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Compilation of Decisions Reached in Executive Session

COMMITTEE ON FINANCE
UNITED STATES SENATE
Russell B. Long, *Chairman*

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FOR IMMEDIATE RELEASE
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COMMITTEE ON FINANCE
UNITED STATES SENATE
2227 Dirksen Senate Office Bldg.

FINANCE COMMITTEE ACTS ON TAX REVISION ISSUES (H.R. 10612)

The Honorable Russell B. Long (D., La.), Chairman of the Senate Committee on Finance, announced today that the Committee had reached the following tentative decisions in its work on the House-passed tax revision bill (H.R. 10612):

1. Deletion of LAL provisions applicable to real estate.--The House bill contains a series of complex provisions designed to limit the deduction of such items as accelerated depreciation (depreciation in excess of straight-line), and interest and taxes incurred during the period of construction of improvements on real estate. The Committee agreed to delete these provisions. In their place the Committee has decided to treat interest (but not taxes) paid during the construction period and accelerated depreciation in excess of straight line as items of tax preference for purposes of the minimum tax. The Committee specifically reserved for later decision any changes in the structure and rate of the minimum tax.

2. Recapture of depreciation on real property.--The Committee approved the provisions of the House bill relating to recapture of depreciation on real property with one modification. Under the House bill, all depreciation in excess of straight line would be recaptured, no matter how long the property is held, except in the case of governmentally subsidized housing held for a specified period of time. Under present law this rule is applicable only to commercial real estate while in the case of residential property, after the property is held 100 months, recapture is phased down by one percentage point per month for the next 100 months. Thus there is no recapture under present law after residential property is held longer than 16 2/3 years.

Recapture of accelerated depreciation in the case of governmentally subsidized housing is phased down under present law after it is held 20 months, with no recapture on property held more than 120 months. Under the House bill, there would be full recapture during the first 100 months (8 1/3 years), with the recapture phased down during the next 100 months; property held more than 16 2/3 years would not be subject to the recapture provision. Under the Committee bill, the House provision on governmentally subsidized housing would apply only during 1977. For governmentally subsidized housing on which construction begins on or after January 1, 1978, full recapture would be applicable, no matter how long the property is held.

3. Deletion of LAL provisions applicable to farm operations.--The House bill contains a series of complex provisions designed to limit the current deduction of certain farm expenses. Farm expenses treated as accelerated deductions and subject to LAL under the House bill include expenses attributable to crops, animals, trees or similar property to the extent incurred before such items become productive or are disposed of. Also included are prepaid expenses for feed, seed, fertilizer, and similar farm supply expenses, and accelerated depreciation of livestock after it has become productive.

a. Farm losses limited to capital at risk.--In place of these provisions the Committee has decided to limit the deduction with respect to farm losses to the amount of capital at risk. This would exclude nonrecourse loan financing, as well as amounts which are protected against loss by guarantees, insurance or otherwise.

b. Prepaid expenses by farm syndicates.--Also approved was a provision to preclude current deduction by farm syndicates for the prepayment of feed, seed, fertilizer or similar farm supplies and amounts spent for the planting, cultivating, maintenance, or development of any grove, orchard or vineyard involving the raising of nuts or fruits. Instead, such expenditures would be capitalized and deducted as used or consumed; in the case of groves, orchards, and vineyards, expenditures would be deducted over the productive life of the trees.

c. Deletion of requirement that farm corporations use accrual method of accounting.--The Committee agreed to delete the provision of the House bill requiring corporations engaged in farming operations to use accrual and inventory accounting methods.

d. Farm excess deduction account.--The Committee agreed to the provision of the House bill under which no additions are to be made to the farm excess deduction account required by existing law for 1976 or subsequent years.

e. Waiver of statute of limitations for hobby loss elections.--The Committee agreed to the House provision which restricts the waiver of the statute of limitations in the case of hobby loss elections. Under existing law, the taxpayer is provided an opportunity to determine whether he has satisfied the rule limiting deductions incurred in an activity which is not engaged in for profit (Code section 183) on the basis of his experience over a five or seven year period. Under the provision agreed to, the waiver of the statute of limitations in these cases would be limited so that the waiver does not apply to unrelated items on the taxpayer's return.

PRESS RELEASE

FOR IMMEDIATE RELEASE
April 29, 1976

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

FINANCE COMMITTEE ACTS ON TAX REVISION ISSUES (H.R. 10612)

The Honorable Russell B. Long (D., La.), Chairman of the Senate Committee on Finance, announced today that the Committee continued its work on the House-passed tax revision bill (H.R. 10612) and made the following decisions:

Tax treatment of movies. -- Under present law motion pictures can be produced or purchased by limited partnerships or individuals which are able to obtain certain tax benefits based upon the use of nonrecourse financing and the deferral of tax liability. The House bill contains a series of provisions called Limitations on Artificial Losses (LAL), designed to limit the amount of deductions available through the use of these devices. In place of these highly specific and detailed provisions, the Committee has agreed to the following general restrictions and limitations on tax benefits available in connection with the production or purchase of motion pictures:

a. "At risk" limitation in the case of purchases of completed films and production of motion pictures. -- In the case of purchases of completed films and production of motion pictures, the Committee decided to limit the deduction for depreciation and losses to the amount which the taxpayer purchasing the film has "at risk". This would preclude the deduction of amounts financed through nonrecourse loans (except to the extent repaid).

b. Capitalization of production costs. -- In the case of the production of motion pictures, books, records, and similar property by a service company which does not own the film, etc., the Committee decided to require the service company to capitalize its costs of production. This would preclude expensing of costs which would normally be capitalized.

PRESS RELEASE

FOR IMMEDIATE RELEASE
April 30, 1976

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

FINANCE COMMITTEE ACTS ON TAX REVISION ISSUES (H.R.10612)

The Honorable Russell B. Long (D., La.), Chairman of the Senate Committee on Finance, announced today that the Committee continued its work on the House-passed tax revision bill (H.R. 10612) and made the following tentative decisions:

1. Tax treatment in the case of equipment leasing.--One means by which businesses acquire productive equipment is through the leasing of equipment. Two basic types of leasing arrangements are generally used. Under a "net lease", equipment is leased for a period approximating the useful life of property under lease and rental payments are set at a level which will cover the expenses of the lessor in connection with the acquisition of the property under lease. Under an "operating lease", property is generally leased for a shorter period than the useful life of the property and the lessor is responsible for the payment of items such as insurance and property taxes on the equipment. Under this latter type of lease, rental payments are generally made at a higher rate than under a net lease. Some taxpayers have been able to obtain the benefit of substantial tax deferral through the use of non-recourse financing and deductions for accelerated depreciation in equipment leasing transactions. The House bill would apply a series of provisions to limit any "artificial losses" in the case of equipment leasing. The Committee has agreed instead to impose the more general restrictions described below.

a. "At risk" limitation in the case of equipment leasing.--In the case of equipment leasing, the Committee decided to limit the deduction for depreciation to the amount which the taxpayer-lessor has "at risk" (plus any amounts of debt from the transaction for which the investor may be personally liable).

b. Applicability of the minimum tax.--Under present law excess depreciation and amortization on personal property subject to a net lease are included in the minimum tax base. The Committee decided to include excess depreciation and amortization from all types of personal property leases in the minimum tax base for individuals.

2. Tax treatment of sports franchises.--Under existing law owners of professional sports teams may determine the amount of their acquisition costs that they will allocate to player contracts (which are then subject to amortization over relatively short periods). Some taxpayers have been able to obtain the benefit of substantial tax savings by applying this amortization against ordinary income and later, when the franchise is sold, treating an equivalent amount as capital gains. The House bill addresses this problem through its limitation on artificial losses (LAL) concept in an attempt to limit the deductions available and the capital gains treatment that would otherwise be possible. The Committee agreed instead to substitute the following provisions:

a. Allocation of basis to player contracts.--In the case of the sale or exchange of a sports franchise the amount of the sales price allocated to player contracts by the purchaser could not exceed the amount of the sale price allocated to these contracts by the seller.

b. Recapture of depreciation on player contracts.-- Where there is a sale or exchange of a sports franchise, a part of the sales price would be allocated to those player contracts which were initially acquired with the original acquisition of the franchise by the seller and that sum so allocated would be recaptured as ordinary income by the seller. This would, in effect, apply existing recapture rules in the case of sports franchise sales. No change would be made in existing law for the tax treatment of dispositions of player contracts which were not among the group of player contracts purchased in connection with the original acquisition of the franchise.

PRESS RELEASE

FOR IMMEDIATE RELEASE
May 4, 1976

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

FINANCE COMMITTEE ACTS ON TAX REVISION ISSUES (H. R. 10612)

The Honorable Russell B. Long (D., La.), Chairman of the Senate Committee on Finance, announced today that the Committee had reached the following tentative decision in its work on the House-passed tax revision bill (H. R. 10612):

Intangible drilling and development costs. -- The House-passed bill contains a series of provisions designed to limit the deduction for intangible drilling costs incurred during drilling of oil and gas wells. In their place, the Committee has decided that the deduction for intangible drilling and development costs should be limited to the amount which the taxpayer has at risk with respect to any oil or gas property. A taxpayer would be considered to be at risk with respect to any borrowed funds used to finance intangible costs to the extent that the taxpayer is personally liable for repayment of the loan or has pledged property of established value as security for the loan.

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

FOR IMMEDIATE RELEASE
May 5, 1976

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

FINANCE COMMITTEE ACTS ON TAX REVISION ISSUES (H.R. 10612)

The Honorable Russell B. Long (D., La.), Chairman of the Senate Committee on Finance, announced today that the Committee continued its work on the House-passed tax revision bill (H.R. 10612) and made the following tentative decisions:

1. Partnership provisions.--The House bill contains a number of provisions pertaining to the tax treatment of partnerships. The Committee has taken the following action:

a. Additional first-year depreciation for partners.--Under present law, an owner of tangible personal property can claim depreciation in the first year the property is used and can elect to deduct additional depreciation equal to 20% of the cost of the property. The maximum amount of this additional depreciation is $2,000 ($4,000 for individuals filing joint returns) and is restricted to property with a useful life of six years or more. Where a partnership is the owner of such property, this limitation applies to each individual partner rather than the partnership as a whole. A corporation is not permitted to deduct more than $2,000 of additional first-year depreciation.

The Committee agreed to the provision of the House bill (section 210(a)) limiting the amount of additional first-year depreciation deductions a partnership may pass through to its partners to $2,000. Each partner would be required to aggregate additional first-year depreciation deductions from the partnership and all other additional first-year depreciation deductions which could be claimed. The total aggregate additional first-year depreciation deductions could not exceed $2,000 (or $4,000 in the case of a joint return).

b. Partnership syndication and organization fees.--Under present law, it has been common for limited partnerships to claim a deduction for payments made to a general partner for services rendered by him with respect to the syndication and organization of the limited partnership. A recent Internal Revenue Service ruling, Rev. Rul. 75-214, and Tax Court case, Jackson E. Cagle, Jr., 63 T.C. 86 (1974), on appeal to the Fifth Circuit Court of Appeals, have held that such payments represent capital expenditures and are not currently deductible. The House bill would require the capitalization of both organizational expenditures and the costs of syndication.

In lieu of the House provision (section 210(b)) the Committee decided that payments made in connection with the organization of a limited partnership should be amortized ratably over five years. Payments made in connection with the syndication of a limited partnership would be capitalized.

c. Retroactive allocations of partnership income or loss.--Presently, investments in limited partnerships are often made toward the end of the year. Prior to the entry of limited partners into the partnership, the partnership may have incurred substantial deductible expenses. Although it is not clear under present law whether retroactive allocations are permissible, in practice a full share of the partnership losses for the entire year is usually allocated to the limited partners entering the partnership at the close of the year.

The Committee agreed to the provision of the House bill (section 210(c)) providing that partnership income or loss, or any special item of income, deduction, or credit would be allocable to an incoming partner either ratably on a daily basis or by separating the partnership year into two or more segments to enable the allocation of such items by segment among the persons who were partners during the respective segments.

d. Partnership special allocations.--Under present law a partnership agreement (for limited or general partnerships) may allocate income, gain, loss, deduction, or credit among the partners in a manner that is disproportionate to the capital contributions of such partners. Such "special allocations" may be made by amending the partnership agreement at any time prior to the initial due date of the partnership tax return for the taxable year. Such special allocations will not be recognized if the principal purpose is to avoid or evade any income tax. However, it has been suggested that special allocations of taxable income or loss, instead of the allocation of specific items of income, gain, deduction, loss, or credit could be recognized even if the principal purpose of such an allocation is the avoidance or evasion of tax. The House bill provides a series of requirements which a partner receiving a special allocation would have to meet in order to be entitled to the tax benefits of the special allocation.

In lieu of section 210(d) of the House bill, the Committee agreed that special allocations of income, gain, loss, deduction, or credit among partners will be permitted unless the allocations do not have substantial economic effect. The purpose of this rule is to prevent the use of special allocations for tax avoidance purposes while permitting special allocations made for bona fide business purposes.

2. Treatment of interest on indebtedness.--Under present law there is considerable uncertainty as to the deductibility of prepaid interest. In 1968, the Internal Revenue Service published a ruling, Rev. Rul. 68-643, in which it took the position that the prepayment of interest by a cash basis taxpayer for a period of more than 12 months beyond the end of the current taxable year will be deemed to create a material distortion of income and will be allocated over the taxable years involved. Deductions for prepaid interest for not more than 12 months after the taxable year in which payment is made are considered on a case-by-case basis to determine whether a material distortion of income has resulted under this ruling. The House bill includes certain limitations with respect to the deductibility of prepaid interest.

In place of the House provision (section 205 of the House bill) the Committee has agreed to require a taxpayer using the cash method of accounting to capitalize prepaid interest and deduct the interest only in the taxable years for which the interest represents a charge for the use or forebearance of money. However, a current deduction would be allowed in the case of "points" paid by a cash basis taxpayer on an indebtedness incurred in connection with the purchase, or improvement of, the taxpayer's residence and secured by that residence (to the extent the payment of points is an established business practice in the area where the transaction takes place and the "points" do not exceed the amount of points generally charged there).

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

FOR IMMEDIATE RELEASE
May 12, 1976

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

FINANCE COMMITTEE ACTS ON TAX REVISION ISSUES (H.R. 10612)

The Honorable Russell B. Long (D., La.), Chairman of the Senate Committee on Finance, announced today that the Committee continued its work on the House-passed tax revision bill (H.R. 10612) and made the following tentative decisions:

1. Minimum tax. -- The present minimum tax is imposed on individuals and corporations; it is added to the taxpayer's regular income tax. The rate of the minimum tax is 10 percent, and nine separate items of tax preference are presently subject to the minimum tax. Preference income which does not exceed $30,000 is exempt from the minimum tax. In addition, a deduction equal to the amount of a taxpayer's regular income tax is allowed in determining preference income subject to the minimum tax, and regular income tax in excess of preference income may be carried forward for up to seven years and then used to offset preference income.

The House bill contains a number of modifications that would be made to the minimum tax. The changes approved by the House apply only to individuals, estates, and trusts. The rate of tax would be increased from 10 percent to 14 percent. The exemption for preference income would be decreased from $30,000 to $20,000 and phased out as preference income increases above $20,000 to $40,000. The House bill would eliminate the deduction for regular income taxes and would add additional items of tax preference. The Finance Committee has taken the following action in connection with these proposed modifications:

a. Application to individuals, trusts, and estates. -- The minimum tax would be payable by individuals, trusts, and estates and would be added to a taxpayer's regular income tax, as under present law. (There would be no change in the minimum tax on corporations.)

b. Rate of minimum tax. -- The minimum tax rate would be set at 15 percent.

c. Exemption for preference income. -- An exemption of $5,000 or the amount of regular income taxes paid, whichever is greater, would be provided in determining the amount of preference income subject to the minimum tax.

d. Items of tax preference. -- Items of tax preference would include the following items from present law:

(1) The excluded portion of capital gains.
(2) The excess of percentage over cost depletion.
(3) The bargain element of stock options.
(4) The excess of accelerated depreciation over straight line depreciation on real property.
(5) The excess of accelerated amortization over straight line amortization for railroad rolling stock.

In addition, the following new items of tax preference would also be included:

(6) The excess of investment interest over investment income. In the case of limited partnerships, that portion of each limited partner's loss representing investment interest over investment income from the partnership, whether or not such partnership is classified as conducting an active trade or business, would be treated as an item of tax preference. Interest paid with respect to a mortgage on an individual's principal residence would be excluded from this item of tax preference. Finally, the interest deduction limitation contained in present law (section 163 (d) of the Internal Revenue Code of 1954) would be repealed.

(7) The excess of itemized deductions, other than deductions for medical expenses and casualty losses, over 60 percent of adjusted gross income (less any excess investment interest included as an itemized deduction).

(8) Intangible drilling costs in excess of the costs deductible had they been capitalized and in excess of related income from oil and gas wells.

(9) Real estate construction period interest.

(10) Accelerated depreciation on all personal property subject to a lease (present law applies only to net lease property).

2. Maximum tax on personal service and investment income. -- Under present law a maximum tax of 50 percent is imposed on personal service income (sometimes called "earned income"). Such income is limited to wages, salaries, professional fees and other compensation for personal service, including a reasonable amount of self-employment income (not in excess of 30 percent of the profits of the business).

a. Revision of maximum tax. -- The Committee has agreed to apply the maximum tax to a limited amount of investment income. The maximum tax of 50 percent would apply to a taxpayer's investment income no greater in amount than the taxpayer's earned income, but in no event could the investment income eligible for the 50 percent limit exceed $100,000. Investment income would not include capital gains. Personal service income ("earned income") would include pension payments other than lump-sum distributions from pension plans.

The Committee would also repeal the $30,000 exemption for preference income which must be used to offset personal service income eligible for the 50 percent maximum tax rate. In addition, the list of preferences would be revised to conform with and include all items of tax preference subject to the minimum tax as listed above.

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

FOR IMMEDIATE RELEASE
May 13, 1976

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

FINANCE COMMITTEE ACTS ON TAX REVISION ISSUES (H.R. 10612)

The Honorable Russell B. Long (D., La.), Chairman of the Senate Committee on Finance, announced today that the Committee continued its work on the House-passed tax revision bill (H.R. 10612) and made the following tentative decisions:

1. Provisions affecting U. S. individuals abroad. -- Presently U. S. citizens working abroad are permitted to exclude from income up to $20,000 of income earned abroad for periods in which they reside outside the United States for 17 out of 18 months or during the period they are bonafide residents of foreign countries. This exclusion is increased to $25,000 for individuals who have been bonafide residents of foreign countries for three years or more.

Under the House bill, the $20,000 exclusion (or $25,000 exclusion where applicable) for income earned abroad by U. S. citizens residing overseas would be phased out over a four-year period, except that employees working on construction projects (other than oil and gas wells) would continue to receive the full $20,000 exclusion through the end of the four-year phase-out period. The $20,000 exclusion would also be retained for employees of U. S. charitable organizations who work abroad.

In lieu of the House provisions, the Committee agreed to retain the exclusion under present law with these modifications:

a. The amount of foreign taxes paid on income which is eligible for the exclusion would not be allowed as a foreign tax credit against U. S. income tax.

b. Additional income received by individuals (beyond the income eligible for the exclusion) would be subject to U. S. tax at the higher tax rate brackets which would apply if the excluded income were also subject to tax.

c. Also ineligible for the exclusion would be any income earned abroad which is received outside of the country in which earned in order to avoid tax in that country.

The Committee agreed to the provision of the House bill permitting individuals claiming the standard deduction a foreign tax credit against U. S. income tax for foreign taxes paid.

2. U. S. taxpayers married to nonresident aliens. -- Present law permits a husband and wife to file a joint income tax return even though one of the spouses may have no gross income or deductions. However, a joint return may not be made if either a husband or wife at any time during the taxable year is a nonresident alien.

The Committee agreed to the provisions of the House bill which would permit U. S. taxpayers married to nonresident aliens to file joint returns with their spouses if both taxpayers elect to be taxed on their worldwide income. The Committee changed the effective date for this provision contained in the House bill and made it effective for taxable years beginning after December 31, 1972. The Committee also approved the House provision making community property laws of foreign countries inapplicable to married taxpayers for U. S. tax purposes where one spouse is a nonresident alien.

3. Treatment of foreign trusts and excise tax on transfers of property to foreign persons. -- Under present law, trusts which qualify as being comparable to a nonresident alien individual are taxed as foreign trusts. In general, a U. S. taxpayer-beneficiary of a foreign trust is taxed in the same fashion on distributions as would a beneficiary of a domestic trust. However, in certain circumstances, a U. S. beneficiary under a foreign trust created by a U. S. person is taxed differently from a beneficiary of a domestic trust with respect to an accumulation distribution which includes capital gains income earned by the trust. In such instances a portion of the distributions to a U. S. beneficiary is taxed at favorable capital gains rates although, had such distribution been made by a domestic trust, the favorable tax rate for capital gains would only apply after all other income is distributed and taxed as ordinary income.

In addition, present law imposes an excise tax of 27-1/2 percent on certain transfers of property to foreign trusts as well as to foreign corporations (if it is a contribution of capital) and to foreign partnerships. The excise tax is only imposed on the transfer of stocks or securities and applies only to the value in excess of the adjusted basis of the stock or securities over its adjusted basis in the hands of the transferor.

U. S. grantors of foreign trusts with U. S. beneficiaries under the House bill would be taxed currently on the income of these trusts under the grantor trust rules of present law. Also, U. S. beneficiaries of foreign trusts under which trust income is not taxed to the grantor would be required to pay a nondeductible interest charge when accumulation distributions are received by the beneficiary. The interest charge would be 6 percent per year on the amount of the tax on the trust distribution.

Finally, under the House bill, the existing excise tax on transfers of stocks and securities to foreign entities would be increased from 27-1/2 percent to 35 percent and would be extended to transfers of other types of property in addition to stocks and securities. The excise tax would apply only to any unrealized appreciation in the value of the assets transferred.

The Committee agreed to the provisions of the House bill relating to the treatment of foreign trusts and the excise tax on transfers of property to foreign persons, with these modifications:

a. The provision concerning the current taxation of trust income would apply only to transfers to foreign trusts made after May 29, 1974 (compared with May 21 in the House bill).

b. A taxpayer could elect to be taxed on the unrealized gain on the property transferred to foreign persons and to receive an adjusted step-up in basis if such treatment were elected.

4. Foreign tax deferral. -- Generally, the foreign source income of a foreign corporation under present law is subject to U. S. tax only when that income is actually remitted to the U. S. corporate or individual shareholders as a dividend. U. S. tax is then imposed on the shareholder-recipient and not the foreign corporation. The practice of imposing no U. S. tax until and unless income is distributed to U. S. shareholders is commonly referred to as tax deferral. No basic changes in the present practice of deferral were adopted by the House. However, a number of technical provisions relating to deferral and the taxation of foreign subsidiaries of U. S. corporations were included in the House bill.

The Committee agreed to the provision of the House bill under which U. S. shareholders holding stock of less-developed country corporations for ten years or more would receive the same treatment U. S. shareholders in other controlled foreign corporations receive when they dispose of their shares in foreign corporations and realize a gain. This means that the gain realized by the less developed country corporation shareholder upon disposition of his stock would be treated as a dividend subject to ordinary income tax treatment to the extent of the shareholder's portion of the less developed country corporation's accumulated earnings and profits.

