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SECTION-BY-SECTION SUMMARY

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Revenue Act of 1978 (P.L. 95–600; H.R. 13511)

Energy Tax Act of 1978 (P.L. 95–618; H.R. 5263)

Foreign Earned Income Act of 1978 (P.L. 95–615; H.R. 9251)

Fringe Benefits Act (P.L. 95–427; H.R. 12841)

PREPARED FOR THE USE OF THE

COMMITTEE ON WAYS AND MEANS
U.S. HOUSE OF REPRESENTATIVES

AND THE

COMMITTEE ON FINANCE
U.S. SENATE

BY THE STAFF OF THE

JOINT COMMITTEE ON TAXATION

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PREFACE

This pamphlet provides a section-by-section summary of the provisions of the following tax legislation:

(1) Revenue Act of 1978 (Public Law 95–600; H.R. 13511);
(2) Energy Tax Act of 1978 (Public Law 95–618; H.R. 5263);
(3) Foreign Earned Income Act of 1978 (Public Law 95–615; H.R. 9251); and
(4) Fringe Benefits Act (Public Law 95–427; H.R. 12841).

In addition, Appendix I gives the revenue effects of the Revenue Act of 1978 by provision, with separate tables for calendar year liabilities for 1979–1983 and for fiscal year receipts for 1979–1983. Appendix I also includes tables on the distribution of the individual income tax provisions by income levels. Appendix II shows the new individual income tax rate schedules, and Appendix III gives the revenue effects for fiscal years 1979–1983 of the provisions of the Energy Tax Act of 1978.

In view of the significant revisions of the Internal Revenue Code included in these Acts, the limitations of attempting to describe such revisions in a summary should be kept in mind. The official reports of the respective conference, House and Senate committees are the ultimate legislative and interpretative authorities with respect to these Acts.

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SUMMARY OF REVENUE ACT OF 1978

Sec. 3. Policy With Respect to Additional Tax Reductions

The Act provides that as a matter of national policy the rate of growth in Federal outlays, adjusted for inflation, should not exceed one percent per year between fiscal year 1979 and fiscal year 1983; Federal outlays as a percentage of gross national product should decline to below 21 percent in fiscal year 1980, 20.5 percent in fiscal year 1981, 20 percent in fiscal year 1982, and 19.5 percent in fiscal year 1983; and the Federal budget should be balanced in fiscal years 1982 and 1983. If these conditions are met, it is the intention that the tax-writing committees of Congress will report legislation providing significant tax reductions for individuals to the extent that these tax reductions are justified in the light of prevailing and expected economic conditions.

TITLE I—INDIVIDUAL INCOME TAX PROVISIONS

A. INDIVIDUAL TAX REDUCTIONS AND EXTENSIONS

Secs. 101 and 106. Widening Tax Brackets, Rate Cuts, and Increase in Zero Bracket Amount

Under present law, there is no tax on the initial tax bracket, called the zero bracket amount, which is also a floor under itemized deductions. (The zero bracket amount was formerly referred to as the standard deduction.) Under prior law, the zero bracket amount was $3,200 for married couples filing joint returns and $2,200 for single persons. Above the zero bracket amount, tax rates range from 14 percent to 70 percent, and under prior law there were 25 tax rate brackets for joint returns. There are different rate schedules for married couples filing joint returns, single persons, single heads of households, married persons filing separate returns, and for estates and trusts.

Widening of tax brackets.—The Act provides a new tax rate schedule with 15 instead of 25 tax brackets for married individuals filing jointly and 16 brackets for single individuals. The tax rate brackets, particularly the top brackets, are widened considerably.

Reduction in certain tax rates.—The Act reduces most tax rates in the lower brackets and increases some tax rates in the higher tax brackets.

Increase in zero bracket amount.—The Act increases the zero bracket amount from $3,200 to $3,400 for joint returns, and from $2,200 to $2,300 for single persons and heads of households. For married persons filing separate returns, the increase is from $1,600 to $1,700.

Effective date.—These changes are effective for taxable years beginning after December 31, 1978.

Fiscal year taxpayers.—The Act provides (sec. 106) that the changes in the zero bracket amount, the tax rate changes, and the increase in the personal exemption are to be prorated for fiscal year taxpayers under section 21 of the Code.[1] This means that a fiscal year taxpayer will receive these tax reductions with respect to that part of his or her 1978–79 fiscal year which falls in 1979.

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[1] The expiration of section 42 of the Code, the general tax credit, and section 301 of the Act relating to corporate rate reduction are also treated as a change in the rate of tax for this purpose. No other changes are to be so treated.

Sec. 102. Increase in the Personal Exemption

Under prior law, the amount of the personal exemption was $750 for the taxpayer, his or her spouse, and each dependent whose gross income was less than $750 (unless the dependent is the taxpayer's child and is either under age 19 or a student). An additional exemption is provided for a taxpayer who is blind or age 65 or over. Prior law also provided a general tax credit, which was the larger of $35 per exemption or 2 percent of the first $9,000 of taxable income (in excess of the zero bracket amount), with a maximum credit of $180. The credit was scheduled to expire at the end of 1978.

The Act provides a permanent increase in the personal exemption from $750 to $1,000, and increases the gross income limit for a dependent from $750 to $1,000. The general tax credit is allowed to expire at the end of 1978.

The increase in the personal exemption is effective for taxable years beginning after December 31, 1978.

Secs. 101 and 102. Changes in Filing Requirements and Withholding Changes

Under prior law, an income tax return had to be filed by a single person and a head of household if his or her gross income was $2,950 or more for a taxable year, by a married couple under age 65 filing a joint return if their income was $4,700 or more, and by a married couple where both are age 65 or over if their income was $6,200 or more. The Act increases the filing levels for a single person and a head of household to $3,300 and increases it to $5,400 for a married couple where both are under age 65, and to $7,400 for a married couple where both are age 65 or over.

The requirement for withholding of tax from wages paid by an employer reflected the prior law tax rates, the zero bracket amount, and the amount of the personal exemption. The Act provides that the withholding rates and tables are to be changed by the Secretary of the Treasury to reflect the increase in the zero bracket amount, the personal exemption, and the new tax rates.

Two technical changes are also made. The section relating to withholding allowances based on itemized deductions (sec. 3402(m)) is changed to reflect the higher zero bracket amount and the higher personal exemption. Also, the income averaging pre-1977 base period adjustment is retained at $3,200 for joint returns and $2,200 for single persons rather than being increased to reflect the higher zero bracket amount for 1979 and later years.

The changes in the filing requirements are effective for taxable years beginning after December 31, 1978, and the withholding changes apply to wages paid after December 31, 1978.

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Sec. 103. Earned Income Credit Made Permanent

Under prior law, the earned income credit was due to expire on January 1, 1979. The Act makes the earned income credit permanent.

Sec. 104. Increase in and Simplification of the Earned Income Credit

Under prior law, an eligible individual was allowed a credit against tax equal to 10 percent of the first $4,000 of earned income (for a maximum credit of $400). The amount of the credit was phased out as the adjusted gross income (or earned income, if greater) of an individual increased from $4,000 to $8,000. Under this phase-out, one dollar of credit was lost for each $10 of income in excess of $4,000, regardless of whether the individual had at least $4,000 of earned income. An individual was eligible for the earned income tax credit only if that individual maintained a household in the United States for himself or herself and for one or more children who were under the age of 19, were students, or were disabled dependents. Further, earned income was eligible for the credit only if it was includible in the gross income of the taxpayer during the taxable year in which the credit was claimed.

The Act makes three changes which simplify the computation of, and determination of eligibility for, the credit. First, the Act provides that, effective for taxable years beginning after December 31, 1978, an eligible individual is allowed a credit against tax equal to 10 percent of the first $5,000 of earned income (for a maximum credit of $500). The allowable credit will be limited to the excess of $500 over 12.5 percent of the excess of adjusted gross income (or earned income, if greater) over $6,000. The credit is zero for taxpayers with incomes over $10,000. Thus, for each $10 of income in excess of $6,000, $1.25 of credit will be lost. In addition, the Act provides that the amount of credit allowed is to be determined under tables prescribed by the Secretary of the Treasury.

Second, the Act repeals the provision that earned income eligible for the credit does not include any items which are excluded from adjusted gross income. (Thus, excludible items such as excluded disability income and the rental value of a parsonage need not be subtracted in determining earned income eligible for the credit.)

Third, the Act also changes eligibility requirements for the credit so that individuals who are eligible for the credit can be identified from entries on the individual income tax return (Form 1040) after a slight modification in the form to identify heads of household who maintain a household for a child. These changes will allow the Internal Revenue Service to give the credit to taxpayers who are eligible for the credit but who neglect to claim it. Any individual who is considered to be married and who is entitled to a dependency exemption for a child, any surviving spouse, and any head of a household who maintains a household for a child generally will be eligible for the earned income credit if the taxpayer and child reside in the United States.

Sec. 105. Advance Payments of Earned Income Credit

Prior law contained no special provision for advance payments of the earned income credit. Thus, most eligible taxpayers did not benefit from the credit until after their income tax returns were filed. Also, under prior law, the earned income credit could not be taken into account for purposes of determining eligibility for, or the amount of, benefits or assistance under any Federal program or State or local program financed in whole or in part with Federal funds.

The Act provides that an eligible individual may elect to receive advance payment of the earned income credit from his or her employer. Any individual who receives advance payments during a calendar year would be liable for a tax equal to the excess of such payments over the actual amount of the credit determined on his or her annual tax return. Conversely, individuals whose advance payments are less than the actual amount of the credit will be allowed a credit or refund equal to the excess of the actual credit over the advance payments.

An employee who believes that he or she is eligible for the credit may claim advance payments by providing the employer with a certificate on which the employee certifies that he or she expects to be eligible for the credit and that he or she does not have a certificate in effect with another employer, and on which the employee states whether his or her spouse has a certificate in effect. For an employee with a certificate in effect, the employer is to add the advance payment to the employee's paycheck. The amount of advance payment is to be determined from tables which take into account the amount of wages paid and whether an employee's spouse also is claiming advance payments. Employers would reduce their liability for income tax withholding and FICA taxes by the aggregate amount of advance payments. Employers would reduce their liability for income tax withholding and FICA taxes for the aggregate amount of advance payments made to employees in any pay period.

In addition, the Act terminates the provision requiring that the credit not be taken into account for purposes of Federal or Federally aided assistance programs, effective January 1, 1980.

B. ITEMIZED DEDUCTIONS; UNEMPLOYMENT COMPENSATION; CREDITS

Sec. 111. Repeal of Nonbusiness Deduction for State and Local Taxes on Gasoline and Other Motor Fuels

Under prior law, an individual who itemized deductions could deduct State and local taxes imposed on gasoline, diesel, and other motor fuels not used in business or investment activities. For example, taxes on gasoline consumed in personal use of a family car were deductible by an individual itemizing deductions.

The Act repeals the itemized deduction for State and local taxes on gasoline, diesel, and other motor fuels not used by the taxpayer in business or investment activities. The repeal of the deduction is effective for taxable years beginning after December 31, 1978.

Sec. 112. Taxation of Unemployment Compensation Benefits at Certain Income Levels

Under prior law, there was no express exclusion from gross income for amounts received under unemployment compensation programs. However, unemployment compensation paid under most government programs was exempt from taxation under a series of Internal Revenue Service rulings beginning in the 1930s.

The Act provides that unemployment compensation paid pursuant to government programs generally must be included in taxable income for higher income taxpayers. Effective for taxable years beginning after December 31, 1978, the amount of unemployment compensation included generally is an amount equal to one-half of the excess of income (including unemployment compensation and excludable disability income) over $20,000 for single taxpayers, over $25,000 for married taxpayers filing jointly, and over zero for married taxpayers filing separately. For example, a married taxpayer who files a joint return and has income of $30,000 (including $5,000 of unemployment compensation) would include $2,500 of unemployment compensation. in adjusted gross income (which is one-half of the unemployment compensation taken into account as an amount over $25,000).

In addition, the Act requires any person who makes unemployment compensation payments of $10 or more to any individual during any calendar year to provide the Secretary of the Treasury with a return setting forth the amount of such payments and the names and addresses of the individuals to whom paid. Also, any individual who has received unemployment compensation payments (aggregating $10 or more) must be furnished with a written statement setting forth the name and address of the person who made the payments and the amount of the payments.

Sec. 113. Political Contributions

Under prior law, an individual who itemized deductions could deduct certain political or newsletter fund contributions of up to $100 per year ($200 in the case of a joint return). Alternatively, an individual could elect an income tax credit equal to one-half of the political and newsletter fund contributions, but not more than $25 ($50 in the case of a joint return).

The Act repeals the political contributions deduction, and increases the maximum amount of the income tax credit from $25 to $50 (from $50 to $100 in the case of a joint return). These changes are effective for taxable years beginning after December 31, 1978.

Sec. 121. Child Care Credit for Payments to Related Individuals

Under prior law, payments for child care services by a taxpayer to certain relatives qualified for the child care credit only if the services constituted "employment," as defined for Social Security purposes. Under the Social Security definition, child care services rendered by a grandparent generally do not constitute employment.

The Act provides generally that payments to grandparents for care of their grandchildren may qualify for the child care credit. This provision is effective for taxable years beginning after December 31, 1978.

C. DEFERRED COMPENSATION PROVISIONS

Sec. 131. State and Local Government Deferred Compensation Plans

Under present law, a cash method taxpayer generally is not required to include compensation in income until it is actually received or otherwise made available. This rule applies even if the taxpayer enters into an agreement with a payor to receive compensation on a deferred basis, rather than currently, so long as the agreement is made before the taxpayer obtains an unqualified and unconditional right to the compensation.

On February 3, 1978, the Internal Revenue Service issued proposed regulations which would have changed the tax treatment of participants in certain plans of deferred compensation. The proposed regulations provided generally that, if payment of an amount of a taxpayer's fixed, basic, or regular compensation is deferred at the taxpayer's individual election to a taxable year later than that in which the amount would have been payable but for the election, the deferred amount would be treated as received in the earlier taxable year.

