNS UNDER PRESENT LAW, NUMBER MADE NONTAXABLE BY RELIEF PROVISIONS AND NUMBER BENEFITING FROM RATE REDUCTION UNDER BILL WHEN FULLY EFFECTIVE IN 1972

[Number of returns in thousands]

AGI class	Taxable under present law	Made nontaxable by low-income allowance and 15 percent $2,000 standard deduction	Remaining taxable—benefit from modified rate reduction
0 to $3,000	10,053	5,398	4,655
$3,000 to $5,000	9,562	389	9,173
$5,000 to $7,000	9,779	41	9,738
$7,000 to $10,000	13,815	8	13,807
$10,000 to $15,000	13,062	7	13,055
$15,000 to $20,000	3,852	2	3,850
$20,000 to $50,000	2,594		2,594
$50,000 to $100,000	340		340
$100,000 and over	95		95
Total	63,152	5,845	57,307

TABLE 4.—TAX BURDENS UNDER PRESENT LAW,[1] UNDER H.R. 13270,[2] AND PERCENT TAX DECREASE IN 1972 (ASSUMES NONBUSINESS DEDUCTIONS OF 10 PERCENT OF INCOME)

Adjusted gross income (wages and salaries)	Married couple with 2 dependents			Adjusted gross income (wages and salaries)	Married couple with 2 dependents		
	Present tax law	H.R. 13270 tax	Percent tax change		Present tax law	H.R. 13270 tax	Percent tax change
$3,000	[3] 0	[4] 0	0	$12,500	[5] $1,567	[6] $1,347	−14.0
$3,500	[3] $70	[4] 0	−100.0	$15,000	[5] 2,062	[7] 1,846	−10.5
$4,000	[3] 140	[4] $65	−53.6	$17,000	[5] 2,598	[7] 2,393	−7.9
$5,000	[3] 290	[4] 200	−31.0	$20,000	[5] 3,160	[7] 2,968	−6.1
$7,500	[5] 687	[6] 576	−16.2	$25,000	[5] 4,412	[5] 4,170	−5.5
$10,000	[5] 1,114	[6] 958	−14.0				

[1] Does not include 10-percent surcharge.
[2] Uses provisions effective for tax year 1972.
[3] Uses minimum standard deduction of $600.
[4] Uses minimum standard deduction of $1,100.
[5] Itemizes deductible nonbusiness expenses.
[6] Uses 15-percent standard deduction.
[7] Uses $2,000 limit on 15-percent standard deduction.

TABLE 5.—TAX BURDEN UNDER PRESENT LAW, UNDER H.R. 13270, AND PERCENT TAX DECREASE IN 1972 (ASSUMES NONBUSINESS DEDUCTIONS OF 10 PERCENT OF INCOME)

Adjusted gross income (wages and salaries)	Single persons			Adjusted gross income (wages and salaries)	Single persons		
	Present law tax[1] (1)	H.R. 13270 tax[2] (2)	Percentage decrease in tax under H.R. 13270 (3)		Present law tax[1] (1)	H.R. 13270 tax[2] (2)	Percentage decrease in tax under H.R. 13270 (3)
$900	0	0	0	$7,500	1,168	1,005	−14.0
$1,160	$36	0	−100.0	$10,000	1,742	1,468	−15.7
$1,519	88	0	−100.0	$12,500	2,398	1,977	−17.6
$1,700	115	0	−100.0	$15,000	3,154	2,602	−17.5
$3,000	329	$180	−45.4	$17,500	3,999	3,320	−17.0
$4,000	500	344	−31.2	$20,000	4,918	4,098	−16.7
$5,000	671	524	−21.9	$25,000	6,982	5,635	−19.3

[1] Does not include 10 percent surcharge.
[2] Minimum standard deduction and standard deduction as in H.R. 13270 used where appropriate for taxpayers advantage.

O