The Committee agreed to the House provision which would provide an exception to the tax haven rules for foreign subsidiaries for investment income on earnings which a foreign casualty insurance company must retain to satisfy State insurance solvency requirements (this income would thus not be taxed currently).

Under the House bill, an exception to the tax haven rules for foreign subsidiaries would be provided for income from shipping between two or more points within the country in which a foreign shipping subsidiary is incorporated and in which the ship is registered. In addition, if a company has substantially all of its assets in foreign shipping operations, repayments of unsecured loans would be treated as reinvestment in shipping operations for purposes of the tax haven rules (in the same manner as the repayment of secured loans is treated).

The Committee agreed to the House provision and added an additional exception in the case of a supply shipping operation between a point on shore and an offshore point which is not within the boundaries of another country. An exception would also be provided in the case where the taxpayer has shipping income but owns no shipping assets, arranges no long-term charters, and no natural resources, agricultural commodities, or goods produced by persons related to the taxpayer are transported by the chartered ships.

At present, income from the insurance of foreign risks is taxed as though it arises at the place of signing of the contract. This rule lends itself to manipulation by insurors and the insured. The Committee agreed to determine the source of income from insurance of foreign risks by looking to the location of the risk rather than the place where the contract is signed.

Under the House bill, an exception to the tax haven rules for foreign subsidiaries would be provided for income from the sale of agricultural commodities which differ in grade or type from agricultural products grown in the United States. The Committee agreed instead to provide an exception for the sale of all agricultural commodities grown and sold outside the U. S.

5. Money or other property moving in or out of the United States.--Under present law, interest, dividends, and other similar types of income earned in the U. S. by a nonresident alien or foreign corporation are subject to a 30 percent tax on the gross amount earned if such income or gains are not related to the conduct of a trade or business within the U. S. This tax is generally collected through withholding by the person making the dividend or interest payment to the foreign recipient of the income and is therefore commonly referred to as a withholding tax. Interest from deposits in the U. S. with persons engaged in the banking business is exempt from this tax. This exemption is scheduled to expire on December 31, 1976.

The Committee approved the provision of the House bill which would make permanent the exemption from the 30 percent withholding tax on bank deposit interest payments to nonresident aliens.

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

FOR IMMEDIATE RELEASE
May 14, 1976

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

FINANCE COMMITTEE ACTS ON TAX REVISION ISSUES (H.R.10612)

The Honorable Russell B. Long (D., La.), Chairman of the Senate Committee on Finance, announced today that the Committee continued its work on the House-passed tax revision bill (H.R. 10612) and made the following tentative decisions:

1. Money or other property moving in or out of the United States.--Under present law, interest, dividends, and similar types of income earned in the U. S. by a nonresident alien or foreign corporation are subject to a 30 percent tax on the gross amount earned if such income or gains are not related to the conduct of a trade or business within the U. S. This tax is generally collected through withholding by the person making the dividend or interest payment to the foreign recipient of the income and is, therefore, commonly referred to as a "withholding tax." Interest earned by foreign recipients on deposits in the U. S. with persons engaged in the banking business is exempt from this tax. This exemption is scheduled to expire on December 31, 1976.

a. Interest paid to nonresident aliens on investments made in the U. S.--The Committee agreed to make permanent the present exemption from the 30 percent withholding tax on bank deposit interest payments to nonresident aliens and foreign corporations. The Committee also agreed to exempt other interest paid to nonresident aliens and foreign corporations from the 30 percent withholding tax.

b. Treatment of reorganizations involving foreign corporations.--Under existing law, certain kinds of corporate organizations, reorganizations, and liquidations can be carried out without the imposition of any U. S. tax on the corporation or its shareholders. If a foreign corporation is involved in a similar transaction, however, then tax-free treatment is not permitted unless the Internal Revenue Service rules, before the transaction occurs, that a principal purpose of the transaction is not the avoidance of Federal income taxes. An IRS ruling is required for each transaction unless the transaction only involves a change in the form of organization of a lower tier foreign subsidiary and no change in ownership of the subsidiary.

The Committee agreed to the provisions of the House bill (section 1042) relating to reorganizations involving foreign corporations:

(1) The requirement of present law that advance rulings from the IRS be obtained for all reorganization-type transactions involving foreign corporations would be modified so that rulings would be required only for transfers of property out of the United States. Such rulings could be requested up to 183 days after the beginning of the transaction. These rulings would be subject to Tax Court review.

(2) For transfers of property into the United States and transfers among foreign corporations, the IRS would be required to draft regulations by January 1, 1978, specifying when the portion of the gain realized on such transfers which is attributable to accumulated earnings is to be treated as a dividend paid to the U.S. shareholders.

(3) The provision of present law taxing gain realized from the sale of stock of a foreign subsidiary as ordinary income to the extent of accumulated earnings would be extended to apply to certain nontaxable transfers of such stock where the non-recognition provisions of present law would otherwise prevent the taxation of the earnings attributable to the stock.

c. Contiguous country branches of domestic insurance companies.-- Under present law, a domestic mutual life insurance company is subject to tax on its worldwide taxable income. If the company pays foreign income taxes on its income from foreign sources then it is allowed a foreign tax credit against its U.S. tax liability for foreign source income.

The Committee agreed to the provisions of the House bill (section 1043) (with a technical amendment) relating to contiguous country branches of domestic insurance companies:

(1) Mutual life insurance companies maintaining separate operations in countries contiguous to the United States would be permitted to treat such operations as if carried on through a foreign subsidiary. The corporations would be treated as having transferred their contiguous country life insurance assets to these branches and would be subject to the normal tax requirements regarding transfers of property out of the United States (except that losses would be netted against gains).

(2) Stock life insurance companies would be permitted to transfer assets of their foreign branch operations in contiguous countries to foreign subsidiaries under rules similar to those applied above to mutual life insurance companies.

d. Transitional rule for bond, etc. losses of foreign banks. -- Under present law, as amended by the Tax Reform Act of 1969 (P.L. 91-172), financial institutions may not treat net gains from the purchase and sale of corporate and government bonds, etc., as capital gains. The 1969 Act amendments treat gains and losses from these transactions as ordinary income and ordinary losses. This change was also made applicable to foreign corporations which are considered banks. These corporations had previously treated income from the transactions in question as resulting either in capital gains or capital losses.

The Committee agreed to section 1044 of the House bill under which foreign banks would be allowed the same transitional treatment as was provided in 1969 for domestic banks with respect to carrying forward pre-1969 capital losses to be offset against gains from subsequent sales or exchanges of bonds, debentures, notes or certificates or other evidence of indebtedness.

2. <u>Foreign tax credit provisions</u>.--Taxpayers subject to U. S. tax on foreign income, under present law, are permitted to take a foreign tax credit for the amount of foreign taxes paid on income from sources outside the U. S. The foreign tax credit is also allowed with respect to dividends received by U. S. shareholders from foreign corporations operating in foreign countries and paying foreign taxes. To prevent taxpayers from using foreign tax credits to reduce U. S. tax liability on income from sources within the U. S., two alternative limitations on the amount of foreign tax credits which can be claimed are applicable under present law. The overall limitation limits the amount of foreign tax credits to the ratio of taxable income from sources outside the U. S. (less relevant deductions) to worldwide taxable income. Under the per-country limitation the same calculation made under the overall limitation is made on a country-by-country basis. Allowable foreign tax credits from any single foreign country cannot exceed the ratio of taxable income from that country to worldwide taxable income

Under present law, as amended by the Tax Reduction Act of 1975, the foreign tax credit on income from oil and oil-related activities must be computed under a separate overall limitation which applies only to oil-related income. Any losses from oil-related activities are "recaptured" in future years through a reduction in foreign tax credits allowable to offset subsequent foreign oil-related income.

<u>Repeal of per-country limitation</u>.--The Committee agreed to repeal the per-country limitation on the foreign tax credit for all foreign countries and for possessions of the U. S. with a three-year transition period for certain mining investments and investments in U. S. possessions.

<u>Recapture of foreign losses</u>.--Under the House bill, losses from overall foreign operations which reduce U. S. tax on U. S. income would be recaptured in subsequent years by reducing the maximum amount of foreign tax credits which could be claimed in those years.

The Committee approved the provisions of the House bill with these modifications:

a. Recapture of losses incurred during the transition period in the House bill provision repealing the per-country limitation on the foreign tax credit for certain mining investments and investments in U. S. possessions would apply only on a per-country basis.

b. Taxpayers would be allowed to elect to have recapture occur more rapidly than otherwise required in order to reflect the fact that some countries have net operating loss rules similar to the U. S. rules.

c. An exception from the recapture rules would also be provided where a take-over by a foreign Government is accomplished by acquisition, before the effective date of the provision, using obligations of the foreign Government which are disposed of by the taxpayer at a loss; and

d. Losses arising from worthless securities would be excepted from the recapture rules where the securities became substantially worthless prior to the effective date of the provision.

<u>Dividends of corporations operating in less-developed countries</u>.--The Committee agreed to the House provision (section 1033) under which dividends from less-developed country corporations would be treated in the same manner as dividends from other

corporations. This means the dividends would be "grossed up" by the amount of taxes paid to less-developed countries for purposes of computing the foreign tax credit (and taxable income).

The Committee agreed to the House provision (section 1034) under which foreign source capital gains and losses would be netted against domestic source capital gains and losses in computing the foreign tax credit limitation. In the case of corporations, amounts included in the foreign tax credit limitation would be adjusted to take into account the fact that capital gains are subject to a 30 percent tax rate in the U. S. Also, capital gains from property sold outside of the country in which was located the business in which the the property was used (or, for an individual, outside of the country of residence) would not be eligible for a foreign tax credit unless a substantial foreign tax (i.e., 10 percent or more) were paid on the gain.

The Committee agreed to the House provision (section 1035) under which amounts not allowed as foreign tax credits on foreign oil extraction income in 1978 and later years (as a result of the amendments made by the Tax Reduction Act of 1975) could be carried back to taxable years ending in 1975 to 1977.

The Committee agreed to correct a technical error in the amendments made by the Tax Reduction Act of 1975 which inadvertently excluded interest from the definition of foreign oil-related income in the case of domestic subsidiaries operating abroad.

The Committee agreed that the rules for computing the deemed paid credit under section 902 of the Internal Revenue Code which permit U.S. corporations receiving a dividend from a foreign corporation to treat a pro rata portion of the foreign income taxes paid by the foreign subsidiary to be deemed paid by the U. S. corporation, which is then allowed a foreign tax credit in that amount, to be extended to deemed dividends under Subpart F.

3. Special categories of corporate tax treatment--Western Hemisphere Trade Corporations.-- Under present law, domestic corporations qualifying as "Western Hemisphere Trade Corporations" (WHTC's) are entitled to a deduction which may reduce the applicable corporate income tax rate by as much as fourteen percentage points below the applicable rate for other domestic corporations. The Committee approved the provision of the House bill (section 1052) which phases out over a five-year period the 14 percent lower tax rate for WHTC's according to the following table:

For taxable year beginning in	Percentage
1976	11%
1977	8
1978	5
1979	2
1980 and later years	0

Corporations conducting business in possessions.--Corporations operating a trade or business in a possession of the U. S., under present law, are entitled to exclude from gross income all income from sources outside the U. S., including foreign source income earned outside of the possession in which they conduct business operations, under certain circumstances. The exclusion of possessions income applies to corporations operating in Puerto Rico, Guam, the Canal Zone, and Wake Island. The exclusion also applies to business operations of individuals in the Canal Zone and Wake Island.

The Committee approved the provision of the House bill (section 1051) which would provide a new tax credit for U. S. corporations qualifying as possessions corporations (to replace the income exclusion provided under present law). The tax credit would equal the U. S. tax attributable to the possessions corporation's income from a possessions trade or business and from qualified possessions' investments. Other income (including other foreign source income) of a possessions corporation would be subject to U. S. tax.

Under the House bill, U. S. corporations receiving dividends from possessions corporations would be eligible for the appropriate dividends received deduction (either 85 percent or 100 percent). In addition, the Committee agreed that taxes paid to a possession on the repatriated income would not be eligible for the foreign tax credit.

Under the House bill, in order to qualify as possessions corporations (in addition to the requirements of present law), corporations would be required to elect to remain in possessions corporation status for a minimum of 10 years. In addition, the Committee specified that if after the 10-year period it becomes disqualified, a new 10-year election must be made.

China Trade Act corporations.--The Committee approved the substance of the provision of the House bill (section 1053) which would phase out the special tax benefits for China Trade Act corporations. However, the Committee agreed to a two-year transition rule (rather than the four years agreed to by the House), with a 50 percent reduction of the present benefits in each year.

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

FOR IMMEDIATE RELEASE
May 19, 1976

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

FINANCE COMMITTEE ACTS ON TAX REVISION ISSUES (H.R. 10612)

The Honorable Russell B. Long (D., La.), Chairman of the Senate Committee on Finance, announced today that the Committee continued its work on the House-passed tax revision bill (H.R. 10612) and made the following tentative decisions:

1. Domestic International Sales Corporations (DISCs) and other foreign income provisions. -- Under present law, a corporation organized as a Domestic International Sales Corporation (DISC) is not liable for corporate income taxes. The profits of a DISC are taxed when actually distributed to its shareholders. Each year a DISC is deemed to have distributed income representing 50 percent of its profits and that income is subject to current taxation at the shareholder level. To be classified as a DISC, at least 95 percent of the corporation's assets and its gross income must be export-related and derived from export-related activities. The President is provided with authority to exclude from export property eligible for DISC benefits any property he determines by executive order to be in short supply. In addition, energy resources such as oil and gas and depletable minerals are ineligible for DISC benefits. Finally, products which are prohibited or restricted from export by reason of scarcity under the Export Administration Act of 1969 are ineligible for DISC benefits.

The House bill makes a number of changes in the DISC provisions. Products sold for use as military equipment and agricultural products not in surplus in the U. S. would be ineligible for DISC benefits. DISC benefits would only apply to incremental export sales over a designated base period. An exemption from this requirement is provided for companies whose total DISC benefits are less than $100,000 per year.

The Finance Committee has agreed to the following modifications of the DISC provision:

a. Military equipment sales would be eligible for DISC benefits if the equipment is competitive with foreign manufactured equipment.

b. Agricultural product sales would continue to be eligible for DISC benefits.

c. Corporations with earnings exceeding $100,000 claiming DISC benefits would be allowed such benefits only with respect to DISC receipts in excess of 60 percent of base period receipts of the DISC. For 1977 and 1978 the base period would be the average receipts for any three of the four years 1973 - 1976. Beginning in 1979, the four years used to determine base period receipts would move forward one year each year.

d. The incremental rule regarding DISC receipts, including the fixing of a base period, would not apply in the case of agricultural product exports until 1980. The base period would then be any three of the prior five years.

2. Denial of tax benefits to taxpayers participating or cooperating with an international boycott. -- The Committee approved a provision to deny foreign tax credits, the right to defer tax on the unrepatriated earnings of controlled foreign subsidiary corporations, DISC benefits, and the exclusion for income earned abroad by certain eligible U. S. citizens, where a person participates in or cooperates with an international boycott by agreeing, as a condition of doing business (directly or indirectly) within a country or with the government, a company, or a national of a country:

a. to refrain from doing business in another country or with the government, companies, or nationals of another country;

b. to refrain from doing business with any United States person engaged in trade in another country or with the government, companies, or nationals of another country;

c. to refrain from doing business with any company whose ownership or management is made up, all or in part, of individuals of a particular nationality or to remove (or refrain from selecting) corporate directors who are individuals of a particular nationality; or

d. if he agrees, as a condition of the sale of a product to the government, a company, or a national of a country, to ship such products only on a carrier which is not on an international boycott list.

3. Modification of foreign tax credit limitation on foreign oil and gas extraction income for individuals. -- Amendments under the Tax Reduction Act of 1975 set a limitation on the foreign tax credit which may be claimed in connection with foreign oil and gas extraction income. Under this limitation, the foreign tax credit is limited to two percentage points above the U. S. rate (50 percent) multiplied by the taxpayer's foreign oil and gas extraction income. Individuals who receive foreign oil extraction income are presently subject to the 50 percent limitation on foreign tax credits attributable to that income even though their effective U. S. tax rate exceeds 50 percent.

The Committee agreed that in the case of individuals, the 50 percent limitation would be replaced with a limitation equal to the taxpayer's average effective tax rate on all taxable income multiplied by the taxpayer's foreign oil extraction income.

4. Transition rule for recapture of foreign oil-related losses. -- The amendments under the Tax Reduction Act of 1975 provides that foreign oil-related losses which have been deducted from domestic income will be recaptured in a subsequent profitable year by limiting the foreign tax credits available with respect to such subsequent foreign oil-related income. This provision is applicable to losses sustained in taxable years ending after December 31, 1975.

The Committee has agreed to provide a transition rule in connection with the recapture provision of present law for foreign oil-related losses incurred before January 1, 1979, pursuant to a binding contract in effect before July 1, 1974. Under the transition rule, the amount of the loss which could be recaptured in any year would be limited to 15 percent of the loss in each of the first four years in which foreign oil-related income is earned. The remaining loss would be recaptured in the fifth year.

5. Investments by foreign subsidiaries of U. S. corporations in U. S. property. -- Under present law, investments by foreign subsidiaries of U. S. corporations in U. S. property are taxed to the U. S. corporation as a dividend. The House bill limits the definition of an investment in U. S. property so as to treat as a dividend only investments in the stock or obligations of a related U. S. person or intangible property which is leased to, or used by, a related U. S. person.

The Committee has approved a similar provision. The definition of investments in U. S. property would be modified to permit foreign subsidiaries to make portfolio investments in unrelated entities in the United States. Also, leases between a foreign subsidiary and a related U. S. person would be treated as investments in U. S. property only in cases where the property leased is located in the United States.

6. Modification of foreign tax credit limitation on foreign oil and gas extraction income for regulated utilities.-- The definition of foreign oil-related income would be modified, under the Committee's decision, to exclude income from the transmission and distribution of natural gas by a regulated public utility for use within the utility's own distribution system within the country in which such system is located, if the company so elects.

7. Investment tax credit in the case of movies and television films.-- Under present law an investment tax credit for tangible personal property placed in service by the taxpayer is provided. To qualify for the full credit, the property must have a useful life of seven years and, in addition, there cannot be any predominant foreign use of the property during any taxable year. Prior to 1971, it was not clear whether the investment credit was available for movies or television films. Amendments made under the Revenue Act of 1971 made clear that motion pictures and television films are to be treated as intangible personal property eligible for the investment tax credit. However, the issue is still being litigated for years prior to 1971 and a number of issues remain unsettled, including how to determine the useful life of a film, the basis on which the credit is to be computed, and how to determine whether there has been a predominant foreign use of the film.

The Committee generally agreed to section 802 of the House bill, relating to the investment tax credit for movies, with the following modifications:

a. The credit would be available for educational films (as well as motion picture and television films).

b. Any taxpayer who has filed suit prior to January 1, 1976, regarding his entitlement to the investment tax credit for any prior year may elect to have his right to the investment credit for all years beginning prior to January 1, 1975, determined under present law as interpreted by the courts, rather than by any of the alternatives set forth under the proposal. However, taxpayers wishing to use this election would be required to notify the IRS within 30 days after enactment of this legislation.

c. With respect to the issue of "participations", the Committee provided that "participations" could be included in the investment credit tax base subject to certain limitations:

(1) "Participations" paid with respect to any one individual in connection with any one film could not exceed $1 million;

(2) Subject to rule (1), "participations" could be included in the investment tax credit base to the extent of the lesser of (i) 50 percent of qualifying participations, or (ii) 25 percent of the production costs of the taxpayer's films for the year. This is to be determined on a vintage year basis.

d. The Committee provided that carryovers for unused investment tax credits, whether attributable to periods prior to 1971 or subsequent to 1971, would be permitted under the normal rules governing the future use of excess investment tax credits.

8. Deduction for expenses attributable to business use of homes.-- Under the House bill, a taxpayer would not be permitted to deduct any expenses attributable to the use of his home for business purposes except to the extent attributable to the portion of the home used exclusively on a regular basis as:

(a) the taxpayer's principal place of business, or

(b) a place of business which is used for patients, clients, or customers in meeting or dealing with the taxpayer in the normal course of business.

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Further, in the case of an employee, the business use of the home must be for the convenience of his employer.

In addition, an exception is provided which allows a deduction for the allocable expenses in storing inventory in the taxpayer's home.

An overall limitation is provided which limits the amount of the deductions to the income generated by the business activity of the taxpayer in his home.

Committee amendment. -- The Committee agreed that the provisions of the House bill disallowing the deduction would not apply to the extent that the space is used exclusively and on a regular basis in the conduct of:

a. The taxpayer's trade or business of selling goods or services, but only if the dwelling unit is the sole fixed location of such trade or business, or

b. the business of the taxpayer's employer, for which no other office or fixed location is provided by the employer. The provisions would also not apply in the case of a free-standing structure used exclusively for business purposes.

9. Deduction for expenses attributable to rental of vacation homes. -- Under the House bill, if a vacation home is used by a taxpayer for personal purposes for more than two weeks or 5 percent of the actual business use (that is, rental time), then the deductions allowed in connection with the vacation home cannot exceed the gross income from the business use (rental) of the vacation home.

In addition, where the two weeks or 5 percent rule applies, the deductions attributed to the rental activities would be limited to the proportion which actual rental use bears to the total actual use of the property (that is, business use plus personal use). However, expenses which are allowable in any event (such as interest and taxes) would not be limited by this provision.

Committee amendment. -- The Committee agreed to the House bill with these changes:

a. The percentage allowed for personal use by a taxpayer would be increased to 10 percent.

b. If the property is rented for less than one month during the year, there would be neither operating gain nor loss for tax purposes.

10. Deduction for attending foreign conventions. -- Under the House bill, deductions would be allowed for expenses incurred in attending not more than two conventions, educational seminars, or similar meetings, outside the United States, its possessions, and the Trust Territory of the Pacific.

The amount of the deduction for transportation expenses to and from these foreign conventions could not exceed the cost of air fare based on coach or economy class charges.

Transportation expenses would be deductible in full only if more than one-half of the total days of the trip (excluding the days of transportation to and from the site of the convention) are devoted to business-related activities. If less than one-half of the total days of the trip are devoted to business-related activities, a deduction would be allowed for transportation expenses only in the ratio of the business time to total time.

Deductions for subsistence expenses, such as meals, lodging and other ordinary and necessary expenses, paid or incurred while attending the convention would be limited to the fixed amount of perdiem allowed to government employees at the location where the convention is held. However, in order to deduct subsistence expenses up to this limitation for a day, there must be at least six hours of business-related activities scheduled daily (or 3 hours for a deduction for one-half day) and the taxpayer must have attended two-thirds of these activities.

<u>Committee amendment</u>. -- In lieu of the House provision, the Committee agreed to deny a deduction for foreign travel expenses (including transportation, meals and lodging) held outside North America (including the Caribbean) unless, taking into account the factors enumerated below, it is more reasonable to hold the meeting outside the North American area. This rule would provide an exception for a meeting conducted by an organization which draws from foreign members to the extent the number and location of its foreign meetings are reasonable in view of the number of foreign members and attendees and their geographic dispersion. In addition, an exception would also be provided where the subject matter of the meeting and purpose of the organization are such that it is more appropriate to hold the meeting abroad rather than in the U. S.