Under the Act, amounts of compensation deferred by a participant in an eligible deferred compensation plan maintained by a State or local government unit or a tax-exempt rural electric cooperative (and certain tax-exempt affiliates), plus any income attributable to the investment of such deferred amounts, will be includible in the income of the participant or his beneficiary only when such amounts are actually paid or otherwise made available.

To qualify as an eligible deferred compensation plan, the plan must not allow the deferral of more than $7,500, or 33⅓ perecnt of the participant's includible compensation for the taxable year, whichever is less. In addition, the plan must satisfy other requirements relating to (1) the timing of an election to defer compensation (the plan must not permit deferral for a calendar month unless an agreement has been entered into before the beginning of such month), (2) the timing of distributions under the plan (deferred compensation cannot be made available to participants before separation from service with the sponsoring entity or the occurrence of an unforseeable emergency, whichever is earlier), and (3) the ownership of investments made with deferred amounts (all amounts of compensation deferred under the plan, all property purchased with amounts deferred, and any earnings on such property must be assets of the plan sponsor subject to the claims of its general creditors). Under the Act, a plan can provide an increased limitation in the 3 years before a participant retires.

All plans to which the Act applies will have until January 1, 1982, to satisfy the plan requirements for classification as an eligible State or local government deferred compensation plan. However, the limitations on amounts which can be deferred under such a plan will apply for all taxable years beginning after December 31, 1978.

Sec. 132. Certain Private Deferred Compensation Plans

The present law treatment of participants in unfunded deferred compensation arrangements maintained by taxable entities is the same as the tax treatment of participants in such arrangements maintained by State and local government units.

The Act provides that the taxable year for including compensation deferred under a deferred compensation plan maintained by a taxable entity is to be determined in accordance with the principles set forth in regulations, rulings, and judicial decisions relating to deferred compensation which were in effect on February 1, 1978. Thus, the proposed regulations of February 3, 1978, are not to be applied to participants in unfunded deferred compensation plans maintained by taxable entities.

Sec. 133. Deferred Compensation Payments to Independent Contractors

Under present law, an employer generally is permitted a deduction for deferred compensation provided under a nonqualified plan in the year that the compensation is includible in the employee's gross income, even though the employer is on the accrual basis of accounting and normally would be entitled to a current deduction for the year in which the liability is accrued. However, this rule applies only where there is an employer-employee relationship. Thus, an accrual basis taxpayer generally is able to establish an unfunded deferred compensation plan for a cash basis independent contractor and obtain a deduction for the liability in accordance with the usual accrual accounting rules.

The Act provides that, effective for taxable years beginning after December 31, 1978, no deduction is allowed for deferred compensation provided under a nonqualified plan to nonemployee participants until that compensation is includible in gross income by the participants.

The Act also clarifies current law by providing that a method of compensation or employer contributions having the effect of a plan deferring the receipt of compensation does not have to be similar to a stock bonus, pension, profit-sharing, or annuity plan to be subject to the deferred compensation deduction-timing rules.

Sec. 134. Tax Treatment of Cafeteria Plans

Under a "cafeteria" or "flexible benefit" plan, an employee may choose from a package of employer-provided fringe benefits, some of which may be taxable and some of which may be nontaxable. Under a provision of the Employee Retirement Income Security Act of 1974 (ERISA), an employer contribution made before January 1, 1977, to a cafeteria plan in existence on June 27, 1974, was required to be included in an employee's gross income only to the extent that the employee actually elected taxable benefits. In the case of a plan not in existence on June 27, 1974, the employer contribution was required to be included in income to the extent the employee could have elected taxable benefits. Under the Tax Reform Act of 1976, these rules applied with respect to employer contributions made before January 1, 1978.

The Act provides that employer contributions under a written cafeteria plan generally are excluded from the employee's gross income to the extent that nontaxable benefits are elected. However, in the case of a highly compensated employee, amounts contributed under a cafeteria plan will be included in gross income, for the taxable year in which the plan year ends, to the extent the individual could have elected taxable benefits unless the plan meets nondiscrimination standards with respect to plan coverage and eligibility and with respect to contributions or benefits. The Act applies to taxable years beginning after December 31, 1978.

Sec. 135. Certain Cash or Deferred Arrangements

Under present law, the tax treatment of amounts contributed by an employer, at the election of an employee, to a qualified cash or deferred profit-sharing plan depends upon when the plan was established. (In general, under a cash or deferred profit-sharing plan, the employer gives an employee the choice of (1) being paid a specified amount in cash as current compensation, or (2) having that amount contributed to the plan.) Under a provision of the Employee Retirement Income Security Act of 1974 (ERISA), as amended by the Tax Reform Act of 1976, the tax treatment of contributions to qualified cash or deferred profit-sharing plans in existence on June 27, 1974, was governed (until January 1, 1978) under the law as it was applied prior to 1972. (Under the rules then in effect, an employee generally was not taxed currently on amounts he chose to have contributed to the plan.) In the case of plans not in existence on June 27, 1974, employer contributions were taxable to the employees.

Under the Act, a participant in a qualified cash or deferred profit-sharing arrangement will not have to include in income any employer contribution to the plan merely because he could have elected to receive the amount in cash instead. For the cash or deferred arrangement to be a tax-qualified plan, it must satisfy the usual pension plan qualification rules. In addition, it must not permit the distribution of amounts attributable to employer contributions merely because of the completion of a stated period of plan participation or the passage of a fixed period of time, and all amounts contributed by the employer pursuant to an employee's election must be nonforfeitable at all times. Under the Act, special nondiscrimination rules are provided for these arrangements to test for discrimination as to actual plan participation or as to the amount of contributions to the plan.

The Act applies to taxable years beginning after December 31, 1979. However, a transitional rule is provided for those cash or deferred arrangements in existence on June 27, 1974, under which their qualified status for plan years beginning before January 1, 1980, will be determined under the law with respect to cash or deferred arrangements as it was administered before January 1, 1972.

D. EMPLOYEE STOCK OWNERSHIP PLANS

Sec. 141. Employee Stock Ownership Plans

Under prior law, the term "employee stock ownership plan" was used to describe a type of defined contribution plan under which a contributing employer could receive an additional investment tax credit. This type of plan was commonly referred to as a TRASOP (Tax Reduction Act Stock Ownership Plan) or investment tax credit ESOP. The term "employee stock ownership plan" was also used under prior law to describe a type of defined contribution plan which was exempt from certain of the prohibited self-dealing rules. This type of plan was commonly referred to as an ESOP or leveraged ESOP.

Under the Act, the type of plan previously referred to as a TRASOP or investment tax credit ESOP is designated as an ESOP, and the type of plan previously referred to as an ESOP or leveraged ESOP is designated as a leveraged employee stock ownership plan. However, for purposes of this summary, the terminology of prior law is used to avoid confusion. Thus, the summary uses the terms TRASOP and leveraged ESOP to describe the two types of plans.

(a) Expiration date of TRASOP provisions

Under prior law, the TRASOP (Tax Reduction Act Stock Ownership Plan) provisions were scheduled to expire on December 31, 1980.

The Act makes the TRASOP provisions, as amended, part of the Code for the first time and extends the expiration date of the provisions for three years until December 31, 1983.

(b) Qualification requirements for TRASOPs

Under prior law, a TRASOP was not required to be a tax-qualified plan. A TRASOP which was not tax-qualified, however, was required to satisfy certain of the special rules applicable to tax-qualified plans.

The Act requires all TRASOPs to be tax-qualified plans.

(c) Date by which a TRASOP must be established for a taxable year

Under prior law, a TRASOP had to be established by the close of an employer's taxable year to be treated as tax-qualified for the year.

The Act provides that a TRASOP may be treated as tax-qualified from its effective date even though the TRASOP is not actually established until the date for filing the employer's tax return for the taxable year (including extensions) in which the effective date falls.

(d) Allocation of TRASOP contributions

Under prior law, an employee who participated in a TRASOP at any time during a year for which an employer contribution was made was entitled to an allocation of the contribution.

Under the Act, employer contributions to a TRASOP for a plan year generally are to be allocated in accordance with the rules governing the allocation of contributions to tax-qualified plans. The Act re-

tains the present law requirement that the allocation of employer contributions to a TRASOP for a year must be made in proportion to the total compensation of all participants sharing in the allocation for the plan year, taking into account only the first $100,000 of compensation for an employee.

(e) Provisions relating to voting of employer securities held by leveraged ESOPs and TRASOPs

Under prior law, a plan participant was required to be entitled to direct the voting of all employer stock allocated to the participant's account under a TRASOP.

The Act provides that if a leveraged ESOP (Employee Stock Ownership Plan) or a TRASOP holds employer stock issued by a corporation whose stock is "publicly traded," the plan must provide that the stock is to be voted by the plan participants. The Act also provides that a leveraged ESOP or a TRASOP which holds employer stock issued by a corporation which is not publicly traded must provide that the plan participants are entitled to exercise voting rights with respect to the stock on any corporate issue which must by law (or charter) be decided by more than a majority vote of outstanding common shares on the issue.

(f) Definition of employer securities for leveraged ESOPs and TRASOPs

Under prior law, the securities contributed to (or purchased by) a TRASOP were required to be common stock with voting and dividend rights no less favorable than the voting power and dividend rights of other common stock of the issuing corporation. Securities convertible into such common stock were also acceptable.

The Act provides that, in the case of a TRASOP, the only types of employer securities which may be acquired and held by the plan are common stock of the issuing corporation and preferred stock of the issuing corporation which is readily convertible into its common stock. Unless the stock is readily tradable on an established securities market, it must have a combination of voting rights equivalent to rights possessed by shareholders of the class of common stock of the issuing corporation having the greatest voting rights and dividend rights equivalent to rights possessed by shareholders of the class of stock of the issuing corporation having the greatest dividend rights.

In addition, the Act applies a 50-percent test in lieu of the prior law 80-percent test for purposes of determining whether stock of a parent corporation can be contributed to its subsidiary's TRASOP.

(g) Nonrecognition of gain or loss on contribution of stock of parent to TRASOP

Under prior law, the contribution by a subsidiary corporation (including a second-tier subsidiary) of stock of its parent corporation to a TRASOP was treated as a taxable exchange whether or not the subsidiary and parent were members of the same affiliated group of corporations.

The Act provides that where a parent corporation and a subsidiary corporation (including a second-tier subsidiary) are members of the same affiliated group of corporations, the subsidiary corporation will not recognize gain or loss on a contribution of stock of the parent corporation to a TRANSOP maintained by the subsidiary.

(h) Minimum tax

Under prior law, the additional investment tax credit attributable to a TRASOP contribution may result in the imposition of additional minimum tax.

The Act provides that no additional investment tax credit attributable to a TRASOP contribution could result in the imposition of additional minimum tax on the employer.

(i) Prohibition of withdrawal of TRASOP contributions on recapture or redetermination

Under prior law, an employer could withdraw TRASOP contributions to the extent of recapture or redetermination of additional the investment tax credit attributable to the contributions.

The Act provides that a TRASOP contribution made with respect to the additional investment tax credit attributable to a particular qualified investment may not be withdrawn if all or a portion of the credit is later redetermined or recaptured.

(j) Distributions from leveraged ESOPs and TRASOPs

Under prior law, the type of property which could be distributed from a leveraged ESOP or a TRASOP depended on the nature of the particular plan (profit-sharing, stock bonus, etc.).

The Act provides that a participant in a leveraged ESOP or a TRASOP who is entitled to a distribution under the plan must be given the right to require that the distribution be made in the form of employer securities. Subject to such right, the plan may elect to distribute the participant's interest in cash, in employer securities, or partially in cash and partially in employer securities.

(k) Put option on leveraged ESOP or TRASOP stock

Prior law contained no statutory requirement that leveraged ESOP or TRASOP participants be given the right to require the employer to repurchase distributed stock ("put option").

The Act requires that participants receiving a distribution of employer stock from a leveraged ESOP or TRASOP must generally be given a "put option" for the stock which meets specified requirements if the stock is not publicly traded.

(l) Effective dates

The provisions of the Act relating to leveraged ESOPs and TRASOPs generally apply with respect to qualified investments in taxable years beginning after December 31, 1978.

Sec. 142. Estate Tax Exclusion for Certain Lump Sum Distributions

Under prior law, it was unclear whether a death benefit distribution from a tax-qualified plan, which could be treated as a lump sum distribution, was eligible for the estate tax exclusion generally applicable to death benefit distributions from qualified plans. Denial of the estate tax exclusion could have applied whether or not the recipient actually elected to treat the distribution as a lump sum distribution to which favorable income tax treatment applies.

The Act provides that a death benefit under a qualified plan, which is eligible to be treated as a lump sum distribution, may be excluded from the gross estate of a deceased plan participant dying after Decem-

ber 31, 1978. The recipient of the distribution must agree in writing not to elect to treat the distribution as a lump sum distribution eligible for the special income tax treatment and the distribution must be otherwise eligible for the exclusion.

Sec. 143. Voting Rights on Employer Securities Held by Qualified Defined Contribution Plans

Under prior law, tax-qualified defined contribution plans generally were not required to pass through to plan participants voting rights on employer securities allocated to their accounts.

The Act provides that a tax-qualified defined contribution plan which is established by an employer whose stock is not publicly traded and which, following any acquisition of employer securities after December 31, 1979, holds more than 10 percent of its assets in employer securities must provide that the plan participants are entitled to exercise voting rights with respect to employer stock held by the plan on any corporate issue which must by law (or charter) be decided by more than a majority vote of outstanding common shares voted on the issue.

E. RETIREMENT PLAN PROVISIONS

Sec. 152. Simplified Employee Pensions

Under present law, employer- or union-sponsored pension plans are subject to comprehensive rules regarding employee participation, vesting, nondiscrimination, funding, fiduciary matters, and self-dealing. Pension plans are also required to comply with detailed reporting and disclosure rules.

Present law also provides for individual retirement accounts (IRAs) with rules which are considerably less complex than those applicable to pension plans. Deduction for IRA contributions are limited to the lesser of 15 percent of compensation or $1,500 ($1,750 in the case of spousal IRAs).

The Act raises the deduction limit for individual retirement accounts and individual retirement annuities to $7,500 or 15 percent of compensation (whichever is less), if the account or annuity qualifies as a simplified employee pension. The $7,500 limit applies only to employer contributions to a simplified employee pension.