PRESS RELEASE

FOR IMMEDIATE RELEASE
May 20, 1976

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

FINANCE COMMITTEE ACTS ON TAX REVISION ISSUES (H.R. 10612) AND ON H.R. 8948 - GAO AUDIT OF IRS

The Honorable Russell B. Long (D., La.), Chairman of the Senate Committee on Finance, announced today that the Committee continued its work on the House-passed tax revision bill (H.R. 10612). The Committee also ordered favorably reported H.R. 8948 with an amendment.

H.R. 8948 -- GAO Audit of Internal Revenue Service, etc. -- The Committee ordered favorably reported H.R. 8948 with an amendment. The House-passed bill would permit the General Accounting Office to audit the Internal Revenue Service and the Bureau of Alcohol, Tobacco and Firearms, and would provide access to tax returns and tax return information in connection with such audits. The Committee amendment would limit access to tax returns and tax return information to instances where prior consent has been obtained from the Ways and Means Committee, the Finance Committee, or the Joint Committee on Internal Revenue Taxation.

H.R. 10612 -- FURTHER COMMITTEE ACTION

1. Contributions to capital of public utilities in aid of construction. -- Contributions to capital of public utilities in aid of construction occur where a builder, customer, or governmental unit contributes either utility-type facilities or cash to a utility as a means of financing the construction of needed utility facilities. These contributions can include the contribution of a completed water system by a developer or contributions of cash by a customer to cover the cost of connecting his home to the utility. Prior to February 1, 1976, the Internal Revenue Service took the position that such contributions were not taxable to the utility under section 118 of the Code as contributions to capital. However, after that date, the Service has announced in Revenue Ruling 75-557 that it will treat such contributions as income to the utility. Under the Service position, there can be a substantial amount of income bunched into the year of contribution even though most of the expenses associated with that income might not accrue for years after the contribution.

The Committee agreed to an amendment which basically adopts the prior position of the Internal Revenue Service that contributions in aid of construction are not taxable under section 118 of the Code as contributions to capital. The amendment has the same net effect as if the contributions were treated as income recognized on a pro rata basis over the life of the asset. Any contributed funds which are not spent within a reasonable time for construction of utility facilities would be included in income at that time.

2. Limitation on capital gain throwback rule to distribution made prior to effective date of repeal of provision.-- A trust is generally treated as a separate entity and is taxed in the same manner as an individual under present law. Certain trusts accumulate income for designated beneficiaries. Beneficiaries are then taxed on distributions received from accumulation trusts in substantially the same manner as if the income had been distributed to the beneficiary as earned by the trust instead of having been accumulated in the trust. This procedure is referred to as the "throwback" rule under which distributions of accumulated income to beneficiaries are thrown back to the year in which they would have been taxed to the beneficiary if they had been made currently. Present law also provides an unlimited throwback rule for capital gains allocated to the corpus of an accumulation trust. For this purpose, a capital gains distribution is deemed to have been made only when the distribution is greater than all of the accumulated ordinary income.

The House bill (section 701) would repeal the capital gain throwback rule on distributions made after December 31, 1974. The Committee added an amendment under which the capital gain throwback rule would not apply to a distribution actually made after the effective date of the repeal of the provision where the IRS terminates a trust which would result in a capital gain distribution deemed to have been made prior to the effective date of the repeal of the provision.

3. Deduction for attending conventions.-- Yesterday the Committee agreed to certain provisions relating to the deduction of certain expenses incurred in connection with attending foreign conventions. Today the Committee agreed that no deductions would be allowed for expenses incurred in connection with conventions on cruise ships.

4. Qualified stock options. -- Under the House bill, in the future, qualified stock options issued in the future would be subject to the same rules as presently apply in the case of nonqualified options. Generally, the value of the option would constitute ordinary income to the employee if it has a readily ascertainable fair market value at the time it is granted, but when the option is exercised the spread between the option price and the value of the stock would constitute ordinary income to the employee.

In general, these rules would apply to options granted after September 23, 1975, pursuant to a written plan adopted and approved before September 24, 1975; these rules apply for options granted on or after that date under a qualified plan adopted by a board of directors before that time, even if the plan was approved by the shareholders after that date. These rules also apply for substitute options granted after September 23, 1975, as a result of a corporate reorganization or similar transaction. The transition rules cover these options as long as they are exercised before September 24, 1980.

Committee amendment. -- The Committee approved the House provision, but modified the effective date to apply to options granted after May 20, 1976. An exemption would be provided for new or small firms.

5. Fairs. -- The Committee agreed to an amendment under which income received by certain nonprofit organizations from qualifying public entertainment activities held in conjunction with a public fair, or conducted under State law which allows only certain tax-exempt organizations or governmental units to conduct the specified activity, would not be taxable as unrelated trade or business income, and would not affect the tax-exempt status of such organizations. Such activities could not be carried on for more than 20 days per year.

6. Recycling tax credit. -- The Committee agreed to allow a tax credit (effective January 1, 1977) on purchases by a recycler of recyclable ferrous and nonferrous metals, textile, waste paper and glass; gold, silver, platinum and other precious metals would not be eligible for the credit. On metals, the credit would be one-half the percentage depletion rate on virgin metals; a 10 percent credit on textile and paper waste and 5 percent credit on glass would be provided. In any year, no credit would be allowed on purchases less than the base period amount. The base period quantity would be 75 percent of the average amount of recyclable material consumed in 1973 through 1975. After a four-year phase-in of the tax credit, the three-year base period will advance one year at a time. During the phase-in period, all recyclers will receive 25 percent of the credit in the first year, 50 percent in the second year, 75 percent in the third year, and 100 percent in the fourth and all later years.

The tax credit would be terminated for any natural resource materials if the depletion allowance or capital gains treatment for those materials is repealed. The Secretary of the Treasury, in the case of waste paper and textiles, may increase the tax credit to a minimum of $10.00 per ton in any year in which the Administrator of the Environmental Protection Agency certifies in writing that such allowance is essential to accomplish recycling of lower grade materials. The Committee agreed in principle to the concept of a maximum dollar credit per ton for any recycled material.

7. Legislators' travel expenses away from home. -- Under the House bill, the "tax home" of a State legislator would be his place of residence within the legislative district which he represents.

The allowable deduction by State legislators for living expenses would be limited to an amount determined by the IRS. The IRS would determine a daily amount taking into account the cost-of-living at the place where the State legislature meets and the amounts normally allowed businessmen under similar circumstances. A State legislator would be allowed to deduct up to this daily amount multiplied by the number of days of his legislative participation during the calendar year.

The $3,000 limitation presently allowed to Members of Congress would be modified to provide that deductions by a Member of Congress would be limited, as in the case of State legislators, to an amount determined by the IRS. The IRS would establish an annual amount taking into account the number of days that the Members are away from home, the cost-of-living in Washington, D. C., and the amount normally allowed businessmen in similar circumstances.

These provisions would apply to taxable years after December 31, 1974.

For taxable years beginning before December 31, 1974, a State legislator could elect to have the above rules apply. If an election is made, the legislator would be treated as having expended for living expenses an amount equal to the daily per diem allowed U.S. government employees multiplied by the number of days the State legislature was in session. However, the total amount of deductions allowable could not exceed the amount already claimed on the State legislator's tax return for the year in question.

Committee amendment. -- The Committee agreed to the House provision as it affects State legislators, with these changes:

a. The living expense deduction would be determined by the Bureau of Labor Statistics rather than the Internal Revenue Service.

b. In counting the number of days of legislative participation, there would be included any day in which the legislature was in recess for a period of four or less consecutive days.

The provisions of the House bill relating to Members of Congress would be deleted.

8. Tax simplification study. -- The Committee agreed to direct the Joint Committee on Internal Revenue Taxation staff to conduct a comprehensive study and review of the Internal Revenue Code for the purpose of determining how the tax laws can be simplified and whether tax rates can be reduced by repealing any or all tax deductions, exemptions, and credits.

The Committee also agreed to direct the Secretary of the Treasury to furnish the Treasury Department's findings in connection with a similar study now in progress. This report is to include an analysis of the integration of individual and corporate income taxes as well as the matter of simplification.

9. Revision of tax tables for individuals. -- The Committee agreed to the provision of the House bill (section 501) revising the optional tax tables for individuals so that taxpayers would use a simplified table. The new tables would be based on taxable income instead of adjusted gross income and would apply to taxable incomes up to $20,000 (instead of $15,000 of adjusted gross income). They would be available to taxpayers who itemize and to those who take the standard deduction.

10. Alimony payments. -- The Committee approved the provision of the House bill (section 502) under which alimony payments would be changed from an itemized deduction to an "above the line" deduction from gross income. This change would allow taxpayers who elect the standard deduction to claim an alimony deduction.

11. Retirement income credit. -- The House bill restructures the present retirement income credit and converts it to a 15 percent tax credit for the elderly, available to all taxpayers age 65 or over regardless of whether they have retirement income or earned income.

The maximum amount on which the credit is computed is increased to $2,500 for single persons age 65 or over (or for married couples filing joint returns where only one spouse is age 65 or over) and to $3,750 for married couples filing joint returns where both spouses are age 65 or over.

The reduction for social security benefits and other tax-exempt pension income is retained.

In place of a reduction for earnings over $1,200, the House bill provides an income phaseout based on adjusted gross income (rather than just earned income) above $7,500 for single persons and $10,000 for married couples ($5,000 for a married person filing a separate return) in order to limit the benefits of the credit to low- and middle-income elderly taxpayers. Under this phaseout, the maximum amount on which the credit is computed would be reduced by $1 for each $2 of adjusted gross income (AGI) above the indicated AGI levels.

The requirement that to be eligible for the credit the taxpayer must have met the test of earning $600 a year for 10 years would be eliminated. Further, the variation in treatment of married couples depending on whether they are separately eligible for the credit would be removed.

For individuals under age 65 receiving public retirement pensions, the maximum amount on which the credit may be computed would be increased to $2,500 for single persons and $3,750 for married couples. Also, for individuals under age 65, the 10-year, $600 earnings requirement and the variation in treatment of married couples would be eliminated.

Committee amendment. -- The Committee agreed to the House provision, but would phase in the increase in the maximum amount on which the credit is computed over a 3-year period. In addition, under the Committee amendment the separate treatment for retirement income of public employees under age 65 would be eliminated.

12. Credit for child care expenses. -- In lieu of present law provisions, the House bill provides a nonrefundable tax credit equal to 20 percent of employment-related expenses.

The credit may be taken against an annual maximum of $2,000 for one dependent and $4,000 for two or more dependents.

The credit is made available to married couples where one or both work part-time or where one spouse is a full-time student. Eligible expenses are then limited to the amount of earnings of the spouse earning the smaller amount, or in the case of a single person, to his or her earnings.

Divorced or separated parents having custody of the child but not entitled to a dependency exemption may claim the credit.

A deserted spouse may claim the credit after six months.

The distinction between care for children in the home and care outside the home is eliminated.

The requirement that the eligible expenses be reduced by disability income received by the dependent is eliminated.

A credit for payments to relatives is permitted if

(a) the related individual is not a resident of the same household as the taxpayer,

(b) the related individual is not a dependent of the taxpayer or his spouse, and

(c) the services constitute employment covered by the Social Security Act.

Committee amendment. -- The Committee agreed to the House provision, with this modification: Payments to relatives would be permitted whether or not the related individual is a resident of the same household as the taxpayer.

PRESS RELEASE

FOR IMMEDIATE RELEASE
May 21, 1976

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

FINANCE COMMITTEE ACTS ON TAX REVISION ISSUES (H.R. 10612)

The Honorable Russell B. Long (D., La.), Chairman of the Senate Committee on Finance, announced today that the Committee continued its work on the House-passed tax revision bill (H.R. 10612) and made the following tentative decisions:

Sick Pay and Certain Military Disability Pensions

Present law. -- Under present law gross income does not include amounts received under wage continuation plans when an employee is "absent from work" on account of personal injuries or sickness. Payments received by an employee absent from work are generally referred to as "sick pay". A series of percentage limitations on amounts received and a minimum requirement for days of absence from work are applied to determine the sick pay exclusion currently.

House bill. -- The House bill would repeal the present sick pay exclusion and provide a maximum annual exclusion of $100 a week for taxpayers under age 65 who have retired on disability income and are permanently and totally disabled. Permanently and totally disabled for this purpose means unable to engage in any substantial gainful activity by reason of any medically determinable physical or mental impairment which can be expected to result in death or which has lasted, or can be expected to last, for a continuous period of not less than 12 months. The maximum excludible amount would be reduced on a dollar-for-dollar basis by adjusted gross income (including disability income) in excess of $15,000, thus phasing out the exclusion entirely at $20,200 adjusted gross income.

The House provision would apply both to civilians and to military personnel, but all Veterans Administration payments would remain completely exempt from tax. The provision generally would apply to taxable years beginning after December 31, 1975. A transitional rule would allow persons (other than those in the military and certain government services) who retired on disability or were entitled to retire on disability before January 1, 1976, and were, as of that date, permanently and totally disabled, to claim a sick pay exclusion if they otherwise qualify.

In the case of the military and certain government services, the House bill would eliminate the exclusion of certain disability payments prospectively in the case of persons who joined these services after September 24, 1975. All Veterans Administration disability payments would continue to be tax-free. Also, an exclusion would continue to be provided for future members of the armed services if payments to them are directly related to "combat injuries." Even if a future serviceman who retires does not receive his disability benefits from the Veterans Administration, he could still exclude an amount equal to the benefits he could otherwise receive from the Veterans Administration.

Committee amendment. -- The Committee approved the House provision, but agreed to an amendment allowing the exclusion on a per taxpayer basis, as under present law, rather than per return basis. Therefore, the maximum exclusion per year for married couples where both spouses are disabled would be $10,400 rather than $5200 maximum exclusion in the House bill.

Moving Expenses

Present law. -- Present law provides a deduction from gross income for the expenses of moving to a new residence in connection with beginning work at a new location. Reimbursements of moving expenses must be included in gross income but may be offset by deducting qualified expenses.

Deductible expenses include the costs of transporting members of the household as well as household goods and personal belongings from the former to the new residence; meals and lodging enroute; premove house-hunting trips; temporary living expenses for up to 30 days at the new job location; and certain expenses related to the sale or settlement of a lease on the former residence, and the purchase of a new residence at the new job location.

A maximum of $1,000 may be claimed for premove house-hunting and temporary living expenses at the new job location. A maximum of $2,500 (reduced by any deduction for house-hunting or temporary living expenses) may be claimed for certain qualified expenses for the sale and purchase of a residence or settlement of a lease.

The new place of work must be at least 50 miles farther from the former residence than was his former place of work (or his former residence, if no former place of work).

A self-employed person must, during the 24-month period following arrival at new job location, perform services on a full-time basis for at least 78 weeks, with at least 39 weeks of full-time work falling within the first 12 months. An employee must work full-time for at least 39 weeks during the 12-month period following his move.

House bill. -- The House bill would increase the maximum premove house-hunting and temporary living expense deduction to $1,500 and the maximum deduction for qualified expenses for the sale, purchase, or lease of a residence (reduced by deductible premove house-hunting or temporary living expenses) to $3,000. It would also reduce the 50 mile limit to 35 miles.

Several exemptions would be provided for the Department of Defense, the Department of Transportation, and members of the armed forces of the United States on active duty:

(a) the departments and servicemen would not be required to report as income to the servicemen, nor to withhold tax on, any in-kind moving expenses provided by the military for moves pursuant to a military order and incident to a permanent change of station for which a change of residence is required;

(b) servicemen would be allowed to deduct qualified moving expenses, subject to generally applicable dollar limitations, to the extent such expenses exceed in-kind reimbursements without reducing the dollar limitations by the amount of in-kind reimbursements provided by the military; and

(c) servicemen would be exempt from both the 35-mile and the 39-week rules.

Committee amendment. -- The Committee approved the House provision with an amendment to permit the deduction of moving expenses incurred when the family of a serviceman moves to a destination within the United States when the serviceman is assigned overseas.

Accumulation Trusts

House bill. -- Under the House bill, a single method of computing the throwback tax would be substituted for the two alternative methods available under present law. This new method would basically be a revision of the present "short-cut method." This revised method would throw the average accumulation distributions (as determined under present law) back to the 5 preceding years of the beneficiary (rather than the 3 preceding years under present law). However, with respect to the 5 preceding years, the year with the highest expanded taxable income and the year with the lowest expanded income would not be considered. The average amount for the 3 years would be added to the beneficiary's taxable income for these years (rather than requiring the recomputation of his entire taxable income as under present law). In other respects, the present rules under the short-cut method would continue to be applicable, except that no refunds would be available.

Income accumulated by a trust prior to the beneficiary's attaining the age of 21 and the years a beneficiary was not in existence would not be subject to the throwback rule. A special rule would be provided for three or more trusts which accumulate income in the same year for a beneficiary.

The capital gains throwback would be repealed. In its place, however, the bill provides that property transferred to the trust would have a 2-year holding period in order to qualify for long-term capital gain treatment with respect to the unrealized appreciation in the property at the time it is placed in trust. This special rule would not apply to property transferred to a charitable remainder trust or a pooled income fund.

Committee amendment. -- The Committee approved the House provision with an amendment to substitute for the 2-year holding period provided in the House bill for transfers of appreciated property in trust, a provision to tax gains on the sales of property occurring within 2 years of the transfer to the trust by the grantor (to the extent of the unrealized appreciation of the property at the time of the trust) as if the grantor had sold the property.

State and Local Gasoline Tax Deduction

Under present law, an itemized deduction is allowed for State and local gasoline taxes. The Committee agreed to an amendment under which State and local gasoline taxes would be deductible only to the extent they exceed $50.

Investment Tax Credit

Under present law, the investment tax credit is 10 percent through December 31, 1976. A corporate taxpayer may elect an 11 percent investment tax credit if an amount equal to the additional one percent is contributed to an Employee Stock Ownership Plan. After December 31, 1976, the rate of the investment tax credit reverts to 7 percent (4 percent in the case of certain public utility property) and the 11 percent investment tax credit for electing corporate taxpayers terminates.

The Committee agreed to continue the investment tax credit without an expiration date at a 10 percent rate. An 11 percent investment tax credit would also be continued where an amount equal to the additional one percent is contributed to an Employee Stock Ownership Plan. The Committee also agreed that investment tax credits previously claimed which would otherwise have expired in 1976 would be eligible to be carried forward for two additional years so that no investment tax credits carried forward will expire prior to December 31, 1977.

The Committee also approved an amendment to make clear that ships constructed with Capital Construction Funds, as provided in the Merchant Marine Act of 1970, qualify for the investment tax credit.

Employee Stock Ownership Plans

Under present law, an employee's benefits under a tax-qualified employee stock ownership plan (ESOP) are not taxed until they are distributed to the employees under the plan. If a plan meets certain qualification requirements, the employer is allowed a deduction (within limitations) for its contributions; the income earned on assets held under the plan is not taxed until it is distributed; special 10-year income averaging and tax-free rollover rules apply to distributions made in a lump sum; and estate and gift tax exclusions are provided.

Under present law, an employer is entitled to an additional percentage point of investment tax credit (11 percent rather than 10 percent) if it contributes an amount equal to the additional percentage point to an employee trust which satisfies certain requirements (provided in the Tax Reduction Act of 1975) as to vesting, employee participation, allocation of employer contributions, benefit and contribution limits, and voting of stock held by a trust under the plan. ESOPs are exempted from the rules of the 1974 pension act requiring diversification of investments.

Committee amendment. -- The Committee approved the following proposals related to the investment credit ESOP as amendments to H.R. 10612:

1. Flowthrough to utility rate payers of the additional one percent investment tax credit would be prohibited.

2. Employee participation would be broadened in investment credit ESOPs by providing that, generally, all employees who are at least age 25 and have completed 3 years of service must be participants. Union members who elect not to participate and certain nonresident aliens could be excluded.

3. Deductions by employers of contributions of erroneously claimed additional investment tax credits (where this is lost upon audit) or, as an alternative, allowance of the erroneous contributions as offsets against future additional investment tax credit contributions would be permitted.

4. If there is a premature disposition of property with respect to which the additional credit was allowed, the additional credit would not be recaptured if it was contributed to an ESOP (as an alternative, the additional credit would be recaptured and the amount recaptured would be applied to offset future ESOP contributions of additional credit).

5. An ESOP which receives the additional credit would be allowed to bear a portion of the administrative expense.

6. Under the one percent investment tax credit ESOP, the Committee agreed:

(a) To provide that the stock of a corporation which is a member of a controlled group of corporations can be contributed to an investment credit ESOP for employees of other members of the controlled group.

(b) To provide that employer stock held by an ESOP would not be taken into account in determining whether a group of corporations could file a consolidated return.

(c) To permit a union's employees to be included in the ESOP of the union member's employer. This inclusion, if agreed to by the parties, would be on a proportional basis. For example, if one-tenth of the union's members are in an employer's plan, then an ESOP contribution could be allocated on the basis of one-tenth of the union employees' salaries.

(d) To provide in the case of an ESOP under which no more than one-third of employer contributions are allocated to employees who are officers, shareholders (holding more than 10% of the employee's stock outside of the ESOP), or highly compensated, that the limit on the annual addition to an employee's account (presently $26,285 plus cost-of-living increases) would be doubled.

The Committee also approved a number of other provisions relating to Employee Stock Ownership Plans:

(a) A one percent contribution to an ESOP could be made at any time the taxpayer was able to realize the tax benefit of the one percent investment tax credit, i.e., the time when the taxpayer had sufficient tax liability to apply the one percent credit.

(b) The requirement that an employee plan be permanent would be clarified so that the requirement would be satisfied by a commitment to make the one percent contribution only so long as the tax law allowed the additional one percent investment tax credit.

(c) A rule would be provided for the voting of ESOP stock after the contribution was made and before allocation of the contribution to the employee participants.

(d) "Total compensation" would be defined in the same way as under the Employee Retirement Income Security Act (ERISA).

(e) The ERISA fiduciary rules would be amended to allow an ESOP plan fiduciary to loan money to an ESOP without this being a "prohibited transaction."

(f) The one percent ESOP could be administered in tandem with an employee thrift plan, provided that the one percent ESOP rules would apply to the portion representing the one percent ESOP contribution.

(g) The ERISA "exclusive benefit" rule would be amended to the extent necessary to make the rule consistent with the basic purpose of ESOP plans.

PRESS RELEASE

FOR IMMEDIATE RELEASE
May 25, 1976

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

FINANCE COMMITTEE ACTS ON TAX REVISION ISSUES (H.R. 10612)

The Honorable Russell B. Long (D., La.), Chairman of the Senate Committee on Finance, announced today that the Committee continued its work on the House-passed tax revision bill (H.R. 10612) and made the following tentative decisions:

Denial of certain foreign tax benefits in the case of foreign bribes. -- The Committee approved an amendment incorporating the substance of S. 3150, which would require U. S. companies and their foreign subsidiaries to report to the Secretary of the Treasury payments made by it or its subsidiaries to officials of foreign governments. If the Secretary of the Treasury determines these amounts constitute bribes, the Committee amendment would deny the foreign tax credit, deferral of taxation of the income of the foreign subsidiary, and DISC tax benefits in the case of transactions which involve a foreign bribe.

Employee Stock Ownership Plans and Electric Utilities

Present Law

Under present law, an employee's benefits under a tax-qualified employee stock ownership plan (ESOP) are not taxed until they are distributed to the employees under the plan.

If a plan meets certain qualification requirements, the employer is allowed a deduction (within limitations) for its contributions; the income earned on assets held under the plan is not taxed until it is distributed; special 10-year income averaging and tax-free rollover rules apply to distributions made in a lump sum; and estate and gift tax exclusions are provided.