The deduction for employer contributions to an individual's simplified employee pension is allower to an individual even though he or she is an active participant in a qualified plan, a tax-sheltered annuity, or a governmental plan. In other respects, however, the Act does not change the prior law limits on deductions for contributions to IRAs. Accordingly, if employer contributions to an individual's simplified employee pension for a year are less than the usual limit on deductible IRA contributions, the individual could make up the difference making deductible contributions to an IRA if he or she is not an active participant in a qualified plan, etc., for that year.

Under the Act, an individual retirement account or individual retirement annuity maintained by an employee qualifies as a simplified employee pension for a calendar year if the employer's program satisfies requirements as to withdrawals and the employer's allocation formula. The allocation formula must meet requirements as to employee participation and nondiscrimination.

An employer who contributes to a simplified employee pension is required to file a simplified report with respect to the contributions.

Under the Act, the usual limitation on an employer's deduction for contributions to a qualified pension, profit-sharing, or stock bonus plan (or a combination of such plans) is reduced by the deduction for contributions to simplified employee pensions. Employer contributions to simplified employee pensions are taken into account as employer contributions to a defined contribution plan under the limitations on benefits and contributions for qualified plans (sec. 415).

The simplified employee pension rules are effective for taxable years beginning after December 31, 1978.

Sec. 153. Defined Benefit Plan Limits

Under prior law, a participant's annual benefit under a qualified defined benefit pension plan was limited to the lesser of $75,000, adjusted for inflation since 1974 ($90,150 for 1978), or 100 percent of the participant's compensation for the participant's high 3 consecutive years of compensation.

Under the Act, the 100-percent-of-compensation limit is disregarded in the case of an employee who participates in a collectively bargained defined benefit pension plan covering at least 100 participants where specified requirements are satisfied. If the 100-percent-of-compensation rule is disregarded for a participant, under the Act, the $75,000 limit on annual benefits is reduced to $37,500 (adjusted for inflation since 1974).

The provision applies for years beginning after December 31, 1978.

Sec. 154. Custodial Accounts for Regulated Investment Company Stock

Under present law, amounts paid by a tax-exempt charitable organization or a public educational institution to purchase an auunity contract or stock in a regulated investment company to provide a retirement benefit for an employee can be excluded from the employee's income under the tax-sheltered annuity rules. Under proposed Treasury regulations, stock of a regulated investment company is considered purchased to provide a retirement benefit only if the stock cannot be distributed before the employee attains age 65 unless the employee dies or becomes disabled, and cannot be distributed on account of a separation from service unless the employee has attained age 55.

The Act permits stock of a regulated investment company to be considered purchased to provide a retirement benefit under the tax-sheltered annuity rules if it can be distributed only after the employee dies, becomes disabled, separates from service, attains age 59½, or encounters financial hardship.

The provision applies for taxable years beginning after December 31, 1978.

Sec. 155. Pension Plan Reserves

Under present law, special income tax treatment is accorded to a life insurance company with respect to income from the portion of its reserves allocable to annuity contracts entered into with trusts under tax-qualified pension plans or sold for use as individual retirement accounts or tax-sheltered annuities. This special treatment did not apply to earnings on reserves allocable to annuity contracts issued to State and local governments in connection with their unfunded deferred compensation plans or to annuity contracts issued to trusts under State and local retirement plans which were not tax-qualified.

The Act provides that, for taxable years commencing after December 31, 1978, income of a life insurance company from its reserves for

an annuity contract sold to a governmental pension plan (whether or not qualified) or to a government for use under an unfunded plan of deferred compensation will be accorded the same tax treatment as income from its reserves for an annuity contract sold to a qualified plan.

Sec. 156. Rollover of Distributions from a Tax-Sheltered Annuity

Generally, under present law, the recipient of a "lumpsum distribution" from a tax-qualified pension plan may make a tax-free rollover by transferring the otherwise taxable portion of the distribution to an IRA (an individual retirement account, annuity, or bond) or to another qualified pension plan. However, under prior law, recipients of distributions from a tax-sheltered annuity purchased by an employer that is a tax-exempt charitable organization or a public educational institution were not eligible for tax-free rollovers to IRAs.

Under the Act, the recipient of a lumpsum distribution under a tax-sheltered annuity contract is eligible to completely or partially roll over the otherwise taxable portion of the distribution to an IRA or to another tax-sheltered annuity. Subsequently, the amount rolled over to the IRA, plus earnings, may be rolled over to another tax-sheltered annuity, but may not be rolled over to a tax-qualified pension plan. The provisions of the Act apply to distributions or transfers made after December 31, 1978, in taxable years beginning after that date.

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Sec. 157. Individual Retirement Account Technical Changes

(a) *Extension of period for making individual retirement plan contributions*

Under prior law, an individual could make deductible IRA contributions for a taxable year not later than 45 days after the close of that taxable year. Under the Act, for taxable years beginning after December 31, 1977, an individual is permitted to establish and make deductible contributions to an IRA for a year up to the time for filing the individual's tax return for the year (including extensions).

(b) *Deduction of contributions in subsequent year for which there is an unused limitation*

Under prior law, if an individual did not make the maximum deductible contribution to an IRA for a year, the additional amount which the individual could have contributed and deducted was applied to reduce any accumulated excess contributions to the IRA as of the close of the year. However, no deduction was allowed with respect to the reduction of excess contributions.

Under the Act, a deduction is allowed to the extent that an unused IRA deduction limitation for a year reduces excess contributions to the IRA, but only to the extent that the excess contributions were not previously deducted. The provision applies retroactively to taxable years beginning after December 31, 1975. The Act also allows an individual to take a makeup deduction for 1978 for such corrections made in taxable years beginning in 1976 and 1977.

(c) *Additional period to rectify certain excess contributions*

Under prior law, an excess contribution by an individual to an IRA for a year could be corrected without penalty only if the excess contribution and any earnings thereon were withdrawn by the time for filing the indivdiual's tax return for the year (including extensions) and only if the amount withdrawn did not exceed the excess of $1,500 ($1,750 for a spousal IRA) over the amount allowable as a deduction for an IRA contributions for the year.

The Act allows the withdrawal of the excess contributions without incurring a penalty for the year of withdrawal, but only to the extent that a deduction was not previously allowed with respect to the excess contribution. This provision applies with respect to an individual who (1) makes an excess contribution to an IRA for a year (provided the amount of the contribution does not exceed $1,750), and (2) fails to correct the excess contribution by the date for filing the individual's tax return for the year (including extensions). In addition, the Act allows corrections for taxable years beginning after December 31, 1975, and before January 1, 1978, without regard to the $1,750 dollar limitation. Also, the Act allows an excess rollover contribution to be corrected, regardless of the amount, where it resulted from reasonable reliance on certain erroneous information.

(d) Addition of requirement that premiums on individual retirement annuity contracts must be flexible

Under prior law, an individual retirement annuity contract could require the payment of fixed premiums, irrespective of whether the premiums were deductible under the IRA provisions.

Under the Act, individual retirement annuity contracts issued after the date of enactment are required to provide for the flexible payment of premiums. In addition, the Act permits the tax-free exchange of previously issued fixed premium individual retirement annuity contracts for flexible premium individual retirement annuity contracts.

(e) Rollover of proceeds from sale of property

Under prior law, an individual who received property as part of a qualified plan distribution which was eligible for rollover treatment was accorded tax-free rollover treatment only if the actual property distributed from the qualified plan was contributed to an IRA or to another qualified plan.

Under the Act, an individual who receives property after December 31, 1978, as part of a distribution from a qualified plan which is eligible for rollover treatment is permitted to rollover the proceeds from the sale of the property on a tax-free basis.

(f) Rollover contribution to individual retirement plan of distribution to spouse from qualified plan or annuity

Under prior law, the spouse of a deceased participant who received a lump sum distribution from a qualified plan on account of the death of the participant was not eligible to make a rollover contribution of the amount received to an IRA.

Under the Act, the spouse of a deceased participant who, after December 31, 1978, receives a lump sum distribution from a qualified plan on account of the death of the participant is eligible to make a rollover contribution of the amount received to an IRA.

(g) Removal of certain restrictions on rollovers

Under prior law, an individual generally had to have been a participant in a qualified plan for 5 years in order to make a tax-free rollover of a lump sum distribution. Also, under prior law, rollovers between IRAs were permitted only once every 3 years.

Under the Act, an individual who participates in a qualified plan and who receives a lump sum distribution from the plan which is otherwise eligible for tax-free rollover treatment can make the rollover regardless of length of participation in the plan. Also, under the Act, rollovers between IRAs are permitted once a year.

(h) Waiver of excise tax on certain accumulations in individual retirement accounts or annuities

Under the Act, the Secretary of the Treasury is authorized to waive the 50-percent excise tax imposed on an individual who fails to receive certain minimum distributions from an IRA beginning at age 70½, where the failure to make such minimum distributions is due to reasonable error and reasonable steps are being taken to correct the error. The provision applies to taxable years beginning after December 31, 1975.

(i) Removal of certain limitations on provisions allowing correction of excess contributions

Under prior law, an excess contribution to an IRA for a year could be corrected without penalty if the contribution and earnings thereon were withdrawn from the IRA by the date for filing the tax return for the year (including extensions), and if the amount withdrawn did not exceed the excess of $1,500 ($1,750 for a spousal IRA) over the amount allowable as a deduction for an IRA contribution for the year.

Under the Act, the dollar limitations are removed. Thus, an excess contribution of any amount to an IRA for a year may be corrected without penalty if the excess contribution and the earnings thereon are withdrawn on or before the date for filing the tax return for the year (including extensions). The provision applies to taxable years beginning after December 31, 1977.

(j) Simplification of return requirements with respect to individual retirement plans

Under prior law, an individual maintaining an IRA was required to file a tax return with respect to the IRA each year.

Under the Act, IRA tax returns are not required for a year beginning after December 31, 1977, in which no IRA penalty taxes are imposed and no activity occurs with respect to the IRA other than the making of deductible contributions and permissible distributions.

F. OTHER INDIVIDUAL TAX PROVISIONS

Sec. 161(a). Uniformed Services Health Professions Scholarships

Under prior law, participants in the Uniformed Services Health Professions Scholarship Programs (including the Armed Forces and Public Health Services programs) entering these programs before 1979 could exclude from their income amounts received under these programs through 1982.

Under the Act, the exclusion provided for participants in the Uniformed Services Health Professions Scholarship programs (including the Armed Forces and Public Health Services programs) is extended one year so that students entering these programs in 1979 may exclude amounts received under these programs through 1983.

Sec. 161(b). National Research Service Awards

In Revenue Ruling 77–319, the Service ruled that amounts received as National Research Service Awards under the Public Health Service Act of 1974 (42 U.S.C. section 2891(1)), which had no specific statutory exclusion, were not excludable scholarships or fellowship grants.

The Act provides that amounts received under National Research Service Awards made in calendar years 1974 through 1979 may be excluded from recipients' income as tax-free scholarships or fellowships.

Sec. 162. Cancellation of Student Loans

Under certain student loan programs established by the United States, and State and local governments, all or a portion of the loan indebtedness may be discharged if the student performs certain services for a period of time in certain geographical areas pursuant to conditions in the loan agreement.

The Tax Reform Act of 1976 provided that no amount was to be included in gross income by reason of the discharge of all or part of a student loan if, pursuant to the loan agreement, such discharge is made and if the individual works for a certain period of time in certain geographical areas, or for certain classes of employers. This exclusion applied only to loans made by a governmental agency and was effective for discharge of such indebtedness if made before January 1, 1979.

The Act extends the exclusion provided in the Tax Reform Act of 1976 for the discharge of certain student loan indebtedness for 4 more years to apply to loans forgiven prior to January 1, 1983.

Sec. 163. Tax Counseling for the Elderly

The Act authorizes the Internal Revenue Service to enter into training and technical assistance agreements with private or public nonprofit agencies and organizations to prepare volunteers to provide tax counseling assistance for elderly individuals age 60 and older. It permits the Service to provide reimbursement to volunteers for trans-

portation, meals, and other expenses incurred by them in training or providing counseling assistance. These reimbursements received by the volunteer are to be exempt from income and social security taxes, except to the extent that a charitable contribution or other deduction is claimed for these expenses. The Secretary is authorized to provide the volunteers with preferential access to Internal Revenue Service taxpayer service representatives and make available technical information and material needed for their use.

Additionally, the Act provides that, from time to time, the IRS is to direct the attention of elderly individuals to tax measures of particular interest to the elderly, such as the tax credit for the elderly.

Sec. 164. Educational Assistance Programs

Under prior law, there was no provision for a specific exclusion from an individual's income for educational assistance provided by an employer. Thus, a determination as to whether an individual was required to include in income money or benefits furnished to assist him in his education generally was governed by sections 61 and 117 of the Code. Generally, these benefits would be subject to tax under prior law unless they qualified as job-related educational expenses deductible as a trade or business expense by the individual.

The Act excludes from an employee's gross income amounts paid for expenses incurred by the employer for educational assistance to the employee if the amounts are paid or the expenses are incurred pursuant to a program which meets certain requirements. In the case of education paid for, or furnished by, an individual's employer under such a program, the Act eliminates the need to distinguish job-related educational expenses from personal educational expenses for income tax purposes.

The educational benefits which may be excluded from income are those furnished by an employer only to employees. The employer may provide educational assistance to the employee directly or the employer may reimburse the employee for the latter's expenses. Under the Act, an employee can exclude from income tuition, fees, and similar payments, as well as the cost of books, supplies, and equipment paid for, or provided by, his employer; however, the employee cannot exclude tools or supplies which the employer provides and which the employee may retain after completion of the course of instruction. The education which may be furnished is not limited to job-related courses nor to courses which are part of a degree program. However, the exclusion does not apply to educational assistance furnished for courses involving sports, games, or hobbies.

For a program to qualify under this provision, the employees must not be able to choose taxable benefits in lieu of the educational benefits. An employer educational assistance program is not required to be funded nor to be approved in advance by the Internal Revenue Service.

In order to be a qualified program, an educational assistance program also must meet requirements with respect to nondiscrimination in contributions and benefits and in eligibility for enrollment. A program must benefit employees who qualify under a classification set up by the employer and found not to be discriminatory in favor of employees who are officers, owners, highly compensated, or

their dependents. Employees may be excluded from a program if they are members of a collective bargaining unit and there is evidence that educational assistance benefits were the subject of good faith bargaining between the unit and the employer or employees offering the program.

The Act also provides that amounts excluded from income as educational assistance are not to be treated as wages subject to withholding of income tax nor as wages subject to employment taxes (FICA and FUTA).

The exclusion applies to taxable years beginning after December 31, 1978, and ending before January 1, 1984.

TITLE II—TAX SHELTER AND PARTNERSHIP PROVISIONS

A. TAX SHELTER PROVISIONS

Sec. 201. Extension of At Risk Rules to All Activities Other Than Real Estate

Under prior law, there were two "at risk" rules designed to prevent a taxpayer from deducting losses in excess of his actual economic investment in the activity involved. The first of these at risk rules—"the specific at risk rule"—applied to four specified activities: (1) farming; (2) exploring for, or exploiting, oil and natural gas resources; (3) holding, producing, or distributing motion picture films or video tapes; and (4) leasing of personal property. The other at risk rule—"the partnership at risk rule"—applied generally to activities engaged in through partnerships. However, there were two exceptions to this rule. First, the rule did not apply to any activity to the extent that the specific at risk rule applied. Second, the rule did not apply to any partnership the principal activity of which was investing in real property (other than mineral property).

The Act extends the specific at risk rule to all activities except real estate (and certain equipment leasing activities of closely-held corporations, as discussed below). For the newly covered activities, the specific at risk rule covers activities which are a part of a trade or business or are engaged in for the production of income. Separate rules for aggregation and separation of activities are provided for the activities to which the at risk rule is extended by the Act. The holding of real property (other than mineral property) is to be treated as a separate activity, and the at risk rule is not applied to losses from that activity. For purposes of this exclusion, personal property and services which are incidental to making real property available as living accommodations are to be treated as part of the activity of holding the real property. Since all the activities currently covered by the partnership at risk rules would now be covered by the new expanded version of the specific at risk rules under section 465, the partnership at risk rule is repealed by the Act.

This provision is effective for taxable years beginning after December 31, 1978.

Sec. 202. Extension of At Risk Provisions to Closely Held Corporations

Under prior law, the only corporations to which the specific at risk rule applied were subchapter S corporations and personal holding companies. The Act extends the application of this rule to all corporations in which five or fewer individuals own more than 50 percent of the corporation's stock. However, the equipment leasing activities of a closely held corporation are not to be subject to the at risk rule if the corporation is actively engaged in equipment leasing, that is, if 50 percent or more of the corporation's gross receipts is derived from equipment leasing. This provision is effective for taxable years beginning after December 31, 1978.

Sec. 203. Recapture of Losses Where Amount At Risk Is Less Than Zero

Under prior law, the at risk rule under section 465 may have been interpreted to only require the taxpayer to be at risk as of the end of the taxable year for which losses were claimed. Under this interpretation, subsequent withdrawals of amounts originally placed at risk could be made without the recapture of previously allowed losses.

In order to be consistent with the original intent of the at risk rule, the Act requires the recapture of previously allowed losses when the amount at risk is reduced below zero. Mechanically, this rule works by providing that if the amount at risk is reduced below zero (by distributions to the taxpayer, by changes in the status of indebtedness from recourse to nonrecourse, by the commencement of a guarantee or other similar arrangement which affects the taxpayer's risk of loss, or otherwise), the taxpayer will recognize income to the extent that his at risk basis is reduced below zero. However, the amount recaptured is limited to the excess of the losses previously allowed and which reduced the taxpayer's at risk basis in that activity for taxable years beginning after December 31, 1978, over any amounts previously recaptured. A suspended deduction in the amount equal to the amount of recaptured income would be provided to the taxpayer. This suspended deduction would be allowed in a subsequent year if and to the extent the taxpayer's at risk basis is increased. The provision is generally effective for taxable years beginning after December 31, 1978.

B. PARTNERSHIP PROVISIONS

Sec. 211. Penalty for Failure to File Partnership Return

Under present law, partnerships are required to file an annual information return setting forth the partnership income, deductions, and credits, names and addresses of the partners, each partner's distributive share of partnership income, deduction, and credit, and certain other information required by the regulations. Under prior law, neither the partnership nor any partner was subject to a civil penalty for failure to file, or for late filing of, a partnership information return.

Under the Act, a civil penalty is imposed on the partnership for failure to timely file a complete partnership information return as required by existing Code sections. The penalty is assessed for each month, or fraction of a month (but not to exceed 5 months), that the partnership return is late or incomplete. The amount of penalty for each month, or fraction of a month, is $50 multiplied by the total number of partners in the partnership during the partnership's taxable year for which the return is due. The penalty will not be imposed if the partnership can show that failure to file a complete or timely return is due to reasonable cause. The provision is effective with respect to returns for taxable years beginning after December 31, 1978.

Sec. 212. Extension of Statute of Limitations for Partnership Items

Under present law, partnerships are not taxable entities. Instead, a partnership is a conduit, in which the items of partnership income, deduction, and credit are allocated among the partners for inclusion in their respective income tax returns. Under present law, partnerships are required to file an annual information return setting forth the partnership income, deductions, and credits, names and addresses of the partners, each partner's distributive share of partnership income, deduction, and credit, and certain other information required by the regulations. The Code provides a period of limitations during which the Service can assess a tax or a taxpayer may file a claim for refund. Generally, the period is 3 years from the date the tax return is filed. Under prior law, the income tax return of each of the partners of a partnership commenced that individual partner's period of limitations. Under prior law, the date of filing of the partnership return did not affect the period of limitations. In order to extend the period of limitations with respect to partnership items, the Service was required to obtain a consent for extension of the statute of limitations from each of the partners—not the partnership. Generally, an agreement to extend the period of limitations related to all items on the return of the partner who consented to the extension.

The Act extends the period of time in which assessments of deficiencies and claims for refund of tax attributable to partnership items may be made. These special periods of limitation apply only to partnership items which are attributable to "Federally registered partnerships". A Federally registered partnership means any partnership the interests in which have been offered for sale prior to the close of the taxable year in an offering required to be registered with the Securities and Exchange Commission (SEC) or any partnership which is or has been subject to the annual SEC reporting requirements which relate to the protection of investors. If a partnership is excused from registration or reporting by either a statutory or a regulatory exemption of the SEC, it is not to be treated as a Federally registered partnership.

With respect to deficiencies, the Act provides generally that the Service may assess a deficiency attributable to partnership items within 4 years after the partnership return for the partnership taxable year in which the item arose is filed. If the partnership return does not properly show the name and address of the person to be assessed the deficiency, the period of assessment will not expire until one year after that information is provided to the Service in the manner prescribed by regulations. With respect to credits and refunds, the Act provides generally that the taxpayer may file a claim for credit or refund of tax attributable to partnership items within 4 years after the due date (including extensions) of the partnership return for the partnership taxable year in which the item arose. This provision is effective for items arising in partnership taxable years beginning after December 31, 1978.

TITLE III—PROVISIONS PRIMARILY AFFECTING BUSINESS INCOME TAX

A. CORPORATE RATE REDUCTION

Sec. 301. Corporate Rate Reduction

Under prior law (through 1978), corporate income was subject to a normal tax of 20 percent on the first $25,000 of taxable income and 22 percent on income above $25,000, with a surtax of 26 percent imposed on corporate taxable income in excess of $50,000 (for a combined tax rate of 48 percent on income above $50,000). This tax rate structure had been enacted temporarily in the Tax Reduction Act of 1975, and subsequently had been extended through the end of 1978. After 1978, the corporate rate structure was scheduled to return to a normal tax of 22 percent of the first $25,000 of taxable income, with a surtax of 26 percent on income in excess of $25,000.

The Act reduces the top corporate income tax rate from 48 percent to 46 percent and provides a graduated rate structure for corporations with taxable income of less than $100,000. The corporate tax rates under the Act are:

Taxable income	*Tax rate*
$0 to $25,000	17 percent
$25,000 to $50,000	20 percent
$50,000 to $75,000	30 percent
$75,000 to $100,000	40 percent
Over $100,000	46 percent

In general, these corporate rate reductions apply to taxable years beginning after December 31, 1978.

B. INVESTMENT TAX CREDIT PROVISIONS

Sec. 311. Permanent Extension of 10-Percent Rate and $100,000 Used Property Limitation

Under prior law, an investment credit rate of 10 percent, and an annual used property limitation for credit purposes of $100,000, were available on a temporary basis through 1980. In 1981, the investment credit rate and the used property limitation were scheduled to revert to 7 percent generally and $50,000, respectively. The Act makes permanent both the 10-percent rate and the $100,000 used property limitation.

Sec. 312. Increase in Tax Liability Limitation to 90 Percent

Under prior law, taxpayers in general could use investment credits to offset the first $25,000 of tax liability each year, plus 50 percent of tax liability over $25,000. Temporary increased percentage limitations were allowed for taxpayers with specified percentages of investment in utility property, airline property, or railroad property.

The Act increases the 50-percent limitation to 90 percent, to be phased-in at 10 additional percentage points per year beginning with taxable years which end in 1979. The Act also allows taxpayers with utility, airline, or railroad property to use the higher limitation available under either prior law, if applicable, or this provision during the phase-in period.

Sec. 313. Increased Investment Credit for Certain Pollution Control Facilities

Under prior law, the investment credit was allowed for only one-half of the investment in pollution control facilities where the taxpayer had elected to amortize this investment over a 60-month period. (This provision in effect limited the credit to 5 percent for those pollution control facilities electing 60-month amortization.)

The Act generally allows the credit for the full investment in pollution control facilities where 60-month amortization has been elected for these facilities. However, where a facility is also financed with tax-exempt industrial development bonds, the credit is allowed for only one-half of the investment subject to 60-month amortization. This provision applies to property acquired by the taxpayer after December 31, 1978, and to property constructed by the taxpayer after December 31, 1978, to the extent of basis arising after that date.

Sec. 314. Investment Credit for Single Purpose Agricultural or Horticultural Structures

Under prior law, numerous questions had arisen concerning the eligibility of single purpose agricultural and horticultural structures to qualify for the investment credit as tangible property used for productive purposes. The Internal Revenue Service had generally disallowed the credit for these structures on the basis that these structures provided working space for employees or because the useful life

of the equipment within the structure was not contemporaneous with that of the structure itself. However, taxpayers had successfully litigated this issue in some cases.

The Act clarifies prior law by specifically providing that single purpose structures used to produce livestock, poultry, eggs, plants, and plant products are eligible for the investment credit. In order to be covered by this provision a structure must be specifically designed, constructed, and used for a particular agricultural or horticultural production activity, such as producing hogs, cattle, milk, poultry, eggs, plants, or plant products (including mushrooms). The structure must be used exclusively for the specific agricultural or horticultural purposes for which it was designed and constructed. These provisions apply to open taxable years ending after August 15, 1971.

Sec. 315. Investment Credit for Certain Rehabilitated Buildings

Under prior law, expenditures for rehabilitating or renovating buildings used in a trade or business, or held for investment purposes, were not eligible for the investment credit.

The Act extends the investment credit to rehabilitation expenditures for all types of buildings held for business or investment purposes, except those, such as apartments, which are used for residential purposes. Eligible buildings include factories, warehouses, hotels, and retail and wholesale stores.

Expenditures which qualify for the credit are depreciable rehabilitation costs incurred after October 31, 1978, in connection with a building which has been in use for at least 20 years, for the interior or exterior renovation, restoration, or reconstruction of the building. Costs for acquiring or completing a building, or for the replacement or enlargement of a building, are excluded. If more than 25 percent of the exterior walls are replaced, the costs will not qualify.

The rehabilitations must have useful lives of at least 5 years and the credit will be determined using the present limitations applicable to useful lives. In addition, the costs must be incurred at least 20 years after the last prior qualifying rehabilitation (if any) was completed. The investment credit under these provisions is not available where 5-year amortization has been elected for rehabilitation costs on a certified historic structure, and, even if the credit rather than amortization is elected for such costs, they must be certified as appropriate by the Department of Interior in order to qualify.

These provisions generally apply to qualifying expenditures incurred after October 31, 1978.

Sec. 316. Investment Credit for Cooperatives

Cooperatives are generally taxed as corporations, but are allowed to deduct certain payments made to patrons and shareholders. Under prior law, the amount of investment credit available for cooperatives was reduced in proportion to the reduction in taxable income resulting from the special deductions. These otherwise allowable credits expired and were not passed through to the patrons or shareholders.

Under the Act, the special limitations on the use of the investment credit by cooperatives are eliminated. Cooperatives will be permitted to use the investment credit in the year property is placed in service

to the same extent as corporations generally. To the extent a cooperative cannot use an investment credit in the current year, the credit will not be carried back or carried forward but will be allocated to the patrons of the cooperative. Any recapture of investment credits, including credits allocated to patrons, will be effected at the level of the cooperative. These rules are applicable to taxable years ending after October 31, 1978.

Sec. 317. Investment Credit Recapture Under the ConRail Reorganization

Prior law did not provide an exemption from investment credit recapture for the transferor railroads in the ConRail reorganization, although such an exemption is generally otherwise allowed where assets are transferred in a tax-free reorganization. The Act adds an exemption to the investment credit recapture rules so that a transferor railroad will not be subject to additional tax on its transfer of rail properties to ConRail. This provision applies to taxable years ending after March 31, 1976.

C. TARGETED JOBS CREDIT; WIN CREDIT

Sec. 321. Targeted Jobs Credit

Under prior law, an employer could claim a new jobs tax credit for 1977 and 1978, which was equal to 50 percent of the increase in the employer's wage base under the Federal Unemployment Tax Act (FUTA) above 102 percent of that wage base in the previous year. The FUTA base for 1977 consisted of wages paid up to $4,200 per employee; and, although the FUTA wage base rose to $6,000 in 1978, only $4,200 of wages per employee could be taken into account for purposes of the jobs credit in 1978.