Under present tax law, an employer is entitled to an additional percentage point of investment tax credit (11 percent rather than 10 percent) if it contributes the additional credit to an employee trust which satisfies certain requirements (provided in the Tax Reduction Act of 1975) as to vesting, employee participation, allocation of employer contributions, benefit and contribution limits, and voting of stock held by a trust under the plan.

ESOP's are exempted from the rules of the 1974 Pension Act requiring diversification of investments.

On May 21, the Committee agreed to extend the application of the present 11 percent investment credit where ESOP plans have been provided.

Today the Committee also agreed to provide another one percentage point of investment tax credit to any electric utility or local gas distribution utility which adopts an ESOP to which the employer and employees respectively each agree to contribute an additional amount equal to one percentage point of the investment tax credit. Under this proposal:

(a) The additional 2 percentage points of credit would not be subject to the 50-percent-of-income-tax limit of the investment credit; however, the total 12 percent credit could not exceed 100 percent of income tax. The employer would put the 2 percentage points of extra investment credit into the ESOP in the first and second years after the credit is allowed. The contributions representing the larger investment credits that are provided to the employer would not be deductible for tax purposes.

(b) The employer would also contribute out of its own funds an amount equal to one percentage point of the investment credit to the ESOP. This amount, out of the employer's own funds, would be tax deductible. This employer contribution of one percentage point would be matched by the employees of the utility.

(c) The ESOP would have to receive common stock of the employer with voting and dividend rights at least as favorable as the employer's other common stock. If a loan to the ESOP is involved, the ESOP could initially receive convertible debentures, but those securities must be converted to common stock no later than the time the purchase-money loan is paid off. If the ESOP did not incur a purchase-money loan, it would initially receive the common stock at the time of each of the four annual contributions. Officers of the utility could not act as trustees of the ESOP.

(d) The ESOP would have to cover all employees except that (1) it could exclude any employee who has not attained the age of 25, and exclude any employee who has not completed three years of service; (2) it could exclude any nonresident alien with no U. S. source income from the employer; and (3) any employee who is under a collective bargaining agreement could be excluded if that employee individually rejects the plan. Employees of a union which covers any plan participants would be covered on a basis which depends on the proportion of that union's members that have elected to come under the ESOP. Integration with social security would not be allowed. The ESOP would be required to provide full and immediate vesting.

(e) No more than 15 percent of any employer contribution to the ESOP could be allocated to the group of employees consisting of each employee who owns more than 5 percent of the employer's stock (without regard to the stock in the ESOP).

(f) The limits (sec. 415) imposed by ERISA on contributions and benefits under employee plans would apply.

(g) Employees would be taxed on stock distributed to them by ESOP's under the same rule as present law regarding employer securities (i.e., no tax on appreciation in value of stock attributable to employee contributions until the distributed stock is sold or otherwise disposed of in a taxable transaction).

(h) For any year for which an employer provides an investment credit ESOP under the above rules, that employer would also be eligible for the full investment credit progress payments rule of section 46 (d) (rather than phase-in under sec. 46 (d) (7)). Under present law (sec. 46 (d)), a taxpayer may make an irrevocable election that the investment tax credit apply to progress payments for certain qualified property. The property must have a normal construction period of two or more years and be expected to have a useful life of 7 or more years.

The Committee also agreed that there would be an immediate investment credit on progress payments by utilities for construction of property taking 2 years or more to build.

In addition, the Committee agreed to extend the period for adopting a one percent investment credit ESOP by three months.

Net Operating Losses

Under current law, a taxpayer is generally allowed to carry a net operating loss back as a deduction against income for the three years preceding the year in which the loss occurred and to carry any remaining unused losses over to the five years following the loss year. This enables taxpayers to average income and losses over a moving nine-year period.

The Committee agreed to provide an option for business taxpayers (including insurance companies) to elect an eight-year carry over period and no carryback in lieu of the carryback and carryover periods allowed under present law. Additional statutory rules would be provided to restrict "trafficking" in loss corporations through which unprofitable businesses are acquired to obtain the tax benefits of these businesses' net operating loss carryovers.

Deduction of Capital Losses Against Ordinary Income

Present law. -- For individuals, capital losses may be deducted against capital gains. In addition, capital losses in excess of capital gains may be deducted against up to $1,000 of ordinary income each year. When they are deducted against ordinary income, long-term capital losses must be reduced by 50 percent. Capital losses that cannot be deducted against capital gains or ordinary income in a particular year may be carried forward into future years.

For corporations, capital losses may not be deducted against ordinary income. However, capital losses in excess of capital gains are carried back and deducted against capital gains in three prior years. Any remaining capital losses may be carried forward and deducted against capital gains, but the carryforward is limited to five years.

House bill. -- The House bill increases the amount of ordinary income against which individuals may deduct capital losses from $1,000 to $2,000 in 1976, $3,000 in 1977 and $4,000 in 1978.

Committee amendment. -- The Committee agreed to delete the House provision.

Increase in Holding Period for Long-Term Capital Gains

Present law. -- Gains on capital assets held longer than six months are considered long-term capital gains.

For individuals, 50 percent of long-term capital gains are excluded from adjusted gross income. Individuals may elect to have the first $50,000 of long-term capital gains taxed at an alternative rate of 25 percent. Also, when long-term capital losses are deducted against ordinary income, they must be reduced by 50 percent.

Corporations may elect to have their long-term capital gains taxed at an alternative rate of 30 percent (compared to the 48-percent corporate tax rate on taxable income above $50,000).

House bill. -- The House bill increases the holding period defining long-term capital gains from six months to eight months in 1976, ten months in 1977 and one year in 1978 and future.

Gains on agricultural commodity futures contracts are exempt from the increase in the holding period.

Committee amendment. -- The Committee agreed to delete the House provision.

Capital Loss Carryover for Regulated Investment Companies

Present law. -- Unlike corporations, which are generally allowed a three-year capital loss carryback and a five-year carryforward, regulated investment companies (mutual funds) are not allowed any carryback (but are allowed the normal five-year carryforward).

House bill. -- The House bill extends the carryover period for regulated investment companies from five years to eight years.

This provision is to apply to loss years ending on or after January 1, 1970.

The Committee agreed to adopt the House provision.

State taxes on production and consumption of electricity. -- The Committee approved a provision amending Public Law 86-272, to prohibit any State from imposing, directly or indirectly, a discriminatory tax on electrical energy consumed outside the State at a rate higher than that imposed upon electrical energy consumed within the State.

Energy provisions

Home insulation tax credit. -- The Committee approved a tax credit for expenses incurred in insulating a residence. The credit would be equal to 30 percent of the first $750 of insulation expenditures (a maximum credit of $225), and the tax credit would be refundable (that is, a taxpayer whose tax liability is less than the amount of the credit would receive a refund of the difference). Qualified insulation would include regular insulation, storm or thermal windows and doors, or similar items such as weatherstripping and caulking designed specifically and primarily to reduce heat gain or loss of a building. The material installed would have to be first used by the taxpayer claiming the credit, have a useful life of at least three years, and meet those performance standards that may be prescribed in Treasury regulations.

Bus and bus parts. -- Under present law, there is a 10 percent manufacturers' excise tax on buses, and an 8 percent excise tax on bus parts. The Committee agreed to repeal the excise tax for buses and bus parts.

Insulation of business facilities. -- The Committee agreed to a 10 percent investment tax credit for insulation expenditures on existing (but not new) business or commercial structures. Qualified insulation would include regular insulation, storm or thermal windows and doors, and similar items such as weatherstripping or caulking designed specifically and primarily to reduce the heat gain or loss of a building. The material installed would have to be first used by the taxpayer claiming the credit, have a useful life of at least three years, and meet those performance standards that may be prescribed in Treasury regulations.

Rerefined lubricating oil. -- The Committee agreed to a provision which would exempt from the 6¢ per gallon Federal excise tax on oil new oil mixed with waste or rerefined oil under certain circumstances. If the resulting mixture contained up to 55 percent new oil, then all of the new oil in the mixture would be tax exempt. If the mixture contained more than 55 percent new oil, the rerefiner would still be exempt from the tax on so much of the new oil as does not exceed 55 percent of the mixture. However, the tax exemption for new oil would be available only if 25 percent or more of the mixture consisted of waste or rerefined oil.

Solar and geothermal energy equipment in homes. -- The Committee agreed to provide a refundable tax credit for expenses of installing solar or geothermal energy equipment in a residence. The credit would be 40 percent of the first $1,000, plus 25 percent of the next $6,400 of expenditures (a maximum credit of $2,000); these amounts would not be reduced for expenditures on other residences. The credit would be available only to taxpayers in cases where the assessed value of the house for property tax purposes does not include the value of this equipment.

The solar energy equipment for which the credit is available would have to be of a kind which has a useful life of at least three years, which uses solar energy to heat or cool the building or to provide hot water for use within the residence, and the original use of which is made by the taxpayer claiming the credit. The equipment must meet criteria prescribed by the Secretary of Housing and Urban Development under the Solar Heating and Cooling Demonstration Act of 1974.

Heat Pumps. -- The Committee agreed to allow a refundable tax credit for expenditures for installing heat pumps in existing (but not new) residences. The credit would be 20% of the first $1,000 plus 12½ percent of the next $6,400 of expenditures (for a maximum credit of $1,000); these amounts would not be reduced for a taxpayer's expenditures on other existing residences.

Geothermal energy development. -- The Committee agreed to the substance of S. 2608, permitting the current expensing of intangible drilling costs and allowing a 22 percent business deduction against geothermal property income.

Energy use property -- The Committee agreed to the following investment tax credit provisions:

(a) Use of waste as a fuel or for recycling. -- a 12 percent investment tax credit would be extended for a period of 5 years to machinery or equipment necessary to permit waste (or a combination of waste and other fuels) to be used as a fuel. This use as a fuel would include both waste burning and the manufacture of synthetic fuels from solid waste. The benefit would be available only for so much of the property as is necessary to facilitate the use of waste as a fuel or the addition of waste to fuels. The investment tax credit would also be extended to equipment used to recycle solid waste or to prepare solid waste material for recycling.

(b) Oil shale, coal pipelines, gasification, and liquefaction. -- A 12 percent investment tax credit would be extended for a period of 10 years to oil shale equipment and coal slurry pipelines. In the case of shale oil, machinery or equipment necessary to reach or extract oil shale, or to convert oil shale into oil or gas would qualify. In the case of coal slurry pipelines, other coal-transporting pipelines would qualify. This investment tax credit would also be extended to coal liquefaction and coal gasification equipment and equipment to remove pollutants from coal by in-factory processes.

(c) Deep-mining coal equipment. -- A 12 percent investment tax credit would be extended for a period of 5 years to machinery, equipment, and structural components of underground coal mines.

(d) Conversion of organic material. -- A 12 percent investment tax credit would be extended for a period of 5 years to equipment used in the conversion of organic material into methanol or any other synthetic fuel which can be substituted for or blended with conventional fuels. This tax credit would cover equipment which uses organic material which is not "waste" under item (a) above, but which has been grown for conversion to a fuel.

(e) Geothermal energy. -- A 12 percent investment tax credit would be extended for a period of 5 years to equipment installed in business, commercial, and residential structures which permits the use of geothermal heat energy. The tax credit would cover such equipment as heat exchangers and ducting, and would not be restricted to any particular type of fluid or gas extracted from a geothermal resource.

In the case of each of the above credits, an additional 1 percent investment tax credit would be available for taxpayers who establish or maintain an employee stock ownership plan to which the employer contributes stock equal to 1 percent of the value of the qualified investment. For public authorities or agencies which do not have Federal tax liability but which make payments in lieu of taxes, such payments could be reduced by equivalent amounts available to taxpayers for investment in the above qualified energy use equipment.

Air conditioners and space heaters. -- The Committee agreed to a provision denying the investment tax credit to portable-type and self-contained heating and air-conditioning units in the same manner as it is denied under present law to units which are attached to and become part of a building or structure.

Solar and geothermal energy equipment in business and commercial structures. -- The Committee agreed to extend the investment tax credit to solar and geothermal equipment installed in new and existing business or commercial structures. The rate would be 20 percent for both solar energy and geothermal energy equipment installed before January 1, 1981, and 10 percent for such equipment installed between January 1, 1981 and December 31, 1985. In the case of geothermal energy, the tax credit would cover such equipment as heat exchangers and ducting installed by the business or commercial user, and would not be restricted to any particular type of fluid or gas extracted from a geothermal resource.

Excise tax on special motor fuels. -- The Committee agreed to exempt the non-highway use of special motor fuels from the 4 cents per gallon excise tax on special motor fuels. This exemption would include, for example, the use of propane by industrial lift-trucks.

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

FOR IMMEDIATE RELEASE
May 26, 1976

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

FINANCE COMMITTEE ACTS ON TAX REVISION ISSUES (H. R. 10612)

The Honorable Russell B. Long (D., La.), Chairman of the Senate Committee on Finance, announced today that the Committee continued its work on the House-passed tax revision bill (H.R. 10612) and made the following tentative decisions:

Income Tax Return Preparers and Use of Social Security Numbers

Present law. -- Individuals who prepare the tax returns of others for a fee are required by IRS regulations to sign the returns they prepare, but no penalty is provided for failure to sign.

Also, tax return preparers are subject to criminal fraud penalties (up to 5 years and $50,000) for willfully aiding or assisting in the preparation of a fraudulent return.

Tax return preparers are subject to criminal penalties for unlawfully disclosing or otherwise using information disclosed to them in connection with the preparation of a return.

House bill. -- Under the House bill, a series of provisions dealing with income tax return preparers would apply in general to returns and related documents prepared after December 31, 1975. These provisions are as follows:

Each prepared return, statement, or other document must contain the identification number of the return preparer or of the preparer's employer and other data sufficient to identify the preparer. A $25 penalty is provided for each failure to comply, if without reasonable cause.

Each preparer must furnish to the taxpayer a completed copy of the taxpayer's return or claim for refund prepared by the tax return preparer at the time the return or claim is given to the taxpayer for his signature. A $25 penalty is provided for failure to comply, if without reasonable cause.

Each person employing a person to prepare the returns of others must file an annual report with the Service listing the name, identification number, and place of work of each such employed preparer. Self-employed preparers also have to file these returns. Failure to comply without reasonable cause would result in a $100 penalty for each failure to file an annual return and a $5 penalty for each failure to include a name, identification number, or place of work in the annual report. These penalties are not to exceed $20,000 for a 12-month period.

Each return preparer or employer of return preparers must retain for three years either a list of taxpayers for whom returns were prepared or copies of their returns and claims for refunds. A $50 penalty is provided for each failure to retain a copy of a return or to list a taxpayer for whom a return was prepared, up to a maximum of $25,000 for all returns in a year.

A $100 penalty is provided for negligent or intentional disregard of Internal Revenue Service rules or regulations by a tax return preparer. A $500 penalty is provided for a willful attempt to evade, defeat, or understate any tax by a tax return preparer. A separate penalty may be imposed for each return or claim for refund.

A $500 civil penalty is provided for any endorsement or other negotiation by a person who is an income tax return preparer of any check received from the Service by another taxpayer.

The Service would be given the authority to seek a court injunction against income tax return preparers (1) engaging in conduct subject to penalties, (2) misrepresenting their qualifications (including eligibility to practice before the Internal Revenue Service), (3) guaranteeing the payment of a tax refund, or (4) engaging in other conduct similar in nature to the above types of conduct which substantially interferes with the proper administration of internal revenue laws. A tax return preparer who files a bond of $50,000 to guarantee payment of further penalties would not be subject to an injunctive proceeding for penalty-type conduct.

The Internal Revenue Service would be authorized to provide the names, addresses, and taxpayer identifying numbers of preparers to State authorities charged with enforcing State provisions regulating tax return preparers.

The Internal Revenue Service would be specifically authorized by statute to use the social security number of an individual taxpayer or tax return preparer as that person's identification number for income tax purposes.

Committee amendment. -- The Committee adopted the House provisions with these modifications:

1. An individual would not be considered an income tax return preparer merely because he prepared claims for refund which are filed after an IRS audit as the first step in litigating a dispute with the IRS.

2. The IRS could modify the annual report requirement where it concludes that the needed information is available from other sources (for example, where they are on file with a tax return preparer organization in a manner such that there is ready access by the IRS).

3. The injunctive provision would be modified so that the types of conduct for which an injunction could be sought other than the three specific types listed in the bill would be limited to "deceptive and fraudulent" conduct which substantially interferes with the administration of the internal revenue laws. In addition, an injunction prohibiting a preparer from any further preparation of returns would be obtained only where the conduct has been "continuing or repeated" and where the court concludes that other forms of relief (including an injunction against the specific type of conduct involved) would be insufficient.

4. The States and localities would be specifically authorized to use the individual's social security number for administrative purposes, and could require individuals to furnish the number for administrative purposes.

5. Under present law it is illegal for an individual to obtain a social security number fraudulently or to use a social security number fraudulently for the purpose of obtaining benefits under the Social Security Act. The Committee agreed to broaden the crime to include cases where the fraudulent use relates to paying taxes or other fraudulent representations.

Declaratory Judgments--Charitable, Etc., Organizations

Present law. -- In general, an organization cannot have a judicial determination of its status as an exempt organization or charitable donee under the Internal Revenue Code, except in the context of a suit to redetermine a tax deficiency (Tax Court) or for refund of taxes paid (Court of Claims or district court).

The Internal Revenue Service publishes a list of organizations with currently effective favorable charitable donee rulings ("blue book"). The Service cannot be enjoined by the courts to grant a favorable ruling or restrained from removing an organization's name from the blue book (at least in the absence of a favorable court decision in a tax deficiency or refund suit).

House bill. -- The House bill permits a declaratory judgment suit to be brought in the Tax Court or a district court by the organization in order to determine its status (a) as an exempt charity (sec. 501 (c) (3)), (b) as a private foundation (sec. 509 (a)), (c) as a private operating foundation (sec. 4942 (j) (3)), or (d) as a charitable donee (sec. 170 (c) (2)).

Limited protection is provided for donors during the period of dispute in the event the court fails to uphold the organization's claim as a charitable donee. (Of course, if the organization is successful, then the deductions would be allowed under present law.) For this purpose, the period of dispute is the time beginning with the Internal Revenue Service's announcement and ending with the first court decision against the organization. Contributions aggregating up to $1,000 by an individual (or husband and wife together) are protected during this period. Also, other charitable donee organizations may treat the organization in question as being a charitable donee. However, no protection is given to any individual who was responsible for the organization's actions or inactions causing the loss of its charitable donee status.

The declaratory judgment provisions are to apply to pleadings filed more than one year after the bill's enactment, but only with respect to determinations (or requests for determinations) made after the bill's enactment.

Committee amendment. -- The Committee adopted the House provisions with these modifications:

1. The Committee amendment would limit the number of courts that would have jurisdiction of such cases to the United States Tax Court and the United States District Court for the District of Columbia.

2. The bill would apply to pleadings filed six months after the bill's enactment.

3. Suits could be brought with respect to determinations (or requests for determinations) made after January 1, 1976.

Assessments for Mathematical or Clerical Errors

Present law. -- In general the Internal Revenue Service must send the taxpayer a notice of deficiency and provide the taxpayer an opportunity to petition the Tax Court before the Service can assess a deficiency of income, estate, or gift tax, or of a tax imposed under the private foundations provisions (chapter 42) or under the provisions relating to qualified pension, etc., plans (chapter 43).

The Service is, however, permitted to summarily assess any additional tax resulting from correction of a "mathematical error appearing in the return". In such a case, the taxpayer is not entitled to a notice of judicial review before being required to pay the tax.

House bill. -- Summary assessments would be allowed in the following five types of situations:

(a) errors in addition, subtraction, etc., shown on the return;

(b) incorrect use of a Service table if the error is apparent from the return;

(c) inconsistent entries on a return;

(d) omission of information required to be supplied on the return in order to substantiate an item on that return; and

(e) an entry of a deduction or credit in excess of the statutory limit)(e.g., taking a standard deduction greater than the permitted maximum standard deduction).

If the Service determines that there has been such an error, it would notify the taxpayer, who would have 90 days to respond to the Service determination. If the taxpayer requests an abatement of the assessment, the Service would have 60 days to decide whether its original determination was correct. If the Service notifies the taxpayer within the 60 days that it intends to pursue the matter, the taxpayer would have 30 days to confirm the request for abatement which then must be granted. If the taxpayer confirms the request for abatement, the Service may then use the regular notice of deficiency procedure.

The Service would be required by statute to explain to the taxpayer just what adjustments it is making to the taxpayer's return when the Service determines that the taxpayer has an additional tax liability.

During the period when the assessment could be abated, the Service is not to proceed to collect on this summary assessment.

Committee amendments. -- The Committee agreed to this provision of the House bill, but it would apply with respect to returns filed after December 31, 1976 (rather than December 31, 1975) in order to give the Internal Revenue Service an opportunity to put in place the new procedures required by this provision.

The Committee also agreed to provide that the tax due as a result of a mathematical error is immediately assessable and collectible upon the issuance of a notice to the taxpayer but the taxpayer may, by sending a notice to the Internal Revenue Service, abate the assessment.

Withholding of State Taxes -- Armed Forces

Present law. -- Under present law, the Secretary of the Treasury is required to enter into agreements with States which request it to withhold State income tax from Federal employees. These agreements may not apply to members of the Armed Forces.

House bill. -- The House bill would amend present law to eliminate the prohibition against the Secretary of the Treasury entering into agreements with States and the District of Columbia to withhold State (and county "piggyback") income taxes from members of the Armed Services and would provide for such withholding in cases where the members request it.

This provision requires the Secretary to enter into a withholding agreement 120 days after the request from the proper State official and such a request cannot be made until after the date of enactment of this provision.

Committee amendment. -- The Committee agreed to make the withholding mandatory rather than voluntary for those individuals who are legally subject to a State income tax of their State of residence.

Withholding of State and City Taxes -- National Guard and Ready Reserves

Present law. -- Under present law, the Secretary of the Treasury is required to enter into agreements with States and cities to withhold State and city income taxes from the compensation of Federal employees. The agreement, however, may not apply to pay for service as a member of the Armed Forces.

House bill. -- The House bill would extend the provision under present law requiring the Secretary of the Treasury to enter into agreements with States, the District of Columbia, and cities to withhold income taxes from Federal employees to members of the National Guard and Ready Reserve when they are paid for performing regular training.

The bill requires the Secretary to enter into a withholding agreement 120 days after the request from the proper State official and such a request cannot be made until after the date of enactment of this provision.

Committee amendment. -- The Committee agreed to the House provision with these changes:

1. The Committee agreed to permit State income tax to be withheld from Federal employees where the withholding is voluntary.

2. The Committee agreed to change the definition of city so that the provision for Federal withholding of city income tax from Federal employees may also apply to boroughs and townships as long as there are at least 500 Federal employees in the jurisdiction.

Withholding of Federal Tax -- Gambling Winnings

Present law. -- Under present law, withholding of U. S. income tax on racetrack winnings is not required although payouts to winners of the daily double, Exacta, Perfecta, and similar type pools are reportable on Form 1099 information returns if the payout is based on betting odds of 300 to one or higher. In addition, Nevada gambling casinos are required to report certain large winnings from Keno and bingo games on From 1099 to the Internal Revenue Service depending on the price of the ticket purchased, as well as on the amount won.

House bill. -- Under the House bill, the present information reporting requirement on certain gambling winnings would be replaced with a 20 percent withholding requirement on such winnings. The persons making the payment of winnings subject to withholding would be required to deduct and withhold from the payment 20 percent of the payment. The withholding would be based on the entire payment rather than the amount of the winnings. The winnings subject to withholding would be proceeds of more than $1,000 from wagers in sweepstakes, wagering pools, or lotteries (whether or not conducted by a State or agency or instrumentality of a State). In the case of winnings other than those mentioned above, withholding would be required on payments of more than $1,000 from the wagering transaction if the amount of the proceeds was at least 300 times as large as the amount wagered. The receiver of the winnings subject to withholding would be required to furnish the payor with the name, address and taxpayer identification number of the person receiving the payment and of each person entitled to any portion of such payment, under penalty of perjury.

The provisions would apply to wagering transactions occurring after December 31, 1975.

Committee amendment. -- The Committee agreed to the House provision, but it would be effective 30 days after enactment of the bill.

State Conducted Lotteries

Present law. -- Under present law, each person engaged in the business of accepting wagers is subject to an excise tax of 2 percent on the amount of wagers placed with that person. The excise tax on wagers generally applies to any person who is conducting a lottery. In addition, a related occupational tax of $500 per year is imposed on each person who is liable for the tax on wagers (or who is engaged in the business of receiving wagers for or on behalf of a person who is in turn liable to pay the excise tax on wagers). Also, a special occupational tax of $250 per year is imposed on the operation of coin-operated gaming devices, including a vending machine which dispenses tickets on lotteries.

An exemption from the wagering tax is provided for (a) State-licensed parimutuel wagering and (b) sweepstakes or lotteries conducted by an agency of a State if the ultimate winners of the sweepstakes or lotteries are determined by the results of a horse race.

Committee amendment.--The Committee agreed to the provision of the House bill under which State-conducted lotteries, effective March 10, 1964, would be exempt from the 2 percent wagering tax. Vending machines which dispense tickets on a sweepstakes or lottery conducted and maintained by State lottery agencies would be exempted from the occupational tax on wagering.

Jeopardy and Termination Assessments

Present law. -- When the Service determines that the collection of a tax may be in jeopardy, it may forgo the normal time-consuming assessment and collection procedures and immediately assess and collect the tax. For this purpose, there are two basic types of special assessments--jeopardy assessments and termination assessments. Jeopardy assessments are of two different types depending on whether the taxes involved are (1) income, estate, gift, or certain excise taxes (those taxes that are normally dealt with under the notice of deficiency procedures) or (2) other taxes (such as employment taxes and wagering taxes).

If the Service determines that there is a deficiency of income, estate, gift, or certain excise taxes and that its assessment or collection would be jeopardized by the delay, the Service is then authorized immediately to (1) assessthe tax, (2) send a notice and demand for payment, and (3) levy upon the taxpayer's property for its collection. The 10-day waiting period normally required between demand for payment and seizure of the taxpayer's property does not apply in this case. However, if the jeopardy assessment is made before the statutory notice of deficiency is sent to the taxpayer, the Service is required to send the notice within 60 days after the jeopardy assessment is made.

The taxpayer may petition the Tax Court to redetermine the deficiency or may sue for a refund in the Court of Claims or a district court.

During or prior to Tax Court litigation, the Service is generally precluded from selling any of the taxpayer's seized property.

Unlike the ordinary taxpayer, the jeopardy taxpayer loses the use of his seized property while relief is sought in the Tax Court.

If the Service determines that there is a deficiency in a tax other than an income, estate, gift, or certain excise tax and that the assessment or collection of the tax would be jeopardized by delay, the Service is authorized to immediately assess and levy upon the taxpayer's property. No notice of deficiency is required in this type of jeopardy assessment.

The taxpayer may sue for refund in the Court of Claims or a district court, after filing a claim for refund and waiting until either the claim is denied or 6 months have elapsed. The taxpayer cannot petition the Tax Court.

The Service can sell the taxpayer's property prior to litigation.

A termination assessment may be made when the collection of an income tax is in jeopardy before the end of a taxpayer's normal tax year or before the statutory date the taxpayer is required to file a return and pay the tax. Under a termination assessment, which may be made only to collect income taxes, if the Service finds that the collection of a tax is in jeopardy, it is authorized to:

(a) serve notice on the taxpayer of the termination of the taxable period;

(b) demand immediate payment of any tax determined to be due for the terminated period; and

(c) if payment is not received, immediately levy upon the taxpayer's property.

Any amount collected as a result of the termination assessment is credited against the tax finally determined to be due for the taxpayer's full year liability.

House Bill

Under the House bill, Tax Court review of jeopardy and termination assessments would be provided on an expedited basis.

If a jeopardy or termination assessment is made, the taxpayer would be able to promptly petition the Tax Court for judicial review. Within 20 days after the filing of a petition, the Tax Court would determine whether the Service had reasonable cause for making the assessment and whether the amount of the assessment made was appropriate in view of all of the circumstances. In addition, until completion of judicial review, the Internal Revenue Service would not be permitted to sell property (other than perishables) seized pursuant to jeopardy or termination assessment procedures.

Committee Modifications

1. Under the Committee amendment, the reviewing court would be the appropriate U. S. district court.

2. The Committee provided that within 5 days after the jeopardy or termination assessment, the Service must give the taxpayer a summary of the information on which it relied in determining that the assessment should be made. The taxpayer would then be permitted to seek administrative review in the Service. If the dispute as to the propriety of the assessment has not been resolved within 15 days after the taxpayer has applied to the Service, then the taxpayer may seek court review.

3. Additionally, since the seizure of a taxpayer's assets pursuant to a jeopardy or termination assessment is an extraordinary procedure which may well impose significant hardship on the taxpayer, the Committee agreed to put the burden of proof on the Service with respect to whether there should be a jeopardy or termination assessment. (The taxpayer would normally have the burden as to the amount of the assessment.)

4. The Committee agreed to provide that a termination assessment would be treated as closing a taxpayer's taxable year for all purposes; the short taxable year created thereby would count as one taxable year for purposes of limitations on carryovers, carrybacks, etc. The Committee amendment would provide, nevertheless, that the taxpayer has the option of keeping his normal taxable year and requiring the Service to send him a notice of deficiency by the 60th day after the return is filed for that normal taxable year.

5. The Committee agreed to provide that in the case of termination assessments, the Service cannot sell property (other than perishables) seized until the taxpayer's tax liability has been determined by the District Court (if he contests liability in the District Court).

Exemption from Levy

Present Law

Present law provides that the following items of the taxpayer are exempt from levy for taxes: (a) wearing apparel and school books necessary for the taxpayer or members of his family; (b) if the taxpayer is head of a family, up to $500 worth of the following: the fuel, provisions, furniture, and personal effects in his household, arms for personal use, livestock, and poultry; (c) up to $250 worth of books and tools necessary for the taxpayer's trade, business, or profession; (d) unemployment benefits (including any portion payable with respect to dependents); (e) undelivered mail; (f) annuity or pension payments received by a person whose name has been entered on the Army, Navy, Air Force, and Coast Guard Medal of Honor roll, and annuities based upon retired or retainer pay under the Retired Servicemen;s Family Protection Plan; (g) workmen's compensation payments (including any portion payable with respect to dependents); and (h) so much of the taxpayer's salary, wages, or other income as is necessary to comply with a pre-levy court ordered judgment for support of the taxpayer's minor children.

Under present law, a levy extends only to obligations which exist at the time of levy. Consequently, the Internal Revenue Service can levy on salaries and wages only to the extent they have been earned as of the date of the levy. If the amount of such wages or salary levied upon is inadequate to satisfy the taxpayer's obligations, the Internal Revenue Service may utilize successive levies against additional salaries or wages until those obligations have been satisfied.

House Bill

Under the House bill, a limited amount of a taxpayer's wages, salary, and other income would be exempt from levy under jeopardy and termination assessment procedures and otherwise. The amount that would be exempt for a taxpayer who receives all of his wages, salary, or other income on a weekly basis would be $50 plus $15 for each individual who is specified as a dependent of the taxpayer in a verified written statement submitted to the person on whom notice of levy is served.

The bill also provides that a levy on a taxpayer's salary or wages shall be continuous until the tax liability with respect to which it is made is satisfied or becomes unenforceable because of the lapse of time.

These provisions would apply only with respect to levies made after December 31, 1975.

Committee amendment.--The Committee agreed to the House provision, but with the effective date postponed so that these rules would apply with respect to levies made after December 31, 1976.

Administrative Summons

Present Law

Under present law, the Internal Revenue Service is given authority, during the course of an investigation to determine the tax liability of a person, "to examine any books, papers, records, or other data which may be relevant or material" to the investigation. This includes not only the right to examine records in the possession of the taxpayer but also the authority to issue a summons to "any person" having possession or custody of records "relating to the business of the person liable for tax" as well as the authority to take the testimony of any such person under oath.

In certain cases, where the Service has reason to believe that certain transactions have occurred which may affect the tax liability of some taxpayer, but is unable for some reason to determine the specific taxpayer who may be involved, the Service may serve a so-called "John Doe" summons, which means that books and records relating to certain transactions are requested, although the name of the taxpayer involved is not specified.

The summonses served by the Internal Revenue Service, which may be referred to as administrative summonses, may be enforced where necessary by court procedure. Where the summons is served on a person who is not the taxpayer (i.e., a third-party summons), the party summoned may challenge the summons for legal defects. However, there is no requirement that the person to whom the records pertain must be informed that a third-party summons has been served. In addition, in United States v. Miller, decided on April 21, 1976, the Supreme Court ruled that the taxpayer or other person to whom the records pertain has no protectable Fourth Amendment interest in such records.

House Bill

Under the House bill, the case of a third-party summons (when the identity of the taxpayer is known), the Service would be required to include sufficient information to enable the third-party recordholder to locate the records. The taxpayer (or other person to whom the summoned records pertain) would receive notice of the summons from the Service at the time of its issuance and would have the right to stay compliance by notifying the person summoned (within 14 days after the date on which the summons is served), not to comply with the summons. The Service would then be required to seek enforcement of the summons in a Federal Court and the taxpayer would have standing to challenge such enforcement.

However, notice to the taxpayer would not be required in connection with the collection activities of the Service where the purpose of the summons was solely to ascertain whether or not the taxpayer has assets in that bank.

In the case of a "John Doe" summons (where the identity of the taxpayer is not known), the Service would have to go into court, establish reasonable cause for requesting the summons, and receive court approval before issuing the summons.

These provisions would apply to summons issued after December 31, 1975.

Committee Modifications:

1. The Committee provided that notice would be sufficient if mailed (by certified or registered mail) to the last known address of the noticee, that the criminal statute of limitations (as well as the civil statute) is to be suspended if the summons is protected, and that protests of summonses are to receive expeditious court consideration.

2. To permit flexibility, the House bill would be modified to permit the Service to mail (by certified or registered mail) notice to the taxpayer or other noticee within 3 days after the summons is served on the recordkeeper, in which case the taxpayer's opportunity to protest the summons would date from the time that notice was mailed to him. Also, the House bill would be clarified so that in order to stay compliance with the summons, the noticee would have to serve notice of his objections on the Service as well as the third party recordkeeper.

3. An exception to the notice requirement would be provided in cases where the Service goes into court and establishes that notice to the taxpayer might result in a material interference with the civil or criminal investigation (as by the possible destruction of records, intimidation of witnesses, etc.). Also, there would not be a notice requirement in cases where the Service's inquiry is solely for the purpose of ascertaining whether the summoned party has certain records in his possession.

4. IRS would be authorized to reimburse witnesses for the costs of complying with summonses.

5. The provision would apply to summonses issued after December 31, 1976.

Private Letter Rulings

Present Law

The Internal Revenue Service issues private letter rulings and other written determinations as to the tax treatment of specific transactions. A private letter ruling may be issued to a taxpayer setting forth the tax treatment of a specific proposed transaction, or a technical advice memorandum may be issued by the National Office of the Service to a district office in response to the district office's request for advice (generally with respect to an issue arising out of an audit).

A private letter ruling or technical advice memorandum includes a statement of the facts the Service believes to be relevant in the case. The background file for each of these written determinations contains a copy of the request for the determination, a copy of the determination, correspondence, and other information relating to the determination.

Although the Internal Revenue Service has taken the position that letter rulings are a part of a taxpayer's return and are, therefore, required to be held in confidence, the courts have required the Service to make letter rulings open to public inspection under the Freedom of Information Act (FOIA).

The FOIA generally requires an agency to place certain information (including rules of procedure, substantive rules, and a description of its organization) in a public reading room and requires that other information (including opinions and interpretations) be made available for public inspection and copying upon request of a person. The FOIA does not require an agency to disclose matters that are--

a. trade secrets and commerical or financial information obtained from a person and privileged or confidential;

b. personnel and medical files and similar files, the disclosure of which would constitute a clearly unwarranted invasion of personal privacy;

c. properly classified national defense or foreign policy secrets; or

d. matters that are specifically exempted from disclosure by statute.

The FOIA also provides exemptions for investigatory records compiled for law enforcement purposes, reports on financial institutions, geological and geophysical information, and a limited exemption for interagency and intra-agency correspondence.

Under the FOIA, a person requesting a document which is not in a public reading room may be required to pay search and copying charges. (These charges are limited to reasonable charges and may be waived or reduced if disclosure of a document is found to be in the public interest.)

The United States District Courts can enjoin an agency from withholding documents under the FOIA. In a court proceeding (which may be in camera) the agency has the burden of proof. The FOIA also includes provisions designed to insure that disclosure matters will be disposed of by the courts expeditiously. Agency personnel who arbitrarily or capriciously deny a request for documents under the FOIA may be subject to discliplinary proceedings. Litigation costs may be assessed against an agency if the complaintant substantially previals in an FOIA action.

House Bill

Under the House bill (sec. 1212), written determinations issued after July 4, 1967, together with appropriate indices, would be placed in pubic reading rooms. Determinations could also be obtained under the FOIA.

The bill provides that before a letter ruling or technical advice memorandum is placed in a reading room, certain limited material is to be deleted. The bill provides for deletion of--

a. commercial or financial information, and other information, the disclosure of which could reasonably be expected to cause material financial harm to any person, and trade secrets;

b. information, the disclosure of which could reasonably be expected to constitute an unwarranted invasion of personal privacy;

c. information specifically exempted from disclosure under a Federal statute (other than the Internal Revenue Code), which is applicable to the Internal Revenue Service; and

d. national defense or foreign policy secrets and information regarding financial institutions.

In addition to the deletions described above, the House bill provides for deletion of identifying information from audit-type determinations (such as technical advice memoranda) and "required rulings." Identifying details could also be deleted in lieu of commercial, personal, etc. information where the portion of a ruling otherwise open to inspection would be inadequate to explain the application of the law to the facts.

The person to whom a written determination pertains would generally not receive the determination until agreement is reached with the Service on the extent of disclosure. If agreement is not reached on a required ruling or audit-type ruling, the Tax Court could consider the case (in camera, if appropriate) and determine the extent of disclosure. Interested parties could intervene in the case.

Generally, under the bill, written determinations would be publicly disclosed no earlier than 30 days nor later than 40 days after issuance (or after a decision of the Tax Court). However, where necessary to permit the completion of a transaction before disclosure, the disclosure could be postponed for up to one year if the delay permits greater disclosure of meaningful information.

Persons seeking additional disclosure could sue in the Tax Court or the District Court for the District of Columbia. Appeals could be taken to the Court of Appeals for the District of Columbia. Generally, the same procedural rules which would apply under the FOIA would apply to a case brought under the House bill for additional disclosure. However, under the bill, the person to whom the determination pertains or any person whose identifying details are included in the determination could intervene in the case. An action for greater disclosure could be brought within 3 years after any portion of a determination is made open to public inspection or 10 years after the determination is issued (if later).

Under the House bill, special rules would apply to determinations issued after July 4, 1967 (the effective date of the FOIA) and requested before September 25, 1975 (the date of the Ways and Means Committee decision). Identifying details would be deleted from these determinations and their disclosure would be made in order of issuance at the earliest practicable date (contingent upon the availability of funds appropriated to the IRS for this purpose). The Service would issue public notice before disclosing these prior determinations, allowing a 6-month period for persons to whom the rulings pertain to advise the Service as to the portion of a determination which they believe should not be open to public inspection. If agreement is not reached as to the extent of disclosure, the case could be brought to the Tax Court under the same rules as those applicable to required rulings.

Internal Revenue Service determinations disclosed under the bill could not be used as precedent by any person in any case.

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Committee Modifications:

1. Background files relating to Internal Revenue Service written determinations could be obtained by the public upon request, after payment of charges for search, deletion, and copying, with provisions for a reduction or waiver of these charges where the disclosure is in the public interest.

2. The House bill provides that private letter rulings for the future should disclose the names of the taxpayer asking for the rulings. The Committee decided that names would not be disclosed for future or, as described below, past rulings, but all cases would be "flagged" where there have been communications made to the IRS by anyone other than the taxpayer or his representative. This flagging would include any Treasury, White House, or Congressional communcations, but would not include those made by the staff of the Joint Committee on Internal Revenue Taxation.

3. Early disclosure (on a last-in/first-out basis) of prior determiantions which have been used by the Service as guidelines for other determinations would be provided for.

4. Prior nonguideline determinations could be obtained on request, after payment of charges for search, deletion, and copying.

5. The disclosure of Internal Revenue Service written determinations under pending court actions would not be delayed by this provision.

6. The Internal Revenue Service could designate determinations which would be used as precedent. The precedential status of excise tax determinations, however, would remain the same as under present law.

7. For prior rulings issued to individuals or corporations, unless the taxpayer consents, identifying details (including names) would not be disclosed.

8. The exemptions from disclosure would be more closely conformed to the FOIA standards.

9. The new rules would be the exclusive means of obtaining Internal Revenue Service written determinations (and background files if permitted). An exception would be provided for requests pending in the courts under the FOIA.

10. Disclosure of pre-1967 determinations would be provided.

Disclosure of Tax Return Information

The general statutory rules governing disclosure apply to tax "returns." In general, "return" is defined as including information returns, schedules, lists, and other written statements filed with Internal Revenue Service which are supplemental to or become a part of the return and other records, reports, information received orally or in writing, factual data, documents, papers, abstracts, memoranda, or evidence taken, or any portion thereof relating to returns and schedules, etc.

Under present law, all income tax returns are described as "public records." However, tax returns are generally open to inspection only under regulations approved by the President, or under Presidential order. This applies to returns concerning income tax, estate tax, gift tax, manufacturers excise taxes, communications tax, and transportation tax. Additionally, the statute provides a number of specific situations in which tax returns can be disclosed.

Disclosure to Congress

Present law.--Congressional committees are classified in three categories for disclosure purposes. The tax committees may inspect tax information in executive session. Select committees of the House and Senate may inspect tax information, in executive session, if specifically authorized to do so by a resolution of the appropriate body. Standing and select committees may inspect tax information under an executive order issued by the President for the committee in question, and on the adoption of a resolution (by the full committee) authorizing inspection.

The tax committees and select committees authorized to inspect tax information may submit "any relevant or useful" information obtained to the House or Senate.

Committee amendment.--1. Upon written request from the committee chairman, the Committee on Ways and Means, the Senate Finance Committee, and the Joint Committee on Internal Revenue Taxation, tax information may be obtained in a session closed to the public. The chief of staff of the Joint Committee on Internal Revenue Taxation would also, upon written request, have access to tax information. The Joint Committee could provide tax information to the Ways and Means Committee and the Senate Finance Committee witting in closed executive session. Closed sessions would not be required if taxpayers were not identified or if the taxpayers consented to disclosure of identity in open session.

2. Any other committee of the Senate or House specifically authorized by resolution of the appropriate body may obtain tax information, following committee action approving a request for the information, on the written request of the chairman and ranking minority member of the committee, in a session closed to the public.

3. With respect to the nontax writing committees, the resolution authorizing these committees to obtain tax information would have to specify the purpose for inspection and specify that no inspection is to be made unless there is no alternative source of information contained in the tax returns which is reasonably available to the committees.

4. Any of these committees could designate not more than 4 (2 majority and 2 minority) agents to inspect tax information.

5. The tax-writing committees could submit tax information to the Senate or House.

Disclosure to the White House

Present law.--The Internal Revenue Code does not provide specifically for disclosure to the President. However, the Code generally provides that disclosure can be made as authorized in rules and regulations established by the President. (Sec. 6103(a).) Under this provision, the President could issue a "rule or regulation" providing for his access, and that of White House employees, to tax information.

President Ford, by executive order, has established rules that govern the disclosure of tax information to the White House. (Executive Order 11805, September 20, 1974.) Under this order, tax returns are available for inspection by the President. Requests for inspection are to be in writing and signed by the President personally. Requests are to state the name and address of the taxpayer in question, the kind of returns which are to be inspected, and the taxable periods covered by the returns.

Under this executive order, other White House employees also may obtain tax information. The order provides that the President may designate, by name, employees of the White House who may receive tax information. This is limited to employees with an annual rate of basic pay not less than that prescribed by 5 U.S.C. Section 5316 (at present, $37,800 per year). No further disclosure (except to the President) may be made by any such employees without the written direction of the President.

Committee amendment. -- The Committee agreed to require the President personally to sign each request for tax information, such request specifying the reasons therefore and specifying the taxpayer, the returns involved and the taxable years involved. Any such request (and the reasons therefor) would be reported to the Joint Committee on Internal Revenue Taxation (JCIRT). This report would remain confidential and would not be disclosed unless disclosure is in the national interest. This report would be maintained by the JCIRT for two years. The Joint Committee in turn would make a separate annual report to the Congress. The President could designate by name and in writing (signed by him personally) other White House staff members who would have access to tax information. Qualified staff members would have to earn not less than the rate specified for employees at level V of the Executive Schedule ($37,800). Designated staff members could not in turn disclose this information to anyone but the President without the personal written direction of the President. Tax checks would be available for prospective employees of the Executive or Judicial Branch of the Federal Government on the written request of the president or the head of a Federal agency. However, no report would be required for tax checks requested by the President regarding current employees of the Executive Branch. A tax check would disclose whether the individual has filed income tax returns for the last three years, has failed in the current or preceding three years to pay any tax within 10 days after notice and demand or has been assessed a negligence penalty within this time period, has been under any criminal tax investigation and the results of such investigation, or has been assessed a civil penalty for fraud or negligence. The Department of the Treasury would also have to furnish an annual report regarding tax checks requested by the President and carried out by the IRS.

Justice Department -- Tax Cases

Present law. -- The Justice Department is responsible for almost all civil and criminal tax matters litigated before the Federal courts (except for the Tax Court).

Tax returns and other tax information may be furnished without written application to U.S. Attorneys and Justice Department attorneys in civil or criminal tax cases referred by the IRS to the Justice Department for prosecution or defense. Where the Justice Department is investigating a possible violation of the civil or criminal tax laws and the matter has not been referred by the IRS, A Justice Department attorney or U.S. Attorney may obtain tax information upon written application where it is "necessary in the performance of his official duties."

The Justice Department can obtain the returns of potential witnesses and third parties. Also, in a tax case (or any other case), the IRS will answer an inquiry from the Justice Department as to whether a prospective juror has been investigated by the IRS. However, other tax information is not available for examining prospective jurors.

Committee amendment.--1. The Committee agreed to allow disclosure to the Justice Department for civil and criminal tax administration purposes of the tax return and tax return information of the taxpayer whose civil or criminal tax liability is at issue.