The total amount of the credit had four limitations: (1) the credit could be not more than 50 percent of the increase in total wages paid by the employer for the year above 105 percent of total wages paid by the employer in the previous year, (2) the credit could not be more than 25 percent of the current year's FUTA wages, (3) the credit for a year could not exceed $100,000, and (4) the credit could not exceed the taxpayer's tax liability.

An employer's deduction for wages paid was reduced by the amount of the credit.

Prior law also provided an additional nonincremental credit equal to 10 percent of the first $4,200 of FUTA wages paid to handicapped individuals undergoing vocational rehabilitation. This credit could not exceed one-fifth of the regular 50-percent new jobs credit which would have been allowable without regard to the $100,000 limitation. However, the special 10-percent credit was not itself subject to any specific dollar limitation.

The Act replaces the general jobs credit with a targeted jobs credit, equal to 50 percent of the first $6,000 of wages of qualifying trade or business employees for the first year of employment, and 25 percent of such wages for the second year of employment. No credit is allowed with respect to wages paid for employment not in a trade or business. The credit is to be available for hiring: (1) recipients of Supplemental Security Income, (2) handicapped individuals undergoing vocational rehabilitation, (3) individuals of ages 18 through 24 who are members of economically disadvantaged families (defined as families with income during the preceding 6 months which on an annual basis was less than 70 percent of the Bureau of Labor Statistics lower living standard), (4) Vietnam-era veterans under the age of 35 who are members of economically disadvantaged families, (5) recipients of general assistance for 30 or more days, (6) individuals of ages 16 through 18 who are participants in a qualified cooperative education program, and (7) convicts who are members of economically disadvantaged families (if they are hired within 5 years after the date of release from prison or date of conviction). The Act requires that the Secretaries of Labor and Treasury jointly designate a single employment agency in each locality to certify eligible employees.

In order to prevent the hiring of targeted employees from displacing a substantial number of nontargeted employees, the Act provides that qualified first-year wages during a taxable year cannot exceed 30 percent of aggregate FUTA wages for all employees during the calendar year ending in that taxable year. An employer's deduction for wages is reduced by the amount of the credit, and the credit is limited to 90 percent of tax liability. The credit is elective. Further, no credit may be claimed with respect to employees for whom employers receive on-the-job training payments.

The new targeted jobs credit will apply generally to wages paid or incurred after December 31, 1978, in taxable years ending after December 31, 1978, for employees hired after September 26, 1978.

Sec. 322. Work Incentive Program (WIN) Credit Changes

Prior law provided a work incentive (WIN) credit and a welfare recipient tax credit. Under these provisions, employers could claim a tax credit equal to 20 percent of the wages paid during the first 12 months of employment to recipients of aid to families with dependent children (AFDC) who had received AFDC for at least 90 days or who were placed in employment under the WIN program. The amount of the credit available to any employer was limited to $50,000 of tax liability plus one-half of tax liability in excess of $50,000. Generally, up to $5,000 of wages paid for nonbusiness employment were eligible for the credit.

Under the Act, employers who hire AFDC recipients who are placed in employment under the WIN program, or who have received AFDC for at least 90 days, are entitled to a credit equal to 50 percent of up to $6,000 of wages per employee for the first year of trade or business employment and 25 percent of such wages for the second year of trade or business employment. An employer's deduction for wages is reduced by the amount of the credit.

The Act provides that for employment not in a trade or business, the credit is to be 35 percent of the first $6,000 of wages per employee for the first year of employment. Eligible nonbusiness wages are limited to $12,000 for any employer.

Under the Act, no credit is allowed for: (1) expenses reimbursed by a grant; (2) employees who work for the employer 30 days or less on a substantially full-time basis; (3) employees who displace other employees from employment; (4) migrant workers; or (5) employees who are close relatives, dependents, or major stockholders of the employer. In addition, the WIN-welfare recipient tax credit is limited to 100 percent of tax liability.

The WIN-welfare recipient tax credit amendments generally are effective for expenses paid or incurred after December 31, 1978, in taxable years ending after December 31, 1978, for employees hired after September 26, 1978.

D. TAX-EXEMPT BONDS

1. INDUSTRIAL DEVELOPMENT BOND PROVISIONS

Sec. 331. Increase in Limit on Small Issues

Under present law, interest on industrial development bonds is, in general, taxable. However, interest on certain small issues of industrial development bonds is tax-exempt. Small issues are issues of $1 million or less the proceeds of which are used for the acquisition or construction of depreciable property or land. At the election of the issuer, the $1 million limitation could be increased to $5 million under prior law. If this election was made, certain capital expenditures and the total of a series of small issues for a project could not exceed $5 million.

The Act increases the limitation on elective small issues of industrial development bonds from $5 million to $10 million. In addition, the capital expenditure limitation for facilities with respect to which an urban development action grant (UDAG) has been made is increased to $20 million. However, only $10 million of the funds used to finance an urban development action grant facility may be provided through the use of tax-exempt elective small issue industrial development bonds.

The provision increasing the elective small issues limitation to $10 million applies to bonds issued after December 31, 1978, and to capital expenditures made after December 31, 1978, with respect to obligations issued before January 1, 1979. The provision dealing with urban development action grants applies to obligations issued after September 30. 1979, and to capital expenditures made after September 30, 1979, with respect to obligations issued after that date.

Sec. 332. Local Furnishing of Electric Energy

Tax-exempt treatment is provided for industrial development bonds used to provide facilities for the local furnishing of electric energy. Local furnishing has been interpreted by the Internal Revenue Service to mean the furnishing of electric energy to the general populace of an area comprising no more than two contiguous counties (or political equivalents). The Act includes, within the definition of local furnishing of electric energy, the furnishing solely within an area comprising a city and one contiguous county. This provision applies to taxable years ending after April 30, 1968, with respect to obligations issued after that date.

Sec. 333. Industrial Development Bonds for Water Facilities

Under present law, an industrial development bond qualifies for tax-exempt treatment where substantially all the proceeds of the bond are used to provide facilities for the furnishing of water if available on reasonable demand to members of the general public.

The Act provides that members of the general public include commercial users. Thus, under the Act, when the proceeds of an industrial

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development bond are used to provide facilities for the furnishing of water to the general public for any purpose, the interest received on the bond will qualify for tax exemption.

The Act imposes three requirements which the facility must satisfy in order for the bonds to qualify for tax exemption. First, the facility must be for the furnishing of water. Second, the facility must be operated by a governmental unit or a regulated public utility. Finally, the facility must make or will make water available to members of the general public. For purposes of this provision, the general public includes agricultural, industrial, commercial, and electric utility users.

The provision applies to obligations issued after the date of enactment.

Sec. 334. Advance Refunding of Industrial Development Bonds for Certain Public Projects

Under present law, certain industrial development bonds qualify for tax exemption where substantially all the proceeds of the bonds are used to provide certain "exempt activities" facilities, e.g., mass commuting facilities. However, it has been unclear under what circumstances a refunding issue of exempt activity industrial development bonds would qualify for tax exemption.

Under the Act, a refunding of an industrial development bond in advance of its redemption qualifies for tax exemption, but only if substantially all the proceeds of the refunded issue were used to provide a qualified public facility. A qualified public facility is defined as airports, docks or wharves, mass commuting facilities, parking facilities, or storage or training facilities directly related to these facilities, and convention or trade show facilities which are available for use by the general public.

The provision applies to refunding obligations issued after the date of enactment.

2. OTHER TAX-EXEMPT BOND PROVISIONS

Sec. 336. Declaratory Judgments Relating to the Status of State and Local Government Obligations

Present law provides that interest on State and local government obligations is, in general, tax-exempt. However, tax-exempt status is denied to arbitrage bonds and certain industrial development bonds. Moreover, in order for such an obligation to be tax exempt, it must have been issued by a State or local government or issued by an authority "on behalf of" a State or local government.

Under prior law, as a practical matter, an issuer has had no appeal from an Internal Revenue Service private letter ruling (or failure to issue a private letter ruling) that a proposed issue of municipal bonds is taxable. In addition, it has been impossible for an issuer to question the Service's rulings and regulations directly.

The Act authorizes the Tax Court to issue declaratory judgments with respect to the tax-exempt status of proposed bond issues. However, relief under the amendment is available only to the proposed bond issuer and only if: (1) the proposed issuer has requested a private letter ruling from the Internal Revenue Service (IRS), (2) the IRS has acted adversely on the request or has failed to act within 180 days,

and (3) the proposed issuer has otherwise exhausted all administrative remedies. The Tax Court determination is to be based on any facts or arguments which the IRS and/or the proposed issuer wish to introduce at the time of trial. Appeal of the decision of the Tax Court will lie exclusively with the United States Court of Appeals for the District of Columbia Circuit.

The provision applies to requests for determinations (private ruling requests) filed with the Internal Revenue Service after December 31, 1978.

Sec. 337. Treatment of Certain Arbitrage Profits From Advance Refunding of State and Local Government Obligations

Prior to 1969, State and local governments were able to earn arbitrage profits through investing the proceeds of their tax-exempt bonds in higher yielding Treasury obligations. In 1969, tax-exempt status was denied to State and local government obligations (arbitrage bonds) the proceeds of which are invested in materially higher yielding securities or the proceeds of which are used to replace funds which were used to acquire materially higher yielding obligations.

These yield restrictions which were placed on State and local government obligations created a situation where some State and local governments attempted to divert arbitrage profits to third parties which, in some instances, were charities.

On September 24, 1976, the Treasury Department announced regulations which were designed to prevent issuers from diverting arbitrage profits to underwriters and third parties.

The Act, in general, prohibits the Treasury from applying the position taken by the regulations retroactively to prevent arbitrage profits from being donated to a public charity. Thus, under the Act, payment of a refund profit in accordance with a qualified agreement shall not cause the refunding obligation (which gave rise to the refund profit) to be treated as an arbitrage bond or cause imposition of any penalty upon the issuer ("blacklisting") if pursuant to the qualified agreement the refund profit is held (1) in a trust fund, (2) in an escrow account, or (3) by an underwriter or other person.

In addition, where a State or local government accounts to the United States for the refund profit by direct payment or by purchase of low-interest United States obligations because of the Internal Revenue Service's rulings policy, the Treasury shall return such accounted-for refund profits so that it can, within 90 days, be given to the intended beneficiary. Repayment by the Treasury shall be required under the Act, only if on or before January 1, 1977, the State or local government which entered into a qualified agreement requested, in writing, a ruling from the Internal Revenue Service on the tax consequences of paying refund profits to charitable organizations and failed to receive a favorable ruling, and did not pay the refund profit to a charitable organization. The repayment shall be paid out of unappropriated Treasury funds.

E. SMALL BUSINESS CORPORATION PROVISIONS

Sec. 341. Subchapter S Corporation Allowed 15 Shareholders

Under prior law, in order to be eligible for a subchapter S election, a corporation could have only 10 or fewer shareholders. However, after a corporation had been an electing subchapter S corporation for 5 consecutive taxable years, it was allowed to increase its number of qualifying shareholders to 15. In addition, the number of shareholders was allowed to exceed 10 (but not 15) if the additional shareholders acquired their stock through inheritance.

Under the Act, the number of shareholders permitted in order for a corporation to qualify for and maintain subchapter S status is increased from 10 to 15 (without regard to any 5-year period). The provision applies to taxable years beginning after December 31, 1978.

Sec. 342. Permitted Shareholders of Subchapter S Corporations

For purposes of determining the maximum number of shareholders a corporation may have in order to be eligible for a subchapter S election, prior law provided that stock which was community property of a husband and wife (or the income from which was community property income) under the law of a community property State would be treated as owned by one shareholder. Similarly, a husband and wife were treated as one shareholder if they owned the stock as joint tenants, tenants in common, or tenants by the entirety. Also, a surviving spouse and the estate of a deceased spouse (or the estates of both deceased spouses) were treated as one shareholder if the husband and wife were treated as one shareholder at the time of the death of the deceased spouse.

Under the Act, a husband and wife (and their estates) are to be treated as one shareholder for purposes if determining the number of shareholders in a corporation in determining whether it is eligible to qualify as an electing small business corporation. This treatment is to apply regardless of whether shares are individually or co-owned by the spouses. The provision applies to taxable years beginning after December 31, 1978.

Sec. 343. Extension of Period for Making Subchapter S Elections

Prior law required that in order for a subchapter S election to be effective for a taxable year, it had to be filed during a 2-month period which began one month before the start of the taxable year. An election was not valid for either the intended year or any future year if it was not filed within this period. Extensions of time for filing the election were not granted. If an election was found to be untimely upon audit several years later, the corporation was taxed as a regular corporation for all the intervening years.

Under the Act, the period of time to make a subchapter S election is expanded to include the entire preceding taxable year of the corporation. In addition, the bill will permit all corporations to make an election during the first 75 days of the taxable year for which the election is effective. The provision is effective for subchapter S elections made for taxable years beginning after December 31, 1978.

Sec. 345. Small Business Corporation Stock

Under present law, ordinary loss, rather than capital loss, treatment is provided in certain cases for small business corporation stock (section 1244 stock) which is disposed of at a loss by individual shareholders to whom the stock was issued. Under prior law, the maximum amount of ordinary loss from the disposition of section 1244 stock that could be claimed in any taxable year was $25,000 ($50,000 in the case of a joint return). Excess losses are treated as capital losses.

Under prior law, in addition to certain other requirements, the following requirements had to be met for stock to qualify as section 1244 stock: (1) The corporation issuing the stock had to adopt a written plan under which the stock would be issued; (2) the amount of section 1244 stock issued by the corporation could not exceed $500,000 and the total stock issued plus the equity capital of the corporation could not exceed $1,000,000; (3) no prior offering of stock of the corporation or any portion of a prior offering of stock could be outstanding.

The Act increases the maximum amount an individual may treat as an ordinary loss on section 1244 stock for any taxable year from $25,000 to $50,000 ($100,000 in the case of a joint return) and also increases the amount of section 1244 stock that a qualified small business corporation may issue from $500,000 to $1,000,000. Additionally, the Act repeals the: (1) written plan requirement, (2) equity capital limitation, and (3) no prior stock offering limitation. This provision applies to common stock issued after the date of enactment of the Act.