2. The committee agreed to allow the return or return information of a third party to be disclosed to the Justice Department in the event the party was involved in a transaction with the taxpayer whose civil or criminal tax liability is at issue and the treatment of this transaction on such party's return or return information may be relevant to the resolution of an issue in the taxpayer's case. Only such part or parts of the third party's return or return information which reflects this transaction would be disclosed to the Justice Department.

3. A third party's return or return information could be disclosed in a tax proceeding only if it is shown that the treatment in such return or return information of a transaction with the taxpayer whose civil or criminal liability is at issue is directly related to the resolution of an issue in the taxpayer's case. Only such part or parts of the third party's return or return information which reflects the transaction would be subject to disclosure in the tax proceeding.

4. The return or return information of a third party witness in a tax proceeding would also be subject to the above rules.

5. The IRS could not disclose whether a potential juror ad been investigated by the IRS.

6. A written request by the Department of Justice, setting forth the reasons for the disclosure, etc., would be required except when the matter was referred to it by the IRS.

Federal Agencies--Nontax Criminal Cases

Present law.--(Justice Department) Under Treasury regulations, a U. S. Attorney or an attorney of the Department of Justice may obtain tax information in any case "where necessary in the performance of his official duties." This may be obtained on written application, giving the name of the taxpayer, the kind of tax involved, the taxable period involved, and the reason inspection is desired. The application is to be signed by the U. S. Attorney involved or by the Attorney General, Deputy Attorney General, or an Assistant Attorney General.

Tax information obtained by the Justice Department may be used in proceedings conducted by or before any department or establishment of the Federal Government or in which the United STates is a party.

The Service also will answer an inquiry from the Justice Department as to whether a prospective juror has been investigated by the IRS. However, other tax information is not available for examining prospective jurors.

The Organized Crime and Racketeering Section of the Department of Justice coordinates, through Federal Strike Forces, an integrated investigation and prosecution program against organized crime and racketeering activities. These investigations involve the participation of various Federal agencies, including the IRS.

Tax information may be used to provide strike force investigators leads relating to such criminal activity. Moreover, tax information is used to gather leads or make connections between various individuals and entities. The staff has been informed that the tax information considered most useful by strike force personnel in its nontax criminal investigation work is that which IRS investigators acquire from parties other than the taxpayer.

Tax information obtained in strike force investigations is used in prosecuting criminal offenses. Thus, requests are made for tax information pertaining to the defendant, and to defense witnesses in the course of the investigation, at the pretrial level, and sometimes during the trial. The returns of defense witnesses in nontax criminal trials are often requested to obtain information for cross-examination and impeachment of witnesses.

The tax returns of Government witnesses are also obtained in order to evaluate the veracity of their proposed testimony, as well as to evaluate their credibility in general.

Tax information also is obtained with respect to third parties who have had some transactional or other relationship with the defendant in order to seek investigative leads.

(Other Federal Agencies) In connection with the enforcement of nontax criminal statutes (as well as nontax civil statutes), tax information is available to each executive department and other establishments of the Federal Government (e.g., SEC and FTC) in connection with matters officially before them on the written request of the head of the agency. Tax information obtained in this manner may be used as evidence in any proceedings before any "department or establishment" of the United States or any proceedings in which the United States is a party.

Committee amendment. -- 1. The committee agreed to require that tax information be subject to disclosure to Federal agencies for nontax criminal purposes only upon the issuance of an order by a U. S. District Court. The order would be issued upon a showing that there is probable cause to believe, on the basis of the Federal agency's investigation, that a specified criminal act has been committed, that there is reasonable belief that the information contained in the return is probative of the commission of the crime and that no alternative source of the information sought is reasonably available. Only those parts of the return determined by the Court to be necessary to the investigation or prosecution would be subject to disclosure.

2. Information obtained by the IRS as to a possible violation of a Federal criminal law which did not come from the taxpayer could be disclosed in writing to the Justice Department and other Federal agencies in nontax criminal cases. A request for such information would have to be in writing and give the name of the taxpayer, the kind of tax involved, the taxable period involved, and the reason inspection is desired. The request would spell out in detail the reason why the information was desired.

3. Once the Justice Department or any Federal agency has received return information pursuant to a court order, further disclosure thereof in an administrative hearing or trial relating to the violation of the nontax criminal law would not be allowed unless there is a showing to the presiding hearing officer or judge that such return information is directly probative of the defendant's guilt. Admission of the return in this proceeding would not constitute reversable error in the event of an appeal of the District Court's findings in the nontax criminal case.

4. Neither the Justice Department nor any other Federal agency would be authorized to inquire of the IRS as to whether a potential juror or juror has been or is the subject of an IRS audit or investigation.

Nontax Civil Matters--Justice Department and Other Federal Agencies

Present Law

(Justice Department) Under the regulations, a U.S. Attorney or an attorney of the Justice Department may obtain tax information in nontax civil cases in the same manner and to the same extent as in nontax criminal cases.

The Justice Department has used tax returns in suits brought against the Government seeking money damages for injury or wrongful death. The Justice Department has informed the staff that tax information is used in these cases to verify the claims of loss of income, and also to determine, through claimed medical expense deductions, whether the plaintiff had suffered other injuries before or after the accident in question.

Tax information is also used in suits concerning the renegotiation of Government contracts, where the Renegotiation Board has determined that excess profits were earned on a Government contract. Here, tax information is used to verify the income earned on the contracts in question.

Nontax civil cases also involve affirmative money claims, including civil fraud claims, by the Government against various private parties. In these cases, tax information may be used to determine whether the defendant is financially able to pay the demand contemplated by the Government.

Tax returns are also requested after the Government has obtained a judgment against a party in order to verify statements made by the judgment debtor as to his financial ability to make payment of his debt.

(Other Federal Agencies) Tax information is available to each executive department and other establishments of the Federal Government in connection with matters officially before them. To obtain this information, the head of the agency must make written request to the IRS setting forth the name and address of the taxpayer, the kind of tax and tax period in question, the reason why the inspection is desired, and the name and position of the person who will actually inspect the tax information. Information obtained may be used as evidence in proceedings conducted by or before any Federal agency or proceedings to which the United States is a party.

Committee amendment. -- The Committee agreed to preclude disclosure of returns and return information to the Justice Department and other Federal agencies in nontax civil matters except those involving renegotiation of contracts cases where tax information is used to verify the income earned on the contracts in question.

Other Agencies--Inspection on a General Basis

Present law. -- Under the regulations, Federal agencies may, on a general basis, inspect tax information for qualified purposes without the head of the agency having to write a specific request to the IRS identifying the taxpayer and the reason for the desired inspection. For example, the Department of Health, Education and Welfare may inspect individual tax returns as required to administer Title II of the Social Security Act (old-age, survivor, etc., benefits). Inspection is authorized on the written application of any authorized officer or employee of the department.

Also, Customs, Secret Service, and other Treasury enforcement agents may obtain limited tax information on their own request, without the request of the head of their office. This includes information on whether a delinquent account has been issued whether an audit was made, whether an Intelligence investigation was conducted, and the taxpayer's address.

Committee amendment. -- The Committee approved provisions permitting the following:

1. To administer the Social Security Act, the Social Security Administration could obtain information concerning the tax on self-employment income, the Federal Insurance Contributions Act tax, and the withholding tax. Also, the Railroad Retirement Board could obtain information on the railroad retirement taxes.

2. Information could be disclosed to the Department of Labor and the Pension Benefit Guaranty Corporation to administer the pension reform act (Employee Retirement Income Security Act of 1974). Also, as provided under the pension reform act, registration statements providing information on employees' vested benefits could be furnished to the Social Security Administration.

3. Corporate tax information could also be disclosed to the Renegotiation Board as needed in administering the Renegotiation Act.

Statistical Use

Present law. -- Under the regulations, the Department of Commerce (Census Bureau and Bureau of Economic Analysis), the Federal Trade Commission, and the Securities and Exchange Commission are authorized to use information from tax returns for statistical purposes.

Other agencies which do not have Executive orders allowing general inspection of returns probably could obtain tax returns for statistical purposes under the regulations allowing disclosure on a case-by-case basis.

Committee amendment. -- The Committee agreed to permit disclosures for statistical use as follows:

1. The Census Bureau, the Bureau of Economic Analysis, and the Federal Trade Commission could obtain tax returns and limited tax information solely for statistical and research purposes authorized by law, but only such tax information as is necessary to carry out those statistical and research activities. The Federal Trade Commission and the Bureau of Economic Analysis would only be entitled to receive corporate tax return information.

2. Treasury regulations would specify the limited types of tax information (e.g., name, address, SSN, gross receipts, etc.) which would be supplied to each agency under the provision.

3. The publication of any statistical study which would identify any particular taxpayer would be prohibited.

State and Local Governments

Present law. -- Under the regulations, tax returns may be inspected by State tax officials for purposes of administering the State's tax laws. With the permission of the Commissioner and for purposes of State tax administration, a State may be allowed to inspect on a general basis all income, estate, and gift tax returns filed in the district in which the State is located. Additionally, the specifically identified returns of taxpayers who filed within the relevant district, and of taxpayers who filed in districts which do not include the State in question, may be inspected on a case-by-case basis on the written request of the State Governor.

At the Governor's written request, tax information also may be obtained for local governments to be used in administering their tax laws. Income tax information is not furnished directly by the IRS to local governments. Instead, State tax officials furnish such information to local governments where the IRS has approved such action at the request of the Governor.

Committee amendment. -- 1. Upon the written request of the principal tax official of the State, income, gift, highway use, FUTA, and estate tax information could be furnished to State tax officials solely for use in administering the State's tax laws. The tax information would not be available to the State Governor or any other nontax personnel.

2. Federal tax returns would not be available to local governments (but presumably those with income taxes could make use of State audits).

3. No tax information could be furnished a State unless the State establishes procedures (including detailed records of access and strict security measures) satisfactory to the IRS for safeguarding the tax information it received. If the IRS determines that these provisions are not being complied with, the IRS could terminate any disclosure arrangement with the State pending the adoption of adequate safeguards.

4. In the event of an unauthorized disclosure by State officers or employees, disclosure of Federal tax information to the State would stop until the IRS is satisfied that adequate protective measures have been taken to prevent a repetition of the unauthorized disclosure.

5. It would be a violation of Federal law, punishable in the same manner as an unlawful disclosure of Federal tax information, for State tax personnel to make an unauthorized disclosure of Federal tax information required by State law to be attached to the State tax return.

Persons with a Material Interest

Present law. -- Under the regulations, income tax returns presently are open to the filing taxpayer, trust beneficiaries, partners, heirs of the decedent, etc. "Return information", as opposed to the tax returns themselves, is only available to the taxpayer, etc. at the discretion of the IRS.

Also, the statute specifically authorizes the inspection of a corporation's income tax returns by a holder of 1 percent or more of the corporation's stock.

Committee amendment. -- The Committee agreed to permit disclosures to persons with a material interest as follows:

1. As under current regulations, persons with a material interest to whom disclosure could be made would include the filing taxpayer, either spouse who filed a joint return, the partners of a partnership, the shareholders of subchapter S corporations, the administrator, executor or trustee of an estate (and the heirs of the estate with a material interest that may be affected by the information), the trustee of a trust (and beneficiaries with a material interest), persons authorized to act on behalf of a dissolved corporation, a receiver or trustee in bankruptcy, and the committee, trustee or guardian of an incompetent taxpayer.

2. The provision in present law authorizing a one percent shareholder to inspect a corporation's return would be retained.

3. Return information (in contrast to "returns") could be disclosed only to the extent the IRS determines this would not adversely affect the administration of the tax laws.

Miscellaneous Disclosures

Present law. -- Under present law, several provisions of the regulations allow disclosure of tax information for miscellaneous administrative and other purposes. For example, accepted offers in compromise are open to inspection. Internal Revenue officers may disclose limited information to verify a deduction, etc. Additionally, in a number of cases, tax information may be disclosed at the discretion of the Commissioner, as the statute is wholly silent with respect to certain types of returns. For example, FICA tax returns and private foundation excise tax returns are within this category.

In other cases, the statute specifically requires public disclosure of certain types of returns. Under the Code, applications for exempt status by organizations and applications for qualification of pension, etc., plans are generally open to public inspection. Also, the annual reports of private foundations are open to public inspection. Returns with respect to the taxes on gasoline and lubricating oils are open to inspection by State officials. Under certain circumstances, the amount of an outstanding tax lien may be disclosed.

Upon inquiry, the IRS is to disclose whether any person has filed an income tax return for the year in question.

Committee amendment. -- The Committee agreed to provide that, in the interest of the orderly administration of the tax laws, additional disclosures would be permitted only as follows:

1. To any agency or person upon the taxpayer's written consent.

2. Offers in compromise, the amount of an outstanding tax lien, and information available to foreign governments under tax treaties.

3. Identities of income tax return preparers could be disclosed to State agencies charged with their regulation.

4. Tax returns would be open to public inspection in those situations where public disclosure is specifically provided for in present law (e.g., applications for exempt status by organizations, applications for qualification of pension, etc., plans, and the annual reports of private foundations). Private foundation excise tax returns would also be open to public inspection.

5. The IRS would be permitted to disclose identities in order to locate missing taxpayers who are due refunds.

6. The IRS would no longer be permitted to disclose, upon inquiry, whether a person has filed an income tax return for a particular year.

7. Taxpayer identify information (in particular, address information and income) could be disclosed to Federal and State agencies for purposes of locating deserting parents and determining ability to make support payments.

8. Alcohol, tobacco and firearms tax information could be disclosed pursuant to Treasury regulations to Federal agencies that require this information in their official duties.

9. Disclosure would be made to the GAO in accordance with the committee's prior decision to order H.R. 8948 reported favorably, as amended by the Committee. This would permit the GAO to audit the Internal Revenue Service and the Bureau of Alcohol, Tobacco and Firearms, and would provide access to tax returns and tax return information in connection with such audits. The committee amendment would limit access to tax returns and tax return information to instances where prior consent has been obtained from the Ways and Means Committee, the Finance Committee or the Joint Committee on Internal Revenue Taxation.

10. Disclosure could be made by the IRS to correct a misstatement of fact which has become public, but only after approval has been obtained from the Joint Committee. Disclosure could also be made to the media when, after reasonable effort and time, the IRS is unable to locate a taxpayer who is due a tax refund.

PRESS RELEASE

FOR IMMEDIATE RELEASE
May 27, 1976 - Part I

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

FINANCE COMMITTEE ACTS ON TAX REVISION ISSUES (H.R. 10612)

The Honorable Russell B. Long (D., La.), Chairman of the Senate Committee on Finance, announced today that the Committee continued its work on the House-passed tax revision bill (H.R. 10612).

Committee Orders Bill Reported

The Committee ordered favorably reported H.R. 10612 with amendments. In addition to reporting the bill, the Committee made the following decisions:

Extension of Existing Tax Cuts

Present law - Individuals.--The Tax Reduction Act of 1975 provided several tax reductions for the year 1975. The Revenue Adjustment Act of 1975 extended these tax reductions, with certain modifications, for the first half of 1976.

House bill.--The Tax Reform Act of 1975, as it has passed the House, makes permanent the increase in the standard deduction enacted for 1975 in the Tax Reduction Act of 1975. For single returns this would mean a minimum and maximum standard deduction $100 less than a full-year extension of the changes in the Revenue Adjustment Act of 1975. For joint returns the House changes in the minimum and maximum standard deduction are $200 less than would occur under a full-year extension of the 1976 tax cuts. (The percentage standard deduction remains at 16 percent under both the House bill and the Revenue Adjustment Act.)

The House bill also includes a tax credit for the year 1976 equal to 2 percent of the initial $12,000 of taxable income.

The House bill does not include any extension of the earned income credit.

The House bill also provides that a refund of the earned income credit is not to be taken into account as income or receipts for determining eligibility or benefits under Federal or Federally-assisted aid programs.

Present law - Corporations.--Prior to 1975, corporate income was subject to a normal tax of 22 percent and a surtax of 26 percent, with the initial $25,000 of taxable income exempt from the surtax. In the Tax Reduction Act of 1975, the surtax exemption was increased to $50,000 and the normal tax was reduced to 20 percent on the initial $25,000 of taxable income. These changes applied only to the year 1975, but were extended through the first half of 1976 in the Revenue Adjustment Act of 1975.

House bill.--The House bill extends these tax cuts through the end of 1977.

Committee amendment.--The Committee agreed to make the following provisions of present law permanent:

- -- Minimum standard deduction of $1,700 for single returns and $2,100 for joint returns; percentage standard deduction 16% up to $2,400 for single return, $2,800 for joint return.
- -- Corporate surtax rate and exemption changes (20% on first $25,000, 22% on second $25,000).
- -- Earned income credit ("work bonus")

The tax credit equal to the greater of $35 per personal exemption or 2 percent of the first $9,000 of taxable income (for the full year) would be extended through June 30, 1977.

Disclosure of Tax Return Information

A. Procedures and Records Concerning Disclosure

Present law. -- Several different offices of the IRS have responsibility for approving disclosure of tax information to particular agencies. For example, the Disclosure Staff (National Office) deals with case-by-case requests for tax returns by other Federal agencies while the Statistics Division deals with the disclosure of information to Federal agencies (largely on magnetic tape) to be used for statistical purposes. Additionally, the Planning and Research Division deals with disclosure of information on magnetic tape to the States while the Disclosure staff deals with case-by-case disclosure to the States.

While these offices negotiate and approve disclosures of tax information, the actual transfer of the information generally takes place in other offices, such as the Service Centers, District Office, Computer Center, etc. In addition, District Directors and Service Center Directors are authorized to approve applications for certain types of disclosure, such as disclosure to persons with a material interest in the returns and returns of the taxpayer (in tax cases) to U. S. attorneys.

The IRS presently maintains records concerning disclosure. However, the staff understands that the type of records maintained are not standardized as between, e.g., Service Centers, and that the IRS does not maintain a complete inventory of records so, for example, it cannot determine what has been disclosed and what has been returned or destroyed.

Under the Privacy Act of 1974, each Federal agency is to account for disclosures to other agencies, noting the date, nature, and purpose of each disclosure and the name and address of the agency to which disclosure is made. This rule does not apply to disclosures by State agencies. The accounting is designed to enable the agency to inform the individual concerned of disclosures made with respect to him.

Committee amendment. -- The Committee agreed to adopt the following requirements with respect to procedures and records concerning disclosure:

1. In those cases where returns and return information would be open to inspection under other provisions, they would be open to inspection at the times, in the manner, and at the places prescribed by Treasury regulations.

2. The IRS would be required to have one office which would have the responsibility for approving all disclosures of tax returns and tax information. However, IRS district offices would have line authority for disclosure of tax returns. Functional authority concerning disclosure would be vested in the single national office set up by the IRS.

3. The IRS would be required to have a standardized system of permanent records on the use and disclosure of tax returns and information. This would include a record of all requests for inspection and disclosure of tax information and of all inspections and disclosures of tax information. The records are to include the reason for the request and the date of the request.

4. Each Federal and State Agency that receives tax information would be required to maintain a standardized system of permanent records on the use and disclosure of that information. Maintaining such records would be a prerequisite to obtaining and continuing to receive tax information.

5. The record-keeping requirements under section 6103 would effectively modify certain record-keeping requirements under the Privacy Act which would be inappropriate as applied to tax administration. The record-keeping machinery of the Privacy Act would not be utilized to resolve substantive tax disputes.

6. Necessary activities carried out by IRS contractors and Federal storage facilities in connection with the processing, storage and transmission of tax returns and tax return information where necessary for tax administration purposes would not constitute unlawful disclosure of such materials by the IRS.

B. Safeguards

Present law. -- Except for the general criminal penalty for unauthorized disclosure, the tax law does not provide rules for safeguarding tax information disclosed by the IRS to other agencies. However, some of the existing Agreements on Coordination of Tax Administration entered into between the Federal Government and the States include provisions for safeguarding tax information.

The Privacy Act requires that each agency establish appropriate administrative, technical, and physical safeguards to secure records on individuals. This requirement applies to each Federal agency that maintains a "system of records". This provision does not apply to State or local government agencies that receive Federal tax records.

The IRS has no authority under the Privacy Act to audit the safeguards established by other agencies, or to stop disclosure to other agencies that did not properly maintain safeguards.

Committee amendment. -- The Committee agreed to adopt the following provisions with respect to safeguards for tax returns and tax information:

1. No tax information would be furnished to another agency unless the other agency establishes procedures satisfactory to the IRS for safeguarding the tax information it receives. Disclosure of tax information to other agencies would be conditioned on the receipient maintaining a secure place for storing the information, restricting access to the information to people whose duty requires access and to people to whom disclosure can be made under the law, providing other safeguards necessary to keeping the information confidential, and returning or destroying the information when the agency is finished with it. Regulations would be specifically authorized to allow the IRS to carry out these provisions.

2. If there are any unauthorized disclosures by employees of the other agency, disclosure of tax information to that agency must be stopped until the IRS is satisfied that adequate protective measures have been taken to prevent a repetition of the unauthorized disclosure. In addition, the IRS could terminate disclosure. In addition, the IRS could terminate disclosure to any agency if the IRS determines that adequate safeguards are not being maintained by the agency in question. The IRS is to review, on a regular basis, safeguards established by other agencies.

C. Reports to Congress

Present law. -- Since 1971 the Joint Committee on Internal Revenue Taxation has received from the IRS a semi-annual report on disclosure of tax information.

Committee amendment. -- The Committee agreed to require the following reports to Congress:

1. Within 90 days after the end of each calendar year, the IRS would be required to report to the Joint Committee on all requests received for inspection or disclosure of tax information. The report would be confidential unless a majority of the members of the Joint Committee agree by record vote to disclose all or any portion of the report. The report would include, as a separate section which would be publicly disclosed in all cases, a listing of all agencies receiving tax return information, the number of cases in which tax returns or tax return information was disclosed to them during the year, and the general purposes for which the requests were made.

2. The IRS would be required to report quarterly to the tax committees on the procedures established for maintaining the confidentiality of tax information disclosed outside the IRS, on the implementation of these procedures, and on any problems that may develop in connection with these procedures.

D. Enforcement

Present law. -- Unauthorized disclosure of Federal tax information by a Federal or State employee is a misdemeanor punishable by a fine of up to $1,000, or imprisonment of up to one year, or both (together with the costs of prosecution). Federal officers or employees also are to be dismissed from office or discharged from employment. It also is a misdemeanor (punishable in the same manner) for any person to print or publish in any manner not provided by law any income tax return or financial information appearing therein.

One percent shareholders who examine a corporate return are guilty of a misdemeanor (punishable as above) if they disclose in any manner "not provided by law" the amount of any income, etc., shown on the return.

Committee amendment. -- The committee agreed to adopt the following provisions with respect to the penalties for unlawful disclosure of tax information:

1. Violation of the disclosure rules would be a felony. The criminal penalties for unlawful disclosure would be increased to $5,000 (instead of $1,000) and up to five years in jail (instead of one year).

2. Willful receipt of tax information which the recipient knows is disclosed in violation of the law is to be a felony punishable by a fine of up to $5,000 or up to five years imprisonment or both.

3. Any person who willfully or negligently discloses tax information in violation of the law would be liable to any taxpayer injured by the disclosure for civil penalties (including actual and punitive damages plus court costs). These damages shall not be less than liquidated damages of $1,000 for each disclosure.

E. Other

The IRS would be authorized to disclose relevant and material return information to an IRS employee and his attorney in an adverse action proceeding against the IRS employee. This need for limited disclosure arises, for example, in harassment proceedings brought against IRS agents.

Joint Committee Refund Cases

Present law. -- One of the statutory duties of the Joint Committee on Internal Revenue Taxation in investigating the operations and effect of the Federal tax laws is the review of cases involving refunds of income, war profits, excess profits, estate, and gift taxes in excess of $100,000. The Code forbids payment of such refunds until at least 30 days have passed after the Administrative report has been made to the Joint Committee. The number of refund cases received by the Joint Committee has increased from 647 in 1970 to 1,434 in 1975.

Committee amendment. -- The Committee agreed to the following modifications of present law:

1. The jurisdictional amount would be increased to $200,000.

2. The Committee agreed to extend Joint Committee jurisdiction to include refund cases involving the special excise taxes on private foundations and pension plans under chapters 42 and 43 of the income tax provisions.

3. The Committee also agreed to authorize the Chief of Staff of the Joint Committee to conduct a post-audit review on the handling of the returns and issues by the Internal Revenue Service.

Pension Provisions

Present law. -- Generally, personal savings are set aside out of after-tax income, so that the income tax applies equally to income regardless of whether it is spent on consumption items or saved. However, this general rule is departed from in the following cases:

1. Income saved by an employee under a qualified pension or profit-sharing plan which satisfies certain requirements of the tax law is generally not taxed until distributed by the plan. Lump-sum distributions from a qualified plan are subject to special 10-year income averaging rules and special estate and gift tax exclusions apply.

2. Income saved by a self-employed individual under an H.R. 10-plan (a qualified plan covering a self-employed individual) is generally subject to the same treatment as income saved by an employee under a qualified plan except that--

(a) the amount of income that may be set aside on a tax-deferred basis is generally limited to the lesser of $7,500 or 15 percent of earned income (under a special rule, the "jockeys provision", a minimum of $750 may be set aside despite the 15-percent limit, but the $750 minimum amount may not exceed 25 percent of earned income);

(b) an excise tax applies to excess amounts contributed to an H.R. 10-plan; and

(c) the special estate and gift tax exclusions do not apply to benefits of a self-employed individual.

3. Employees of exempt charitable organizations and of governmental educational institutions may have income set aside in an annuity contract or open-end mutual fund under a "tax-sheltered annuity" arrangement.

4. An individual who is not covered by a qualified plan, a tax-sheltered annuity arrangement, or a governmental plan (whether or not qualified), may set aside the lesser of $1,500 or 15 percent of earned income for retirement in an individual retirement account (IRA) on a tax-deferred basis.

House bill. -- Under the House bill (sec. 1502)--

(a) An individual who is an active participant in a qualified plan (other than a governmental plan) would be allowed a deduction for his contributions to an IRA and for his contributions to a qualified plan in existence on September 2, 1974.

(b) The aggregate deductible contributions to the IRAs and plans for a year could not exceed the limits on IRA contributions (the lesser of $1,500 or 15 percent of compensation), reduced by "qualifying employer contributions" to qualified plans on behalf of the employee during the year.

(c) In the case of a defined contribution plan, qualifying employer contributions would be the amounts actually allocated to the employee's account during the year (consisting of employer contributions and forfeitures).

(d) In the case of a defined benefit plan, the qualifying employer contributions would be the annual cost of providing the employee's benefit under the plan (not necessarily the amount actually contributed that year by the employer).

(e) Amounts contributed to a qualified plan by an employee and deductible under these rules would be held in a special account under the plan, called a "limited employee retirement account" (LERA). The account would generally be subject to the same rules as an individual retirement account.

Committee amendment. -- The Committee agreed to delete this provision of the House bill. However, the Committee approved a provision extending the House provision to government employees contingent upon the House provision being adopted. In addition, the Committee approved the following provisions:

1. A member of the Armed Forces Reserves or National Guard would be permitted to make tax deductible IRA contributions for a year in which his service in the Reserves or National Guard is less than 90 days (excluding active dity for training).

2. A contribution of up to $750 could be made out of earned income to an H.R. 10-plan (without regard to the 25 percent overall limitation) by an individual for a year in which his adjusted gross income does not exceed $15,000.

3. The Committee agreed to extend to December 31, 1978, the time set for the Congress to study the appropriate tax treatment of employees covered under "salary reduction pension plans," "cash or deferred profit-sharing plans" and "cafeteria plans" which provide various nonqualified fringe benefits. This provision amends sec. 2006 of the Employee Retirement Income Security Act of 1974.

4. Tax-exempt organizations maintaining sec. 403(b) annuities for their employees would be permitted to invest the funds so set aside with closed-end investment funds.

5. It would be made clear that a segregated asset account held by a life insurance company under a qualified pension or profit-sharing plan need not provide benefits in the form of an annuity.

6. The Committee agreed to extend the coverage of the IRA provisions to non-employed wives who are otherwise precluded from establishing IRAs. Under the Committee amendment, up to $2,000 or 15% of earned income (whichever is less) could be contributed to an IRA established by a taxpayer for himself and his non-employed wife. Such IRA's would have to provide that all funds set aside would be for the benefit of both spouses, under a joint and survivor arrangement. Alternatively, separate IRA's could be established for each spouse subject to a maximum annual contribution of $1,000 per spouse (subject to the same 15% of earned income limit set forth above).

Real Estate Investment Trusts

Present law. -- Under present law, real estate investment trusts ("REITs") are provided with the same general conduit treatment that is applied to mutual funds. Therefore, if a trust meets the qualifications for REIT status, the income of the REIT which is distributed to its owners each year generally is taxed to them without being subjected to a tax at the REIT level (the REIT being subject to tax only on the income which it retains and on certain income from property which qualifies as foreclosure property).

In order to qualify for conduit treatment, a REIT must so elect and must satisfy four tests on a year-by-year basis; organizational structure, source of income, nature of assets, and distribution of income.

House bill. -- In general, the House bill makes the following changes with respect to the provisions of the tax law relating to REIT's:

Under present law, a REIT generally is required to distribute 90 percent of its taxable income each year to its shareholders. If it does not meet this requirement, the trust will be disqualified as a REIT and thus must pay tax on its income as if it were a regular corporation. Under the House bill, a REIT will not be disqualified if it is determined, on audit, that the failure to meet the 90-percent distribution requirement was due to reasonable cause. In this case, the REIT is to be allowed to distribute deficiency dividends to its shareholders to avoid disqualification. However, interest and penalties are to be imposed on the amount of the deficiency dividends paid under this procedure.

Under present law, certain percentages of a REIT's gross income must be derived from designated sources. The House bill provides that if a REIT were found to have failed to meet the income source tests, it would not be disqualified, but would be allowed to pay tax on the net income attributable to the amounts by which it failed to meet the income source tests. This provision would be available only if the REIT initially had reasonable ground to believe that it had met the income source tests.

Present law prohibits a REIT from holding property (other than foreclosure property) for sale to customers. The House bill eliminates the "holding" prohibition and substitutes a limit on the amount of income a REIT can derive from property so held. Under the House bill, a REIT could have a de minimis amount (up to one percent) of its gross income from such sources, and this income would be subject to corporate tax. Any income from such sources in excess of one percent would be subject to an additional tax, but would not disqualify the REIT, provided the REIT had reasonable grounds to believe that the excess income was not holding-for-sale income.

The House bill also provides that certain types of income that customarily are earned in a real estate business but which do not now qualify under the income source tests are to be treated as qualifying income. These include (a) certain rents from personal property leased together with the real property; (b) changes for services customarily furnished in connection with the rental of real property whether or not such changes are separately stated; and (c) commitment fees received for entering into agreements to make loans secured by real property.

The income source requirements are increased by the House bill so that at least 95 percent of the REIT's income must be from passive sources. Also, all income, other than passive income, would be subject to corporate tax.

Under the House bill, a REIT would be required to designate the year to which a dividend payment relates. (Under present law, a dividend may relate either to the year in which it is paid, or the immediately preceding year in most cases.) Also, a REIT is to be subject to a 3 percent charge on the amount by which it fails to distribute at least 75 percent of its income in the year received. In addition, a new REIT would be required to be on a calendar year for tax purposes.

Certain other changes are made concerning technical rules applicable to REIT's, including changes in the rules regarding income from sale of mortgages held for less than four years, and regarding options to purchase real property.

Under the House bill, the provisions outlined above would apply generally to taxable years of real estate investment trusts beginning after the date of enactment.

Committee amendment. -- The Committee agreed to the following modifications:

1. The distribution requirement would be increased from 90% to 95% subject to a 3-year delayed effective date.

2. A REIT would not be disqualified for a violation of the income source test, if (a) the failure is due to reasonable cause and is not due to willful neglect and (b) the trust does not commit fraud on its return in reporting gross income qualified for the tests. However, to encourage compliance with the income source tests, net income attributable to the amount by which the REIT failed the gross income tests could be subject to tax at 100 percent rate. (Under present law, the REIT is disqualified if it fails those tests.)

3. Income not qualifying for the 90 percent income source test (which is increased to 95 percent under the bill) would not be subject to corporate tax. (The increase would have a 3-year delayed effective date.)

5. In the case of holding-for-sale, the committee provided that all holding for sale income of a REIT would be subject to tax at 100 percent rate.

6. With respect to the treatment of losses, the committee provided that a capital gain of a REIT could be offset by ordinary losses. Also, a REIT would be allowed an 8-year carryover with respect to a net operating loss.

7. If a REIT intentionally disqualifies itself, the committee provided that it could not qualify again for 5 years.

8. If interest is based in part on profits, the committee provided that the interest is to be disqualified income for purposes of the income source tests. In such a case, disqualification of the income would be applied after the date of the committee decision.

Railroad provisions -- grading and tunnel bores

Present law. -- Domestic railroad common carriers may amortize railroad grading and tunnel bores that were placed in service after 1968 over a 50-year period on a straight-line basis. This deduction is in lieu of any depreciation or any other amortization deduction for any year for which the election applies.

No such provision applies to grading and tunnel bores placed in service before 1969.

Committee amendment. -- The committee agreed to the provision in the House bill to allow taxpayers who have elected 50-year amortization for railroad grading and tunnel bores placed in service after 1968 to include in that election grading and bores placed in service before 1969.

Railroad Provisions -- Track Accounts: Track, Ties, Etc.

Present law. -- For tax purposes, railroad track and ties are treated under the retirement-replacement method of accounting. Under this system, original track and ties are capitalized, but no depreciation is claimed. When the original track and ties are replaced with tracks and ties of like kind or quality, their costs (both materials and labor) are deducted as current expense. If the replacement is an improvement of quality, the value of the betterment portion is capitalized and the remainder is expensed.

Where wood ties are replaced with concrete ties, the Service has held that this replacement with a different kind of tie is a retirement and substitution under which the cost of the new tie is capitalized, and the replaced wood tie is expensed.

House bill. -- Replacement of an existing tie with a tie of different or improved kind or quality may be treated as a current expense deduction. This includes replacement of wood ties with concrete or steel ties. Materials and labor costs involved in acquiring and installing replacement ties are eligible for a current expense deduction.

Committee amendment. -- In lieu of the House provision, the Committee agreed to the following:

1. Concrete and other non-wood replacement ties would be treated as a betterment, under which the taxpayer would be allowed to deduct the costs of the non-wood replacement up to the current value of a wood replacement, with the remaining cost capitalized.

2. Railroad track, ties, and other items in the track account would be made eligible, on the taxpayer's election, for straight-line amoritization over a fixed period. This alternative, in effect, provides for capitalization of items in the track account instead of the present replacement-retirement system of accounting. The amortization period would be set at ten years.

Railroad Provisions -- Investment Tax Credit

Present law. -- Railroad rolling stock and other equipment with a useful like of 7 or more years is eligible for the investment tax credit under the same conditions as other tangible personal property. This includes the limitation of the credit to 50 percent of tax liability (about $25,000) and carryover of credits not used in the year earned because of the 50 percent limitaiton.

Committee amendment. -- The Committee agreed that unused investment credits would be carried forward indefinitely until applied against tax liability. This proposal could be combined with proposal 3 above for a FIFO sequencing of credits against tax liability.

Five-Year Amortization for Low Income Housing

Present law. -- Under present law, the taxpayer can elect to compute depreciation of certain rehabilitation expenditures in connection with low and moderate income rental housing under a straight-line method over a period of 5 years (60 months).

To qualify for the special treatment, the additions or improvements must have a useful life of 5 years or more, the aggregate rehabilitation expenditures as to any housing unit may not exceed $15,000 and the sum of the rehabilitation expenditures for two consecutive years (including the taxable year) must exceed $3000 per rental unit.

Under current Treasury regulations, occupants of a dwelling unit are considered families and individuals of low or moderate income only if their adjusted income does not exceed 90 percent of the income limits described by the Secretary of Housing and Urban Development (HUD) for occupants of projects financed with certain mortgages insured by the Federal government.

House bill. -- The House bill provides a two-year extension of the special five-year depreciation provisions for expenditures to rehabilitate low and moderate income rental housing.

The House bill also increases the amount of rehabilitation expenditures that can be depreciated over the special five-year period from $15,000 to $20,000 per dwelling unit.

Committee amendment. -- The committee agreed to extend the provisions of the special five-year depreciation provisions to include expenditures incurred pursuant to a "binding contract" which is in effect on the new expiration date rather than as at present, paid or accrued by such date. In addition, the committee agreed to modify the definition of low and moderate income housing to set the income limits consistent with those established for the Section 8 Leased Housing Program.

Tax-exempt status of condominium, cooperative, and homeowner associations

Present law. -- In developing a real estate subdivision, a condominium project, or a cooperative housing project, it is common for developers to form owners' associations as an integral part of the overall development. Generally, membership in the association is open only to owners of lots or dwelling units and is normally required as a condition of ownership.

Such associations are funded primarily by periodic assessments of the members. Generally, there are two categories of assessments and expenditures -- operating and capital.

Under present law, generally a homeowners' association or a condominium association may qualify as a tax-exempt civic league or social welfare organization only if it meets three requirements. First, the association must serve a "community" which bears a reasonable, recognizable relationship to an area ordinarily identified as a governmental subdivision or unit. Second, it must not conduct activities directed to the exterior maintenance of any private residence. Third, common areas for facilities that the association owns and maintains must be for the use and enjoyment of the general public.

If an association is unable to meet these three requirements, it will ordinarily be taxed as a corporation. In general, this means that the excess of current receipts over current expenditures at the end of the year would be taxable to it, unless the excess is refunded to the members or applied to the subsequent year's assessment. Assessments designated to be used solely for making capital improvements are not current income to the association but may be treated as contributions to capital by the owner-members of the association. However, income earned by the association on its accumulated funds is taxable to the association.

House bill. -- Under the House bill (sec. 1301), if a qualified "cooperative housing association" so elects, it is not to be taxed on any "exempt function income". Exempt function income includes membership dues, fees, and assessments received from persons who own residential units in the particular condominium, subdivision, or cooperative and who are members of the association.

The association is to be taxed on any net income which is not exempt function income. For example, any interest earned on amounts set aside in a sinking fund for future improvements is taxable. Similarly, any amount received from persons who are not members of the association for use of the association's facilities would be taxable. Deductions are to be allowed for expenses directly connected with the production of taxable income. The bill provides a $100 deduction against taxable income so that associations with only a minimal amount of taxable income will not be subject to tax.

A cooperative housing association is to be taxed as a corporation without the surtax exemption.

Generally, three different types of homeowners associations may elect to be treated as tax-exempt cooperative housing associations under the bill: Cooperative housing corporations, condominium management associations, and residential real estate management associations.

To qualify for this treatment under the House bill, a cooperative housing association must meet several requirements. First, the association must be organized and operated to provide for the management, maintenance, and care of association property. Although the property maintained by the association is generally property owned by the association and available for common use by all the members, the association may maintain areas that are privately owned but affect the overall appearance and structure of the project.

Second, a cooperative housing association must meet certain income and expenditure tests. To satisfy the income test, at least 60 percent of the association's gross income must consist solely of membership dues, fees, or assessments from tenant-stockholders, owners of residential units, or owners of residences or residential lots, as the case may be. To satisfy the expenditure test, at least 90 percent of all of the annual expenditures of the cooperative housing association must be to manage, maintain, and care for, or improve, association property. Qualifying expenditures include both current and capital expenditures on association property.

In addition to the general requirements, in the case of a condominium management association, substantially all of the dwelling units must be used as residences. Similarly, in the case of a residential real estate management association, substantially all the lots or buildings must be used by individuals for residences. In the case of a cooperative housing corporation, the corporation must meet the special definition for cooperative housing corporations under section 216 (b)(1).

Committee amendment. -- The Committee agreed to the following modifications: The provision would be inapplicable to cooperative housing corporations. However, it would be made clear that cooperative housing corporations are entitled to offset rental income from tenant-shareholders with depreciation on property leased to such tenant-shareholders, notwithstanding one court case which reached a contrary result.

Tax Treatment of Certain 1972 Disaster Loans

Present law.--Under present law, taxpayers are generally allowed to deduct their losses sustained during the taxable year, including losses attributable to fire, storm and other casualty, to the extent that the losses are not compensated for by insurance or otherwise. In the case of any loss attributable to a major disaster which occurred in an area authorized by the President to receive disaster relief, a special rule allows the loss, at the election of the taxpayer, to be deducted on the return for the year immediately before the year of the disaster (that is, the loss may be deducted on the return generally filed in the year the disaster occurs).

Where a deduction resulting from a loss is claimed in one year, and compensation is paid for the loss in a later year, the compensation is generally required to be taken into income by the taxpayer in the later year.

House bill.--Under the House bill, a taxpayer who received income in the form of a cancellation of a disaster loan, or in the form of compensation in settlement of a tort claim with respect to certain disaster losses sustained in 1972 which were determined by the President to warrant disaster assistance, would be accorded special tax treatment to the extent that the cancellation or tort settlement does not exceed $5,000. The tax on the first $5,000 of compensation received in this type of case is not to exceed the tax which would have been payable if the $5,000 (or lesser) deduction had not been claimed. This treatment applies only if the taxpayer elects to come under these provisions. The $5,000 amount would be reduced by $1 for each $1 of the taxpayer's adjusted gross income over $15,000 ($7,500 in the case of a married taxpayer filing a separate return) for the year in which the deduction for the loss was taken.

The House bill also provides that any tax with respect to this $5,000 (or lesser) amount still unpaid on October 1, 1975, may be paid in three equal annual installments, with the first installment payable on April 16, 1976. Also, no interest on any deficiency with respect to this $5,000 amount is to be payable for any period prior to April 15, 1976, and no interest is to be payable on any installment payment before the due date for that installment.

Committee amendment.--The Committee agreed to the House provision, but changed the due date from April 15, 1976 to April 15, 1977.

Tax Treatment of Disaster Payments

Present law.--Under present law, insurance proceeds received by a taxpayer as a result of destruction or damage to crops may be included in income in the year following the year of their receipt, if he can establish that the income from the crops which were destroyed or damaged would otherwise have been properly included in income in the following year.

The purpose of this provision was to avoid the doubling up of income for cash basis farmer by including crop insurance proceeds in income in the year they were received rather than in the year following the year of receipt, which would generally be the pattern of income receipt from sales of crops.

Because of this doubling up of income in the year of receipt, the farmer would have only deductions and no income to report in the next year and therefore would be likely to have a net operating loss to carry back and offset against income in the prior year.

House bill.--In the case of a taxpayer using the cash receipts and disbursements method of accounting, payments received under the Agricultural Act of 1949, as amended by the 1973 Act, would be included in the taxable income of the taxpayer, at his election, in the year in which the income normally received from the crops would have been reported.

This provision is to apply only to payments received as a result of (1) destruction or damage to crops caused by drought, flood or any other natural disaster, or (2) the inability to plant crops because of a natural disaster.

The House bill would apply to amounts received after December 31, 1973, in taxable years ending after that date.

The Committee agreed to the House bill.

Tax Treatment of Certain Debts Owed by Political Parties to Accrual Basis Taxpayers

Present law.--Any deduction generally allowable for bad debts or for worthless securities is not allowed for a worthless debt owed by a political party. This rule applies to all taxpayers other than a bank, but, where the debt arises out of the sale of goods or services, the rule in practice affects only taxpayers utilizing the accrual method of accounting (because only these taxpayers would have taken into income the receipts which give rise to the debt).

Present law for this purpose defines political parties to include all committees of a political party and all committees, associations, or other organizations which accept contributions or make expenditures on behalf of any individual in any Federal, State or local election.

House bill.--The House bill adds an exception to the provision disallowing a deduction for bad debts owed by political parties. The exception applies only to taxpayers who use the accrual method of accounting. These taxpayers are to be allowed a bad debt deduction with respect to debts which are accrued as a receivable in a bona fide sale of goods or services in the ordinary course of their trade or business.

The bill limits this exception to those cases in which 30 percent of all of the receivables accrued in the ordinary course of all of the trades or businesses of the taxpayer are due from political parties.

The bad debt deduction is to be allowed only if the taxpayer has made substantial continuing efforts to collect on the debt.

This provision applies to taxable years beginning on or after January 1, 1975. It also applies to taxable years beginning before January 1, 1975, for which the assessment of a deficiency, or the making of a refund, or the allowance of a refund or credit of any overpayment, is not barred on the date of enactment of this provision.

Committee amendment.--The Committee adopted the House provision, but with a January 1, 1977 effective date.

Clarification of Definition of Produced Film Results

Present Law. -- Under present law, a corporation which is a personal holding company is taxed on its undistributed personal holding company income at a rate of 70 percent. A corporation may be a personal holding company where five or fewer individuals own 50 percent or more in value of its outstanding stock and where at least 60 percent of the corporation's adjusted ordinary gross income comes from specified types of passive income.

One income category treated as personal holding company income is "produced film rents." Generally, this category covers payments received by the corporation from the distribution and exhibition of motion picture films if these rents arise from an "interest" in the film acquired before its production was substantially completed. Produced film rents are not treated as personal holding company income, however, if such rents constitute 50 percent or more of the corporation's ordinary gross income. The qualifying rental interest under this category is one which arises from participation in the production of the film.

A question has arisen, under a recent Tax Court case, as to whether an "interest" in a film, for purposes of the definition of "produced film rents", must be a depreciable interest.

House Bill. -- Under the House bill, in the case of a producer who actively participates in the production of a film, the term "produced film rents" for purposes of personal holding company income would include an interest in the proceeds or profits from the film, but only to the extent such interest is attributable to such active participation.

This provision would apply to taxable years ending on or after December 31, 1975.

The Committee agreed to the provision in the House bill which provides that, in the case of a producer who actively participates in the production of a film, the term "produced film rents" for purposes of personal holding company income would include an interest in the proceeds or profits from the film, but only to the extent such interest is attributable to such active participation.

Prepublication Expenditures for Publishers

Present Law. -- The Internal Revenue Service regulations issued under section 174 (a) (1) specifically exclude expenditures for research in connection with literary, historical, or similar projects from currently deductible research and experimental expenditures and require that such expenditures be capitalized. Prepublication expenditures are those paid or incurred in connection with the trade or business of publishing for the writing, editing, compiling, illustrating, designing, or other development or improvement, of a book, teaching aid, or similar product.

Revenue Ruling 73-395 holds that costs incurred by an accrual basis taxpayer in writing, editing, design and art work directly attributable to the development of textbooks and visual aids do not constitute research and experimental expenditures under section 174, and that these costs cannot be inventoried (under sec. 471) but, instead, must be capitalized (under sec. 263) and may be depreciated (under sec. 167 (a)).