F. FARM ACCOUNTING RULES

Sec. 351. Treatment of Certain Closely-Held Farm Corporations for Accrual Accounting Purposes

With certain exceptions, the Tax Reform Act of 1976 required corporations (and partnerships in which nonexcepted corporations are partners) engaged in farming to use an accrual method of accounting and to capitalize preproductive period expenses. However, subchapter S corporations, family corporations (in which one family owns at least 50 percent of the stock), corporations with annual gross receipts of $1 million or less, and nurseries are not required to use the accrual method of accounting or to capitalize preproductive period expenses.

The 1976 Act provisions generally are effective for taxable years beginning after December 31, 1976. However, the Tax Reduction and Simplification Act of 1977 postponed the effective date of the required accrual accounting provision until taxable years beginning after December 31, 1977, for certain farming corporations controlled by two or three families.

The Act provides exceptions to the required accrual accounting and capitalization of preproductive period expense rules for certain corporations which are controlled by two or three families. The provisions requiring accrual accounting and the capitalization of preproductive period expenses will not apply to any farm corporation if, as of October 4, 1976, and at all times thereafter, either (1) two families own (directly or through attribution) at least 65 percent of the total combined voting power of all classes of stock of the corporation entitled to vote and at least 65 percent of the total number of shares of all other classes of stock of the corporation, or (2) (a) members of three families own (directly or through attribution) at least 50 percent of the total combined voting power of all classes of stock entitled to vote and at least 50 percent of the total number of shares of all other classes of stock and (b) substantially all of the remaining stock is owned by corporate employees, their family members, or a tax-exempt employees' trust for the benefit of the corporation's employees.

The Act also provides that, with respect to corporations described in the preceding paragraph, stock acquired after October 4, 1976, by the corporation's employees, their families, or a tax-exempt trust for their benefit will be treated as owned by one of the two or three families whose combined stock ownership was used to establish the initial qualification for this provision (as of October 4, 1976). The provision requires that corporations must have been engaged in the trade or business of farming on October 4, 1976, and at all times thereafter, to qualify for this exception.

This provision applies to taxable years beginning after December 31, 1977.

Sec. 352. Accounting for Growing Crops

Prior to 1976, farmers, nurserymen, and florists were not required to inventory growing crops regardless of the method of accounting they used for income tax purposes. However, in 1976 the Internal Revenue Service ruled that an accrual method farmer, nurseryman, or florist would be required to inventory growing crops. The changes made by this ruling are to be for taxable years beginning on or after January 1, 1978.

Under present law, corporations and partnerships (in which nonexcepted corporations are partners) engaged in farming are required to use the accrual method of accounting and to capitalize preproductive period expenses (sec. 447). However, subchapter S corporations, family corporations (in which one family owns at least 50 percent of the stock), corporations with annual gross receipts of $1 million or less, and nurseries are not required to use the accrual method of accounting or to capitalize preproductive period expenses. In general, the requirement that preproductive period expenses be capitalized would have the effect of requiring taxpayers to inventory (or capitalize) the costs of growing crops.

The Act permits a farmer, nurseryman, or florist who is on an accrual method of accounting and is not required by section 447 of the Code to capitalize preproductive period expenses to be exempt from the requirement that growing crops be inventoried. The term growing crops does not include trees grown for lumber, pulp, or other nonlife purposes.

The Act also allows those farmers, nurserymen, or florists who are eligible to use an accrual method of accounting without inventorying growing crops to elect, without the prior approval of the Internal Revenue Service, to change to the cash receipts and disbursements method of accounting with respect to any trade or business in which the principal activity is growing crops. If such an election is made, it will be treated as a change in method of accounting initiated by the taxpayer. This election may be initiated only with respect to a taxable year beginning after December 31, 1977, and before January 1, 1981.

Sec. 353. Treatment of Certain Farms for Purposes of Rule Requiring Accrual Accounting

With certain exceptions, the Tax Reform Act of 1976 required corporations (and partnerships in which nonexcepted corporations are partners) engaged in farming to use an accrual method of accounting and to capitalize preproductive period expenses. However, subchapter S corporations, family corporations (in which one family owns at least 50 percent of the stock), corporations with annual gross receipts of $1 million or less, and nurseries are not required to use the accrual method of accounting or to capitalize preproductive period expenses.

In addition to the exceptions to the accrual method of accounting and capitalization of preproductive period expenses provided under section 351 of the Act, sod farms are also excepted from these rules. The provision excepting sod farms is effective for taxable years beginning after December 31, 1976.

G. OTHER BUSINESS TAX PROVISIONS

Sec. 361. Entertainment Facility Expenses

Under prior law, expenses with respect to entertainment "facilities" were deductible if (1) they were ordinary and necessary, (2) the facility was used primarily for the furtherance of the taxpayer's business (i.e., more than 50 percent of the time that it was used), and (3) the expense in question was "directly related" to the active conduct of the taxpayer's business. For this purpose, an entertainment facility generally was any item of personal or real property used for, or in connection with, an activity which was of a type ordinarily considered to constitute entertainment, amusement, or recreation (including social, athletic, and sporting club memberships). There were a number of exceptions, however, to the general rule which disallowed deductions for entertainment facility expenses.

The provisions of the Act, which are effective for expenditures paid or incurred in taxable years ending after December 31, 1978, generally allow deductions for any expense paid or incurred with respect to a facility which is used in conjunction with an activity which is of a type ordinarily considered to constitute entertainment, amusement, or recreation. However, the Act generally continues the exceptions of prior disallow deductions for any expense paid or incurred with respect to a law, and does not apply to qualifying dues or fees paid to clubs, expenditures for tickets to sporting or theatrical events, or to similar expenses if otherwise deductible under the business test.

Sec. 362. Deficiency Dividend Procedure for Regulated Investment Companies

Under present law, in order to receive favorable conduit treatment, a regulated investment company must distribute at least 90 percent of its income to its shareholders during the taxable year or, with certain limitations, within the 12-month period after the taxable year. Under prior law, there was no deficiency dividend procedure for a regulated investment company so that dividends paid after the taxable year and the following 12-month period may be taken into account for purposes of the 90-percent distribution requirement. Thus, a subsequent audit change by the Internal Revenue Service which increases income could cause the company to fail to meet the distribution requirement.

The Act provides a deficiency dividend procedure for regulated investment companies. Under the procedure, the company could make qualifying distributions after the regular period for making distributions when an adjustment by the Internal Revenue Service occurs that either increases the amount which the company is required to distribute to meet the distribution requirement or decreases the amount of the dividends previously distributed for that year. The procedure is similar to the deficiency dividend procedure provided for real estate investment trusts by the Tax Reform Act of 1976. The provision is effective for determinations made after the date of enactment.

Sec. 363. Safe Harbor Rule For Real Estate Investment Trusts

Under present law, a 100-percent penalty tax is imposed upon a real estate investment trust (REIT) from gain derived from property held primarily for sale to customers in the ordinary course of the REIT's trade or business. In addition, the normal corporate tax is imposed on income from certain property acquired by a REIT through foreclosure. Under prior law, a REIT could hold such foreclosure property for a period of 2 years with permissible extensions by the Internal Revenue Service for another 2 years.

The Act establishes for REITs a safe harbor rule which provides that the 100-percent penalty tax will not apply where the following conditions are met: (1) the property has been held by the REIT for at least four years, (2) the total expenditures made by the REIT during the 4-year period prior to sale do not exceed 20 percent of the net selling price of the property, (3) the REIT does not sell more than five properties during the taxable year, and (4) if the property is land or improvements not acquired through foreclosure, the property has been held by the REIT for rent for a period of at least 4 years. In addition, the Act increases the additional period that the Internal Revenue Service may grant to a REIT to hold foreclosure property from 2 years to 4 years (for a total of 6 years that foreclosure property may be held). The safe harbor rule is effective for taxable years ending after the date of enactment. The lengthening of the permissible extension period is effective for extensions granted after the date of enactment with respect to extension periods beginning after December 31, 1977.

Sec. 364. Contributions in Aid of Construction to Regulated Electric or Gas Public Utilities

Prior to 1975, the Internal Revenue Service took the position that contributions in aid of construction to regulated public utilities were not includible in the gross income of the utility. In 1975, the Internal Revenue Service revoked its prior position and held that customer connection fees received by a water utility were includible in the gross income of the utility.

The Tax Reform Act of 1976 provided that contributions in aid of construction to regulated public water and sewerage disposal utilities are to be treated as nontaxable contributions to the capital of the utility. In such a case, the utility is not entitled to any depreciation or investment tax credit with respect to property to the extent acquired with nontaxable contributions.

The Act extends to regulated public gas and electric utilities the nontaxable treatment presently accorded to water and sewerage disposal utilities. Consequently, contributions in aid of construction to regulated public gas and electric utilities are not includible in the gross income of the utility and no depreciation or investment tax credits will be allowable with respect to property acquired with nontaxable contributions. The provision is effective with respect to contributions made after January 31, 1976.

Sec. 365. Liabilities of Controlled Corporations

Upon incorporation of a business, no gain or loss is generally recognized as a result of the transfer of property to the corporation, provided the transferors own 80 percent of the stock of the corporation immediately following the transfer. An exception applies where the corporation assumes a liability or acquires property subject to a liability, and the total amount of these liabilities exceeds the adjusted basis of the property transferred to the corporation. In this situation, the difference between the liabilities over the adjusted basis of the assets is considered as taxable gain to the transferor. Under prior law, it was unclear if an exception applied to this rule in the case of a cash basis transferor for certain trade accounts payable.

Under the Act, in determining the amount of liabilities transferred to a corporation upon incorporation, trade accounts payable and certain other liabilities (including certain payments to a retiring partner) which would have been deductible upon payment by the transferor are excluded. In addition, such excluded liabilities do not reduce the transferor's basis in stock received in the exchange.

The provision applies to transfers occurring on or after the date of enactment.

Sec. 366. Medical Expense Reimbursement Plans

Under prior law, gross income did not include amounts received under a self-insured accident or health plan as reimbursement for employee medical expenses, unless the expenses were deducted in a prior taxable year.

Under the Act, self-insured medical reimbursement plans are subject to rules regarding discrimination as to eligibility and benefits in favor of employees who are officers, shareholders, or highly paid. Reimbursements to an officer, etc., under a discriminatory plan are wholly or partly includible in income.

Under the Act, a plan satisfies the nondiscriminatory eligibility rule if it meets requirements similar to those which must be satisfied by qualified pension plans (sec. 410(b)). In testing the eligibility provisions of a plan, however, part-time employees and seasonal employees may be excluded. Under the Act, employees whose customary weekly employment is for less than 35 hours are considered part-time, and employees whose customary annual employment is for less than 9 months are considered seasonal.

The Act provides that benefits are considered discriminatory unless all benefits provided for officers, etc., are also provided for other employees. However, under the Act, a plan is not considered to provide discriminatory benefits merely because benefits thereunder are offset by benefits paid under another plan of the employer or another employer (insured or self-insured) or by benefits paid under Medicare or other Federal or State law.

The provision applies for taxable years beginning after December 31, 1979.

Sec. 367. Five-Year Amortization for Low-Income Rental Housing

Under the Code, special depreciation rules are provided for expenditures to rehabilitate low-income rental housing. Under the special depreciation rules for low-income rental property, taxpayers can elect

to compute depreciation on certain rehabilitation expenditures under a straight-line method over a period of 60 months, if the additions or improvements have a useful life of 5 years or more.

The Act provides a 3-year extension of the special 5-year depreciation rule for expenditures to rehabilitate low-income rental housing. The three-year extension applies to expenditures paid or incurred with respect to low- and moderate-income rental housing after December 31, 1978, and before January 1, 1982 (including expenditures made pursuant to a binding contract entered into before January 1, 1982).

Sec. 368. Postponement of Effective Date for Special Limitations on Net Operating Loss Carryovers

The Tax Reform Act of 1976 extensively revised the Code provisions dealing with the carryover of net operating losses in cases of acquisitions of loss corporations. That Act eliminated continuity of business requirements for purchase acquisitions and provided parallel continuity of ownership rules for taxable and nontaxable acquisitions (under which loss carryovers are allowed on a declining scale based on the continuing ownership by the former owners of the loss company). These provisions were to apply to plans of reorganization adopted on or after January 1, 1978, and to sales or exchanges in taxable years beginning after June 30, 1978.

The Act delays the effective date of these provisions for 2 additional years so that they will not take effect until January 1, 1980, with respect to plans of reorganization adopted on or after that date, or until June 30, 1980, with respect to sales or exchanges occurring in taxable years beginning after that date. The Act permits the election of the 1976 Act provisions with respect to any acquisition or reorganization, which occurs before the close of the taxpayer's first taxable year beginning after June 30, 1978, if made pursuant to a written binding contract or option to acquire stock or assets entered into before September 27, 1978. If this election is made, the 1976 Act provisions are to apply to all acquisitions and reorganizations by the taxpayer during the applicable postponement period.

Sec. 369. Use of Certain Expired Net Operating Loss Carryovers and Redemptions of Certificates of Value in a Tax-Free Reorganization of a Transferor Railroad

Under present law, tax attributes (including net operating losses) of a predecessor corporation generally carry over to a successor corporation in a tax-free reorganization. Special net operating loss rules apply to railroads which transfer property under the ConRail reorganization (i.e., otherwise expired net operating losses are revived to the extent any income is realized eventually from certificates of value issued for the transfer of property). Present law does not deal specifically with the effect of the tax-free reorganization on the special net operating loss rule for ConRail transferor corporations.

The Act provides that the special treatment of net operating losses of transferor railroads and redemptions of certificates of value is not to be affected by a tax-free reorganization of a transferor railroad and another member of its affiliated group of corporations. This provision is effective for taxable years ending after March 31, 1976.

Sec. 370. Source of Income From Lease of Certain Railroad Rolling Stock

Under present law, a lessor of railroad rolling stock may lose foreign tax credits if the lease produces a tax loss for the year and the cars are used outside the United States. Some lessors have required railroads which lease the cars from them to agree to indemnify them for these adverse tax consequences. This has deterred these railroads from allowing the lease-financed rolling stock to be used outside the United States.