The ruling also states that expenses incurred in the actual printing and publishing of textbooks and visual aids should be inventoried (under sec. 471) with a part of the costs apportioned to books and visual aids still on hand at the end of a taxable year. Expenses for abandoned manuscripts and visual aids are deductible as losses (under sec. 165).

In the same ruling, the Service states that it will not follow a district court decision which held that a taxpayer in the business of writing books could deduct travel expenses incurred while researching, writing and arranging material for the book.

House Bill. -- Under the House bill, taxpayers may treat their prepublication expenditures in the manner in which they have treated them consistently in the past until new regulations are issued by the Service with regard to these expenditures after the date of enactment of the bill.

New regulations will apply prospectively only, i.e., to taxable years beginning after their issuance.

The House bill provides that until the new regulations are issued, the Service must administer sections 162, 174 and 263 without regard to Rev. Rul. 73-395. The Service is to administer these sections in the same manner as they were applied consistently by the taxpayer prior to the issuance of Rev. Rul. 73-395. If a taxpayer followed no specific tax accounting method consistently, his returns are to be treated in accord with usual administrative procedures.

Committee Provision. -- The Committee agreed to extend the House provision to include prepublication expenditures of authors.

Deadwood Provisions

Present Law and House Bill. -- The "deadwood bill" reflects a series of changes which have been developed over a number of years as an attempt to simplify the tax laws by removing from the Internal Revenue Code those provisions which are no longer used in computing current taxes or are little used and of minor importance.

The "deadwood" bill has been introduced as Amendment No. 1322, adding a title II to H.R. 7727. This amendment was approved by the Finance Committee on December 18, 1975, as a Committee amendment to be offered on the floor of the Senate. In a slightly different form, these provisions also appear as Title XIX of H. R. 10612.

The deadwood bill would repeal almost 150 sections of the Internal Revenue Code; it would amend about 850 other sections. These provisions also contain approximately 2,370 amendments to the Code (including the repealed provisions and changes where one section of the Code would be amended several times).

The Committee agreed to the deadwood provisions in the House bill.

Refundable Investment Tax Credit

Present Law. -- The investment tax credit cannot annually exceed the first $25,000 of tax liability plus 50 percent of the tax liability in excess of $25,000. Investment credits which, because of this limitation, cannot be used may be carried back 3 taxable years and then carried forward 7 taxable years. (In the case of public utility property, the 50 percent limit is increased to 100 percent for 1975 and 1976, 90 percent for 1977, 80 percent for 1978, 70 percent for 1979 and 60 percent for 1980.)

Committee Amendment. -- The Committee agreed to provide that investment credits, which are earned with respect to property which becomes eligible for the credit on or after January 1, 1976, and which cannot be used during the normal 3-year carryback, 7-year carryforward period will be refundable at the expiration of the carryforward period. Thus, taxpayers who are unable to use eligible investment tax credits this year and over the next seven years will be entitled to a refund of such credits beginning in 1984.

Employee Stock Ownership Plans

On May 25, the Committee approved a number of provisions relating to ESOP's and electric utilities; on May 21, the Committee agreed to continue the investment tax credit without an expiration date at a 10 percent rate, with the 11 percent rate also continued where an amount equal to the additional one percent is contributed to an ESOP.

Today the Committee agreed to delete its earlier provisions relating to ESOP's and electric utilities and, instead, to allow a 12 percent investment tax credit where an amount equal to the additional two percentage points is contributed to an ESOP.

PRESS RELEASE

FOR IMMEDIATE RELEASE
May 27, 1976 - Part II

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

FINANCE COMMITTEE ACTS ON TAX REVISION ISSUES (H.R. 10612)

The Honorable Russell B. Long (D., La.), Chairman of the Senate Committee on Finance, announced that the Committee had approved the following changes and amendments to the House-passed tax revision bill (H.R. 10612).

Modifications of Previous Committee Action

Movie Shelters

On April 29, in the case of movies, the committee applied the "at risk" rule for purchases of completed films and productions of motion pictures.

In the case of productions of motion pictures, books, records, and similar property by a service company, the committee decided to require the service company to capitalize its costs of production.

Modification of previous committee decision.--Today the committee agreed to the following modification of its earlier decision:

1. Retain the "at risk" rule on the purchase of completed films as previously decided by the committee.

2. In the case of the production of motion pictures, etc.

(a) retain the capitalization requirement as previously provided,

(b) modify the "at risk" rule to make it inapplicable if the following conditions are met:

The investor's equity must be at least 25 percent of the film's total cost. (Thus, not more than 75 percent may be a nonrecourse loan.)

The unpaid balance of any nonrecourse loan, at the end of five years after the first showing of the film, would be required to be taken into income (i.e., recaptured) at that time.

A substantial portion of the film cost (e.g., 80 percent) is spent in the United States.

Declaratory Judgments as to Tax-Exempt Status as Charitable, etc., Organization

On May 26, the committee decided that the U. S. Tax Court and the U. S. District Court for the District of Columbia are to have jurisdiction in the case of an actual controversy involving a determination (or failure to make a determination) by the Internal Revenue Service with respect to the initial or continuing qualification or classification of an organization as an exempt charitable, etc., organization, as a qualified charitable donee, as a private foundation, or as a private operating foundation.

Today, the committee further decided that the U. S. Court of Claims is also to have jurisdiction over such a controversy.

Sports Franchises

The Committee agreed to modify its earlier decision (made on April 30) on recapture of depreciation on player contracts. This modification provides that the amount subject to recapture would be the greater of (1) the amount of depreciation taken on player contracts which were initially acquired with the original acquisition of the franchise by the seller or (2) the amount of depreciation taken on player contracts that are still owned by the seller at the time of sale.

Recyclable Wastepaper

On May 20, the committee previously agreed to allow a 10% tax credit on the purchase of recyclable wastepaper. The committee today agreed to set a maximum credit of $8 per ton and a minimum credit of $5.50 per ton. Both limits would be adjusted annually (after 1977) for changes in the consumer price index.

Recycling Tax Credit

The committee deleted a provision in the recycling tax credit, previously agreed to on May 20. The provision deleted would have required that the recycling tax credit be terminated when the depletion allowance for virgin materials (metals, etc.) and the capital gains treatment for timber and royalties from iron ore and coal were repealed.

Moving Expenses

The committee decided to amend its prior decision, made on May 21, pertaining to the ceiling on moving expenses on the sale or lease of a residence by increasing the maximum deduction for such expenses to $3,500. Originally, the committee had agreed to the $3,000 ceiling contained in section 506 of the House bill.

DISC

On May 19, the committee approved various changes in the tax treatment of Domestic International Sales Corporations (DISC). The committee agreed to modify its prior decision to extend the grace period from a two-year to a three-year period. Thus, the four-year base period for determining incremental DISC receipts would be the average receipts for any three of the four years 1973-1976, through 1979. Beginning in 1980, the four years used to determine base period receipts would be moved forward one year each year.

Carryforward of Expiring Investment Tax Credits

The Committee agreed to modify its earlier decision (made on May 21) allowing a two-year extension of the carryforward of certain investment tax credits which otherwise would expire in 1976 to include any foreign tax credits which otherwise would expire in 1976 in similar circumstances.

Tax Exempt Organizations

Private foundations - mandatory payout.--The Committee agreed to provide for a reduction in the mandatory payout percentage applicable to private foundations to 5% and to eliminate the authority of the Treasury Department to change that rate from year to year. The amendment will apply to taxable years beginning after December 31, 1975.

Charitable remainder trusts and wills.--The Committee agreed to extend the period during which charitable remainder trusts and wills containing such trusts could be amended to conform to the Tax Reform Act of 1969 and thus qualify for the estate tax charitable deduction. The amendment period was extended to December 31, 1977 and applies to wills and trusts executed on or before December 31, 1977. The Committee report will make it clear that this is the last such extension of the amendment period that the Committee proposes to grant.

Private foundation tax.--The Committee agreed to reduce from 4% to 2% the rate of tax on private foundation investment income.

Religious orders.--The Committee adopted an amendment relating to unrelated business income of religious orders. The order would be permitted to deduct amounts which would be fair compensation to their members, had they been lay persons. The compensation attributable to members of the order would be subject to income tax; however, because of personal exemptions, credits, and deductions (including the deduction for charitable contributions), there would probably be little or no tax.

Charitable payout rules.--The charitable payout rules for relatively new private foundations would be amended to permit a new foundation a relatively liberal use of the set-aside-rule. This allows a foundation to treat as a current charitable expenditure an amount set aside to be paid out over 5 years. After the first 5 years, the foundation must keep current on its charitable expenditure requirements.

Private foundations - transition rules.--The Committee agreed to an amendment to modify the transitional rules relating to the private foundation provisions enacted in the Tax Reform Act of 1969. Under this amendment, if a private foundation is leasing property to a "disqualified person" under existing transitional rules, the foundation may then sell the property to a disqualified person before January 1, 1978, if the foundation receives from the sale not less than the fair market value of the property.

Trade shows.--The Committee decided that charitable organizations are not subject to an unrelated business income tax on rental income from trade shows even though the exhibitors sell their products at the trade show.

Tax treatment of Fishermen's Organizations.--Under present law, agricultural organizations qualify as tax-exempt organizations under section 501(c)(5) of the Code. Fishermen's organizations may qualify as section 501(c)(6) business leagues. However, section 501(c)(5) organizations receive certain preferences, such as reduced postal rates. The Committee agreed to a provision expanding the definition of the word "agricultural" to include the harvesting of aquatic resources.

Tariff on imported Canadian crude oil

Canadian crude oil imported into the United States is subject to the imposition of a tariff. The Canadian Government has announced its intention to phase out exports of crude oil to the United States by 1983. The Federal Energy Administration and refiners located along the northern tier of the United States are attempting to ease this situation. One method presently in use is to provide for an exchange of crude oil where the geographic movement of oil is burdensome and costly. Under such an arrangement the U.S. refiners and Canadian companies exchange equivalent quantities of domestic crude oil for Canadian crude oil. This permits the same quantity of oil to be retained in each country, but eliminates the costly transportation of such oil where convenient exchanges of oil can be made.

The Committee agreed to eliminate the tariff imposed on imported Canadian crude oil when exchanged for an equivalent amount of domestic crude oil of the same kind and quality.

Production-Sharing Contracts

The Committee agreed to provide a foreign tax credit for production-sharing contracts in which the IRS has ruled that no foreign taxes are paid. The proposal would provide that in the case of a production-sharing contract there will be treated as taxes paid on the oil extraction income an amount equal to 48 percent of the foreign extraction income from that contract.

This credit will only apply to the extent that there are no excess creditable foreign taxes from other extraction operations (the intent is to grant relief, in effect, only to the smaller companies who have no extra credits to shelter this income).

This credit will only apply to existing production-sharing contracts in a defined area and will only apply for a 5-year period (this will enable the contracts to be renegotiated without any undue pressure being placed upon contractors).

Retail outlets for oil or gas products; transfers of oil or gas properties; computation of taxable income limitation for trusts with oil or gas-related income

Present law. -- In the Tax Reduction Act of 1975, percentage depletion for oil and gas was repealed except for small producers. This exemption was made inapplicable to any producer owning or controlling a retail outlet for the sale of oil or natural gas or petroleum products. In addition, the small producer exemption contains specific rules for the allocation of the depletion allowance among a controlled group of corporations, trusts and estates owned by the same or related persons and among the taxpayer, spouse, and minor children. In addition, the deduction resulting from the small producer exemption cannot exceed 65 percent of the taxpayer's net income from all sources.

Committee amendments. -- In order to deal with the *de minimis* problem in connection with the retailer rule, the Committee provided that any person whose retail outlets did not have retail sales or oil or gas products in excess of $5 million a year would not be treated as a retailer for that year.

In addition, the Committee provided that large bulk sales of oil or natural gas products to commercial or industrial users would not be treated as retail sales.

The Committee agreed that a producer would not be considered a retailer if (a) the producer made no retail sales of oil or gas products in the United States, and (b) none of the producer's domestic production of oil or natural gas is exported.

The Committee agreed that for purposes of computing the 65 percent of taxable income limitation on the percentage depletion deduction in the case of a trust, the limitation is to be computed prior to taking into account the deduction for distributions from the trust.

The Committee agreed that for purposes of the rules disallowing percentage depletion for property which is transferred from one person to another, property owned by a trust, the beneficiaries of which are changed by reason of the death, birth or adoption of any beneficiaries which are lineal descendants of the same family, shall not be considered to constitute a transfer.

Oil and Gas Foreign Extraction Taxes

The Committee agreed to an amendment under which the rules denying creditability for foreign taxes where there is no economic interest in the oil or gas by the taxpayer are not to apply for a period of 10 years to any oil or gas field in which the taxpayer in the past has had an economic interest.

Reorganizations involving Foreign Corporations

The Committee agreed to an amendment that notwithstanding any court case or period of limitation, any double taxation which arose by reason of the liquidation of a foreign subsidiary into its U.S. parent is to be eliminated by adjusting earnings and profits and reducing the basis of assets distributed at time of liquidation according to regulations to be promulgated by the Secretary of the Treasury.

Western Hemisphere Trade Corporations

The Committee agreed that in a consolidated return a WHTC and a nonWHTC, each of which derives substantially all of its income within the same country, would be permitted to average their foreign taxes and foreign source income under the overall limitation, although the general consolidated return rules prohibit averaging of a WHTC with a nonWHTC except in the case of a public utility.

Pollution Control Equipment

New pollution control equipment installed in existing facilities would be eligible for five-year rapid amortization and two-thirds of the 10 percent investment tax credit. Only two-thids of the investment tax credit is available under present law for equipment depreciated over 5 or 6 years.

Railroad Provisions--Investment Tax Credit

The 50-percent limitation on the investment credit would be increased temporarily to 100 percent of tax liability for a brief period (2 years, for example) and phased down to the 50-percent limitation over a 5-year period by 10 percentage points a year. This is the same as the provision enacted in the Tax Reduction Act of 1975 for electric utilities.

Simultaneous Liquidation of Parent and Subsidiary

Under present law, a controlled subsidiary corporation which sells its assets and completely liquidates is taxable on the sale proceeds. The committee agreed to an amendment which would permit such sales to be made without tax, provided that the parent corporation also completely liquidates in the same transaction (so that the parent's shareholders will in effect be taxable on the sale proceeds).

Subchapter S Corporations

The Committee agreed to an amendment to increase the maximum number of shareholders permitted in an electing small business (subchapter S corporation) from 10 to 15 shareholders. The 15 shareholder limit is to apply after the corporation has been an electing subchapter S corporation for 5 years. However, the increased limit could apply sooner if the additional shareholders acquired their shares by inheritance. Where a husband and wife are treated as one shareholder for purposes of the shareholder limitation, then the surviving spouse and the decedent's estate are also to be treated as one shareholder.

Face Amount Certificates

A face amount certificate is an installment investment contract which, on maturity, entitles the holder to receive the face amount of the security (which equals the cumulative installments plus interest). Under pending Treasury regulations, holders of these bonds are taxed on interest income as it accrues each year over the life of the bond, although the interest is not paid until redemption or under an annuity-type arrangement.

The Committee agreed to an amendment providing that face-amount certificates are to be taxed under section 72. As a result, the amount of discount attributable to a face-amount certificate would not be ratably included in the gross income of the holder over the term of the certificate. Instead, the amount of discount would be included in the gross income of the holder upon actual receipt by him either at maturity or upon a premature cancellation. If the holder exercises an option to take annual payments from the corporation in lieu of a lump sum at maturity, the payments will be taxed like annuities are presently taxed under section 72, i.e., a portion of each payment received would be included in gross income and the portion attributable to the consideration furnished would be excluded.

The corporation issuing the certificate would be entitled to an interest deduction in each taxable year equal to the amount of discount accuring within that taxable year.

Personal Holding Company Income

Under present law, amounts which a corporation receives for renting tangible corporate property to a 25 percent or larger shareholder are treated as personal holding company income, but only if the corporation has a sizeable amount of other passive income. On the other hand, the Internal Revenue Service treats amounts which a corporation receives for leasing intangible property (such as a license to use a secret process or trade brand) to such a shareholder as ordinary royalty income. The Committee agreed to an amendment which would treat amounts received under a lease of intangible property to a shareholder under the same rule that now applies to a lease of tangible property to a shareholder.

Franchise Transfers

The Committee agreed to provide that the rules relating to ordinary income treatment on certain transfers of franchises or franchise rights would apply to transfers of franchise rights to a partnership followed by a sale of the franchisor's rights in the partnership to the franchisee. The Committee also agreed that neither these new partnership rules nor the regular rules (sec. 1253) relating to transfers of franchises would apply to transfers of a professional practice if the contract was in existence prior to January 1, 1970, and the transferor is an employee or partner of the transferee.

Light-Duty Truck Parts

The Committee agreed to repeal the 8 percent excise tax on light-duty truck parts sold in connection with (and at the time of) the original purchase of the tax-exempt light-duty truck (10,000 lbs. or less). This would cover, for example, the purchase of a heavy-duty bumper from a dealer where the bumper is added at the time of original sale rather than added by the truck manufacturer (as the part would be exempt from tax by virtue of being included on the truck by the manufacturer).

Employment Taxes of Sternmen

The Committee agreed to make certain fisherman and lobster boat sternmen (whom the Internal Revenue Service usually considers regular employees) self-employed for purposes of income tax withholding, the self-employment tax, and the social security (FICA) tax. These individuals are to be considered self-employed if their remuneration is only a share of the catch--but only if, in addition, their services are on a "substantially intermittent basis." In addition, the boat's crew must normally be made up of fewer than six individuals. Amendments would also be made to the definitions of "employment" and "trade or business" in the parallel social security laws.

Tip Income

The Committee agreed to an amendment to make clear that employers would only be required to report tips which are reported to them by employees under sec. 6053 of the Internal Revenue Code.

Consolidated Income Tax Returns

The Committee agreed to allow life insurance companies (both stock and mutual), on an elective basis, to file consolidated income tax returns with their property-casualty insurance and other corporate affiliates, effective beginning January 1, 1978. Under certain circumstances the amendment would limit the amount of loss offset privileges (in any one year) with respect to net non-life losses. Any net non-life loss not allowed as an offset in one year would be available as a carryback or carryforward.

Normal Tax of Mutual Property-Casualty Insurance Companies

The Committee agreed to correct an inadvertent omission in the Tax Reduction Act of 1975. Although that Act reduced the normal tax paid by most corporations from 22 percent to 20 percent of the first $25,000 of taxable income, it did not reduce the normal tax of mutual property-casualty companies. Under the amendment agreed to by the Committee, the normal tax of these companies would be conformed to the normal tax paid by other corporations.

Insurance Company Deductions for Nonparticipating Policies

The Committee agreed to an amendment of the rules under which a life insurance company computes deductions with respect to nonparticipating policies. Under present law, the deductions are allowed with respect to nonparticipating policies which are issued or renewed for periods of 5 or more years. Under the Committee amendment, for purposes of the 5-year rule, the period for which a policy is issued or renewed includes the period for which it is guaranteed renewable.

Inadvertent distributions by life insurance companies

The Committee agreed not to impose income tax on income of a life insurance company where the tax would be deferred but for an inadvertent distribution of the income to the shareholders of the company. The Committee decided to permit the continued deferral of tax only if the amount distributed to the shareholders is repaid to the company before the time for filing the company's tax return for the year of the distribution. Under the amendment, a shareholder's tax basis for computing gain or loss with respect to his stock in the company would not be affected by the distribution or repayment to the extent a dividend deduction or exclusion is allowed with respect to the distribution.

Tax Incentive for the Removal of Architectural and Transportation Barriers

The Committee agreed to allow businesses or individuals to deduct in the year incurred the full cost of removing architectural and transportation barriers in order to make facilities more accessible to handicapped and elderly persons. The deduction, which would be limited to $25,000 per year, would be allowed to a taxpayer for facilities he owns or leases in connection with his trade or business.

Poultry Operations of Farming Syndicates

The Committee agreed to provide that farming syndicates would be required to capitalize the cost of poultry and to deduct such costs only over the lesser of their useful life or 12 months.

State taxation of barges moving on inland waterways

The Committee agreed to a provision prohibiting State and local governments from imposing property taxes on barges and other vessels which are not based within their jurisdiction; but which occasionally travel on their inland waters.

Federal collection of State income taxes

The Committee agreed to a series of amendments to the provisions authorizing Federal collection of State individual income taxes (the so-called "piggyback" collection rules). The amendments would: (1) permit the piggyback rules to go into effect if any one State elects to have them apply to its tax; (2) permit a piggybacking State to allow its taxpayers an income tax credit on account of the State's sales tax; and (3) make explicit Congress' intent that the Federal government not charge any State for administration of its income taxes under the piggyback provisions.

Welfare Recipient Employment Credit

The Committee approved an amendment (a) modifying the Work Incentive Program (WIN) tax credit provisions making the WIN tax credit available to the employer from the date of hiring, but only if the employment is not terminated by the employer without cause before the end of 90 days; (b) adding an additional exception to the recoupment provision of the credit to provide that there would be no penalty if the employee is laid off due to lack of business; and (c) doubling the dollar amount which any single employer can claim against his tax liability (now $25,000 plus one-half of the amount over $25,000). The amendment also modified the Federal recipient employment incentive tax credit provisions by (a) extending the expiration date of the credit to January 1, 1981; (b) placing a limit of 12 months for which the tax credit could be claimed for any one employee; and (c) authorizing WIN to also certify for the welfare recipient tax credit.

Application of Minimum Tax to Interest Paid on Loans for Existing Low and Moderate Income Housing

The tax preference item in the minimum tax base is not to include investment interest or construction interest in the case of already existing contracts which are attributable to low or moderate income housing.

Relief of Tax Liability for Certain Innocent Spouses

The Committee amended a provision of the Code which allows an innocent spouse who is unaware that a substantial amount was omitted from income on a joint return to seek a redetermination of his or her individual liability and thereby avoid liability on the omitted income, except where the year was closed by the statute of limitations, res judicata, or otherwise. The Committee amendment allows taxpayers who qualify as innocent spouses to seek redetermination of their liability for years (ending after 1960) which were closed because of a court decision which was rendered before the 1971 enactment of the "innocent spouse" provision.

Student Loan Forgiveness

The Committee decided to extend through December 31, 1978, the exclusion from income of all or part of student loan indebtedness which is forgiven on student loans when the student, as part of the loan agreement, works for a certain period of time in certain professions or certain geographical areas or for certain classes of employers.

Tax Court Amendments

The Committee agreed to a series of amendments relating to the U. S. Tax Court which would:

1. permit a judge to continue in office up to 90 days after the expiration of his term.

2. provide full retirement for a judge who has attained age 65 and who has at least 12 years' service as a judge and not less than a total of 35 years' service in the Federal Government.

3. permit Tax Court judges to sit at such times and places as the Chief Judge may direct.

4. permit the Tax Court to waive the $10 filing fee where the taxpayer cannot pay the fee.

5. allow commissioners of the Tax Court to administer oaths, issue subpoenas, and would allow the Tax Court to designate a Chief Commissioner.

6. authorize commissioners to make reports and enter decisions with respect to small tax cases in such manner as the court may provide by rule.

7. increase the jurisdiction of disputes to be heard by commissioners from $1,500 to $2,500.

8. permit the Tax Court to extend for a period of 30 days, the 90 or 150 day period in which to file a petition in the Tax Court where reasonable cause is shown for the delay in mailing the petition.

9. provide that if a Tax Court judge does not become eligible to receive a Tax Court pension, then that judge would be permitted to recognize his Government service for Civil Service retirement purposes.

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