The Act provides that the income or loss from the rental to a railroad of rolling stock placed in service after the date of enactment is to be U.S. source income or loss if the rolling stock is not used outside the United States except on a temporary basis not expected to exceed 90 days in any taxable year. At the election of the lessor, the provision also applies to railroad rolling stock placed in service on or before the date of enactment. This modification of the source rules for the rental of rolling stock would prevent the potential loss of lessors' foreign tax credits and would permit lessees to be more flexible in their utilization of the rolling stock outside the United States.

Sec. 371. Product Liability Net Operating Losses

Under present law, net operating losses incurred in a taxable year generally may be "carried back" and offset against taxable income of the 3 years first preceding the year of loss and, if not fully absorbed, "carried forward" and offset against taxable income of the 7 years next succeeding the year of loss.

Under the Act, the portion of a net operating loss that is attributable to a product liability loss could be carried back to the 10 years first preceding the loss year and carried forward to the next 7 years succeeding the loss year. A taxpayer may elect not to apply this special carryback rule. Under the Act, product liability losses include the liability for damages under product liability claims and the expenses directly incurred in the investigation or settlement of, or opposition to, product liability claims. The definition of product liability in the Act does not include liabilities arising under warranties, which essentially are contract liabilities. Nor does the definition include liabilities related to services performed by the taxpayer. The Act makes it clear that a product liability risk may be taken into account as a business need for which earnings and profits may be retained to a reasonable extent without imposition of the tax on unreasonable accumulation of earnings. The Act applies with respect to taxable years beginning after September 30, 1979.

Sec. 372. Accounting for Magazines, Paperbacks, and Records Returned After the Close of the Taxable Year

Under present law, sellers of merchandise who use an accrual method of accounting generally must include sales proceeds in income for the taxable year when all events have occurred which fix the right to receive the income and when the amount can be determined with reasonable accuracy. The Internal Revenue Service has taken the position that accrual-basis publishers and distributors of magazines, paperbacks, or records must include the sales proceeds of these items in income when they are shipped to purchasers, and may reduce income

for returns only in the year the items actually are returned unsold by the purchasers.

The Act permits an accrual-basis publisher or distributor of magazines, paperbacks, or records to elect to exclude from income amounts attributable to items returned within 2 months and 15 days (in the case of magazines) or 4 months and 15 days (in the case of paperbacks and records) after the close of the taxable year in which the sales of the items were made.

This provision applies to taxable years beginning after September 30, 1979.

Sec. 373. Accounting for Qualified Discount Coupons Redeemed After the Close of the Taxable Year

Under Treasury regulations specifying the appropriate taxable year for inclusion of income items, accrual-basis issuers of premium coupons with sales may reduce gross receipts by the estimated cost of redeeming such coupons outstanding at the close of the taxable year (plus the cost of redeeming coupons during the taxable year that have not previously been taken into account). The term "premium coupons" is not defined in the regulation, and the courts have not directly addressed the question of what constitutes a premium coupon. The Internal Revenue Service has issued two revenue rulings that deny the application of the regulation to two types of coupons which give consumers "cents off" or other discounts on the purchase price of specified merchandise.

The Act provides a special accounting rule allowing certain issuers of qualified discount coupons to deduct for a taxable year the cost of redeeming qualified discount coupons which are both outstanding at the close of the taxable year and redeemed within six months after the close of the taxable year, plus the cost (if not previously taken into account) of redeeming discount coupons received during the year. (This rule only applies to discount coupons and does not affect the tax treatment of premium coupons.) Also, the Act allows taxpayers who, in prior years, have accounted for discount coupons under the existing premium coupon regulation to elect to treat their method of accounting as a proper method for those years.

This provision is effective for taxable years ending after December 31, 1978.

TITLE IV—CAPITAL GAINS; MINIMUM TAX; MAXIMUM TAX

A. CAPITAL GAINS PROVISIONS

Sec. 401. Repeal of Alternative Tax for Noncorporate Capital Gains

Under prior law, in lieu of taxing 50 percent of net capital gains at the regular rates, a noncorporate taxpayer could apply a partial alternative tax of 25 percent on the first $50,000 of such gain if this resulted in a lower tax than that produced by the regular method. The balance of the net capital gain that was included in income was subject to the regular tax rate.

For taxable years beginning after December 31, 1978, the Act repeals the alternative tax for noncorporate capital gains.

Sec. 402. Increased Capital Gains Deduction for Individuals

The Act increases the amount of any net capital gain which a noncorporate taxpayer may deduct from gross income from 50 to 60 percent. The remaining 40 percent of the net capital gain is includible in gross income and subject to tax at the regular rates. The deducted gain is classified as a tax preference item for alternative minimum tax purposes, but not for purposes of reducing the amount of personal service income which is eligible for the maximum tax. A corresponding increase in the capital gains tax preference also is made for November and December 1978 capital gains under the add-on minimum tax. The increase in the capital gains deduction, the elimination of the maximum tax offset, and the increase in the capital gains tax preference are effective for taxable transactions occurring, and installment payments received, after October 31, 1978.

Sec. 403. Reduction of Corporate Alternative Capital Gains Tax

The Act reduces the alternative tax rate on corporate capital gains from 30 to 28 percent. The minimum tax preference of corporate long-term capital gains will be 18/46 of the gain. This change is effective with respect to taxable transactions occurring, and installment payments received, after December 31, 1978.

Sec. 404 One-Time Exclusion of Gain on Sale of Residence

Under present law, the entire amount of gain or loss realized on the sale or exchange of property generally is recognized. However, under a rollover provision of the Code, gain is not recognized on the sale or exchange of a taxpayer's principal residence if a new principal residence, at least equal in cost to the adjusted sales price of the old residence, is purchased and used by the taxpayer within the replace-

ment period. In addition, under prior law, an individual who had attained the age of 65 could elect to exclude from gross income, on a one-time basis, the entire gain realized on the sale of his or her principal residence if the adjusted sales price was $35,000 or less. If the adjusted sales price exceeded that amount, the amount excludible was that portion of the gain which was determined by multiplying the total gain by a fraction, the numerator of which was $35,000, and the denominator of which was the adjusted sales price of the residence.

The Act repeals the provision which relates to the exclusion of gain on the sale of a residence by an individual who has attained the age of 65. It provides instead that an individual who has attained the age of 55 may exclude from gross income, on a one-time elective basis, up to $100,000 of gain from the sale of his or her principal residence. (In the case of a jointly-owned residence, only one spouse must have attained the age of 55.) This exclusion will be available only in the case of gain from the sale of the principal residence which the taxpayer owned and occupied as his or her principal residence for a period aggregating 3 out of the 5 years which precede the sale. (However, a special transition rule is provided by the Act for individuals eligible under the prior law test.) The election for the $100,000 exclusion, which is effective for sales or exchanges after July 26, 1978, must be made in accordance with regulations prescribed by the Secretary.

The Act also provides that gain realized on the sale of a taxpayer's principal residence after July 26, 1978, is not an item of tax preference. under the minimum tax.

Sec. 405. Rollover of Gain on Sale of Residence in a Job-Related Move

Under present law, gain realized on the sale of a taxpayer's principal residence generally is not recognized to the extent the adjusted sales price is reinvested in a new residence. This provision applies where the taxpayer purchases and uses a new principal residence within a period beginning 18 months before and ending 18 months after the sale of the old principal residence. Only the last principal residence purchased and used during the replacement period constitutes the replacement residence for purposes of the rollover provision.

The Act generally provides that taxpayers may use the rollover provision more than one time within the replacement period if the individual relocates for employment purposes. This change is effective only in the case of taxpayers who had a reasonable expectation at the time of the relocation that they would work at the new location for a substantial period of time. The provision applies to both employees and self-employed individuals, and is effective for sales and exchanges of principal residences after July 26, 1978.

B. MINIMUM TAX PROVISIONS

Sec. 421. Alternative Minimum Tax for Individuals

Present law imposes a minimum tax on certain individual and corporate tax preferences. The minimum tax for individuals amounts to 15 percent of the sum of an indivdual's (or estate's or trust's) tax preferences in excess of one-half of regular income taxes paid or, if greater, $10,000.

The tax preference items included in this base of the minimum tax for individuals are:

(1) Accelerated depreciation on real property in excess of straight-line depreciation;

(2) Accelerated depreciation on leased personal property in excess of straight-line depreciation;

(3) Amortization of certified pollution control facilities (the excess of 60-month amortization (sec. 169) over depreciation otherwise allowable (sec. 167));

(4) Amortization of railroad rolling stock (the excess of 60-month amortization (sec. 184) over depreciation otherwise allowable (sec. 167));

(5) Qualified stock options (the excess of the fair market value at the time of exercise over the option price);

(6) Percentage depletion in excess of the adjusted basis of the property;

(7) The deduction for 50 percent of net long-term capital gains;

(8) Amortization of child care facilities (the excess of 60-month amortization (sec. 188) over depreciation otherwise allowable (sec. 167));

(9) Itemized deductions (other than medical and casualty loss deductions) in excess of 60 percent of adjusted gross income; and

(10) Intangible drilling costs on oil and gas or geothermal wells in excess of the amount amortizable with respect to those costs and, for 1977, in excess of net income from oil and gas or geothermal production.

The Act retains the present law minimum tax with respect to all preference items except capital gains and excess itemized deductions. The Act provides for an alternative minimum tax which is payable by an individual to the extent that the alternative tax exceeds the regular income tax increased by the amount of the existing minimum tax, as revised, on preference items other than capital gains and itemized deductions.

The alternative minimum tax base is the sum of an individual's taxable income, adjusted itemized deductions, and the capital gains deduction.

The following rates are imposed on this amount:

	Percent
$0–$20,000	0
$20,000–$60,000	10
$60,000–$100,000	20
Over $100,000	25

The foreign tax credit and refundable credits are the only tax credits which are allowed against any alternative minimum tax liability.

The capital gains preference is increased from 50 percent to 60 percent of the net capital gain. (This change also is made for 1978 under the minimum tax for the part of the year for which the 60 percent deduction applies.) However, gain from the sale of principal residences is not included as a preference item under the alternative minimum tax (or under the add-on minimum tax for sales after July 26, 1978).

Itemized deductions subject to the preference exclude medical and casualty deductions (as under present law) as well as State and local tax deductions and, in the case of income in respect of decedents, amounts deducted (under sec. 691(c)) for estate taxes. The remaining itemized deductions are preferences to the extent they exceed 60 percent of adjusted gross income minus the medical and casualty deductions, State and local tax deductions, and the estate tax deduction previously described.

Special rules are provided to restore certain credit carryovers and for charitable contributions from certain trusts.

In general, these changes are effective for taxable years beginning after 1978. In addition, the provision is not to be treated as a change of the tax rate (under sec. 21 of the Code). Consequently, fiscal year taxpayers are to be first subject to the alternative minimum tax for their taxable years beginning in 1979. The provisions changing the effective date for the capital gains preference (to 60 percent of net capital gain) for purposes of the present minimum tax is to apply for all taxable transactions taking place after October 31, 1978.

Sec. 422. Minimum Tax Treatment of Intangible Drilling Costs

Under prior law, the deduction for intangible drilling costs (IDCs) in excess of the deduction which would have been allowed with respect to those costs for that year through either 10-year amortization or cost depletion was treated as a tax preference item for purposes of the minimum tax for individuals. In the Tax Reduction and Simplification Act of 1977, the Congress provided that for taxable years beginning only in 1977 IDCs (over the amount which would have been allowable under either 10-year amortization or cost depletion) in excess of oil and gas production income would constitute a tax preference item.

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The Act makes permanent the IDC preference adopted for 1977 by the Tax Reduction and Simplification Act. Thus, IDCs will be includible in an individual's minimum tax base only to the extent that those costs, over the portion of those costs amortizable on the basis of a 10-year life or under cost depletion, exceed the taxpayer's net income from oil and gas (or geothermal) properties.

The Act also clarifies the treatment of dry hole costs on properties with no gross income from oil or gas production.

Sec. 423. Amendment to Definition of Foreign Source Capital Gain Tax Preference

Under present law (sec. 58(g)(2)), the deducted amount of net capital gains which are attributable to sources within any foreign country or possession is not treated as a preference item if capital gains do not receive preferential treatment under the laws of the foreign country or possession. The Act generally modifies this exception so that preferential treatment will also not be considered to be accorded in certain limited situations involving capital gains on certain reorganizations of corporations which are treated as taxable for U.S. tax purposes but as nonrecognition transactions in the foreign country or possession in which the corporation's business is primarily carried on and in which the transaction takes place. This provision takes effect on the date of enactment of the Act.

C. MAXIMUM TAX PROVISIONS

Sec. 441. Capital Gains Tax Preference Offset

Under present law, the highest marginal tax rate applicable to personal service income is 50 percent. However, the amount eligible for this maximum tax rate is reduced dollar-for-dollar by the individual's items of tax preference.

The Act removes capital gains as a tax preference which reduces the amount of personal service income eligible for the maximum tax rate. This change generally is effective with respect to taxable years beginning after October 31, 1978. In the case of taxable years beginning before November 1, 1978, and ending after October 31, 1978, the change is effective with respect to so much of the taxpayer's net capital gain as is attributable to post-October 31, 1978 taxable transactions and installment payments.

Sec. 442. Limitation on Personal Service Income

The maximum tax rate on personal service income (i.e., wages, salaries, fees, etc.) generally is 50 percent. Under prior law, in the case of an individual engaged in a trade or business where both personal services and capital are material income producing factors, a reasonable allowance for personal services is treated as personal service income, but this amount cannot exceed 30 percent of the income from the business.

Effective for taxable years beginning after December 31, 1978, the Act eliminates the 30-percent limitation on the amount of income from a trade or business that can be treated as personal service income for maximum tax purposes where capital is a material income producing factor. Individuals will receive the benefits of the maximum tax for income that constitutes reasonable compensation for services rendered.

TITLE V—OTHER TAX PROVISIONS

A. ADMINISTRATIVE PROVISIONS

Sec. 501. Reporting Requirements With Respect to Charged Tips

Present law requires an employee to report tips received to his or her employer, including tips added to a waiter's check by a charge customer and paid over to the waiter by the employer. The employer must report to the Internal Revenue Service (on Form W–2) both tips actually reported to the employer by the employee and, under IRS rulings issued in 1975 and 1976, any charge account tips not reported to the employer by the employee. In section 2111 of the Tax Reform Act of 1976 (P.L. 94–455), the Congress prohibited the IRS from following, prior to 1979, its 1975 and 1976 rulings on employer reporting of charge account tips.

The Act provides that the only employee tips which an employer must report to the IRS are those reported to the employer by employees. Also, the Act provides that, with respect to the amount of tips paid to a particular employee, the only records of charged tips which an employer may be required to keep are charge receipts and copies of tip statements furnished by employees. These rules apply to payments made after December 31, 1978.

Sec. 502. Tax Court Small Tax Case Procedure and Authority of Commissioners

Under prior law, cases involving income, estate or gift tax deficiencies of less than $1,500 may, at the taxpayer's option, be tried under the small tax case procedures of the Tax Court. These trials are conducted informally and neither the taxpayer nor the IRS may appeal the decision. Typically, these small tax cases are tried by commissioners appointed by the chief judge of the Tax Court. Following the trial, the commissioners file written reports of their findings and conclusions of law, and decisions based on these reports are made by the chief judge.

The Act increases the jurisdictional amount for electing the small tax case procedure from $1,500 to $5,000. In addition, it specifically authorizes commissioners to administer oaths, issue subpoenas, examine witnesses, prepare reports, and make decisions in such cases.

The provision of the Act increasing the jurisdictional amount in small tax cases from $1,500 to $5,000 is effective on the first day of the first calendar month beginning more than 180 days after the date of the enactment of the Act. The provisions of the Act relating to the powers of commissioners is effective on the date of enactment.

Sec. 503. Disclosure of Tax Return Information to the Department of Justice in Tax Administration Matters

Under present law, in tax administration matters, returns and return information are generally made available to attorneys of the Department of Justice (including United States attorneys) in preparation for any proceeding (or investigation which may result in such a proceeding) before a Federal grand jury or any Federal or State court. One of the requirements to be met before the return is made available in these situations is that the taxpayer whose return is the subject of disclosure either be or may be a party to the proceeding involved. The return of a third party could also be made available to the Department of Justice in preparation for tax proceedings where the third party's return or return information relates or may relate to a transaction between the third party and the taxpayer whose tax liability is or may be at issue, and the return information pertaining to the transaction may affect the resolution of an issue of the taxpayer's liability. The disclosure of a third party return in a tax proceeding is subject to the same transactional tests, described above, except that the transactions must have a direct relationship to the resolution of an issue of the taxpayer's liability.

The Act modifies present law in three respects. First, the return of a taxpayer who is not a party to the proceeding may be made available to the Department of Justice if the proceeding arose out of, or in connection with, determining the taxpayer's civil or criminal tax liability or the collection of civil tax liability. The second modification makes it clear that disclosures of third party returns made to the grand jury in tax cases are investigative disclosures and, thus, not subject to the more restrictive requirements applicable to disclosures of third party returns in tax proceedings. The third modification allows disclosure of returns to officers and employees of the Department of Justice, rather than just the attorneys of the Department of Justice. These modifications apply to disclosures made after December 31, 1978.

Sec. 504. Refund Adjustments for Amounts Held Under Claim of Right

If a taxpayer includes in income for a prior year an amount received or accrued under a "claim of right," and it is determined in a later year that no right to the income existed, then a deduction may be allowed for the amount previously included in income. The tax benefit (i.e., reduction in current year taxes) that is attributable to this deduction is the greater of the tax reduction that would be realized by treating the item as a deduction in (1) the year it originally was included in income, or (2) the subsequent year in which it was discovered that the right to the income did not exist. If the greater tax benefit is realized by treating the item as a deduction in the prior year, the tax benefit may be greater than the entire tax liability otherwise due in the current year. If that is the case, the excess benefit is

treated as an overpayment of tax and is refundable. Under present law, however, this refund may take anywhere from several months to several years to receive, since it is treated as an overpayment of tax for the current year and could be subject to audit along with the current year's return.

The Act allows a taxpayer to apply for a "quickie" refund of an overpayment of taxes in the current year, to the extent that the overpayment is attributable to the extra tax benefit realized by treating a "claim of right" deduction as an adjustment to income of a prior year. The provision applies to refund claims filed after the date of enactment.

B. ESTATE AND GIFT TAX PROVISIONS

Sec. 511. Jointly-Owned Farms and Closely Held Businesses

In general, for estate tax purposes, the value of a joint tenancy with rights of survivorship is included in the joint tenant's gross estate except for the portion of the value shown to be attributable to consideration furnished by the surviving joint tenant. The Act provides a special rule for excluding a portion of the value of certain jointly-owned property used in a farm or other business. The exclusion is based on the number of years the surviving joint tenant materially participated in the business. The provision applies only to a joint interest in property held by a husband and wife.

The amount excludable would be determined by applying a percentage rate of 2 percent for each year the surviving spouse materially participated in the business (not to exceed 50 percent) to the excess of the value of the joint interest over the amount attributable to the original consideration furnished. In addition, the amount attributable to the original consideration furnished by the surviving spouse would be excludable. For this purpose, the amount attributable to the original consideration would consist of the amount of that consideration plus assumed appreciation at the rate of 6 percent simple interest for the period of investment of the consideration.

The amount by which the value of a joint interest includible in the gross estate may be reduced is limited to $500,000.

The provision is to apply if elected by the executor of the estate not later than the time for filing the estate tax return (including extensions) and in the manner prescribed under Treasury regulations.

The provision is to apply with respect to estates of decedents dying after December 31, 1978.

Sec. 512. Attribution Rules for Extension of Time to Pay Estate Tax

Under present law, a 15-year period is provided for the payment of the estate tax attributable to the decedent's interest in a closely-held business (including a farm). In order to qualify for this treatment, the value of the closely-held business (or businesses) in the decedent's estate must exceed 65 percent of the value of the gross estate reduced by allowable expenses, indebtedness, and losses. The provision applies with respect to an interest as sole proprietor in a trade or business; an interest as a partner in a partnership having not more than 15 partners, or in which the decedent owned 20 percent or more of the capital; or ownership of stock in a corporation having not more than 15 shareholders, or in which the decedent owned 20 percent or more in value of the voting stock.

The Act applies attribution rules for purposes of determining the number of shareholders in a corporation or partners in a partnership in determining eligibility for the 15-year extended payment provision

for estate tax attributable to a closely-held business. Stock or partnership interests held by the decedent's family (e.g., father, mother, spouse, brothers, sisters, and descendants) will be treated as held by a single shareholder or partner, as the case may be.

In addition, the Act allows an executor to elect to apply the family attribution rules in order to determine whether at least 20 percent of the capital interest or value of voting stock in a business is included in the decedent's gross estate. However, in the case of stock, this attribution provision may be elected only if there was no market on a stock exchange or in an over-the-counter market for it at the time of the decedent's death. If an executor makes an election under the provision relating to the 20-percent capital interest or value of voting stock requirement, then the extended payment period for the estate tax due with respect to that estate cannot exceed 10 years, and the special 4 percent interest rate for closely held business interests will not apply.

This provision applies with respect to the estates of decedents dying after the date of the enactment of the Act.

Sec. 513. Subordination of Special Liens for Estate Tax Attributable to Special Valuation Property

Under present law, the Internal Revenue Service may agree to the subordination of a prior tax lien to a subsequent security interest if certain conditions are satisfied (i.e., an amount equal to the security interest is paid over or the Service believes that subordination of the tax lien would increase the amount ultimately realizable). The Act permits the subordination of the special lien for the recapture of the estate tax savings attributable to the special valuation of farm or closely held business real property. The special lien may be subordinated if the Secretary of the Treasury is satisfied that the interests of the United States are protected adequately after subordination. The provision applies with respect to estates of decedents dying after December 31, 1976.

Sec. 514. Time to Amend Governing Instruments of Charitable Split Interest Trusts

The Tax Reform Act of 1969 imposed new requirements that must be met in order for a charitable deduction to be allowed for income, gift, and estate tax purposes for the transfer of a split interest to charity (i.e., part charitable and part noncharitable). In the case of a remainder interest in trust, the interest passing to charity must be in either a charitable remainder annuity trust, a charitable remainder unitrust, or a pooled income fund. In the case of an "income" interest passing to charity (i.e., a charitable lead trust), the "income" interest must be either a guaranteed annuity or a fixed percentage of the fair market value of the trust (determined at least annually).

Congress provided, as early as 1974, that the governing instruments of charitable remainder trusts could be amended to meet the new rules within certain time limitations for estate tax purposes. The latest extension of these time limitations was made by the Tax Reform Act of 1976 which permitted amendment of charitable remainder trusts until December 31, 1977, in order to qualify the trust for the charitable estate tax deduction. However, it provided this relief only in the case of the charitable deduction for estate tax purposes and only for remainder

interests passing to charity. No relief was provided for the charitable deduction for income or gift tax purposes or for "income" interests passing to charity for income, gift, or estate tax purposes.

The Act extends until December 31, 1978, the time to amend (or to commence judicial proceedings to amend) instruments establishing charitable remainder trusts which were executed before December 31, 1977, to comply with the requirements of the Tax Reform Act of 1969 in order for a charitable deduction to be allowed for estate tax purposes. The Act also provides that instruments establishing charitable lead trusts and charitable remainder trusts in the case of income and gift taxes, which were created (or executed in the case of charitable lead trusts for estate tax purposes) before December 31, 1977, could be amended to comply with the requirements of the 1969 Act if the instrument is amended (or judicial proceedings to amend are commenced) by December 31, 1978.

Sec. 515. Deferral of Carryover Basis Rules

Under the Tax Reform Act of 1976, the basis of property passing from a decedent is "carried over" from the decedent to the estate or heir. Adjustments to basis are made for death taxes, pre-1977 appreciation, and a $60,000 minimum basis. The provision was to apply with respect to property passing from decedents dying after December 31, 1976.

The Act postpones the effective date of the carryover basis provisions so that they will only apply to property passing from decedents dying after December 31, 1979.

C. EXCISE TAX PROVISIONS

Sec. 520. Reduction of Excise Tax on Private Foundation Investment Income

Private foundations are subject to an annual excise tax on net investment income, defined as the sum of gross investment income and the full amount of net capital gains, reduced by expenses paid or incurred in earning the gross investment income. Gross investment income includes interest, dividends, rents, and royalties, but does not include taxable business unrelated income.

The Act reduces the rate of this tax from 4 percent to 2 percent for taxable years beginning after September 30, 1977.

Sec. 521. Excise Tax on Certain Gaming Devices

There is an annual Federal excise tax of $250 on each slot machine or other coin-operated gaming device. Under prior law, up to 80 percent of the Federal tax could be offset by similar State taxes. Under the Act, the available State credit is increased from 80 percent to 95 percent of the Federal tax for years ending June 30, 1979, and June 30, 1980. The Federal excise tax is repealed after June 30, 1980.

Sec. 522. Treatment of Certain Private Foundations for Purposes of Section 4942

Under present law, the term "private foundation" means any charitable, educational, religious, or other organization described in section 501(c)(3), other than certain specified categories of organizations (sec. 509(a) of the Code). These categories (known as "public charities") include churches, schools, hospitals, or certain medical research organizations, certain other organizations which receive specified "public" support, and organizations which are "supporting" organizations to other public charities. For this purpose, under Treasury regulations, the term "hospital" does not include "convalescent homes or homes for children or the aged, nor does the term include institutions whose principal purpose or function is to train handicapped individuals to pursue some vocation" (Reg. sec. 1.170A–9(c)(1)).

In addition to other restrictions on private foundations, a private foundation is required to make annual expenditures or distributions for exempt purposes generally equal to the net income of the private foundation. However, an exception to this rule is provided for certain private foundations known as "operating foundations." A private foundation may qualify as an "operating" foundation if it spends directly for the active conduct of its exempt-purpose activities amounts which are at least equal to 85 percent of its adjusted net income, and which are at least equal to 3⅓ percent of its net endowment assets, or if the foundation meets certain other tests (sec. 4942(j)(3)).

The Act provides that, for purposes only of the distribution requirements of section 4942, an "operating foundation" includes a private

foundation which, on May 26, 1969, and continuously thereafter to the close of the taxable year, operates and maintains as its principal functional purpose facilities for the long-term care, comfort, maintenance, or education of permanently and totally disabled persons, elderly persons, needy widows, or children if the foundation meets the distribution requirements applicable to operating foundations (sec. 4942(j)(3)(B)(ii)). The provision is effective for taxable years beginning after December 31, 1969.

D. OTHER TAX PROVISIONS

Sec. 530. Employment Tax Status of Individuals as Independent Contractors or Employees

With certain limited statutory exceptions, the classification of particular workers or classes of workers as employees or independent contractors (self-employed persons) for purposes of Federal employment taxes must be made under common law rules. A determination of an employer-employee relationship is important because a certain amount of wages paid to employees generally is subject to social security taxes imposed on the employer and the employee under the Federal Insurance Contributions Act (FICA) and unemployment taxes imposed on the employer under the Federal Unemployment Tax Act (FUTA). On the other hand, payments to independent contractors are subject to the tax on self-employment income (SECA). In addition, Federal income tax must be withheld from compensation paid to employees, but payments to independent contractors are not subject to withholding.

Generally, the basis for determining whether a particular worker is an employee or an independent contractor is the common law test of control. Under Treasury regulations, if a person engaging the services of another has "the right to control and direct the individual who performs the services, not only as to the result to be accomplished by the work, but also as to the details and means by which the result is accomplished," the relationship of employer and employee is deemed to exist. On the other hand, the absence of a right to control generally indicates that the person performing the services is an independent contractor. In interpreting the Treasury regulations, twenty factors are used in determining whether workers are employees or independent contractors.

The Act provides an interim solution for controversies between the Internal Revenue Service and taxpayers involving whether certain individuals are employees under interpretations of the common law. Eligible taxpayers are relieved of all liability for Federal income tax withholding, social security (FICA) taxes, and unemployment (FUTA) taxes with respect to their workers for any period ending before January 1, 1979, provided the taxpayers had a reasonable basis for not treating the workers as employees.

Generally, the Act grants relief if a taxpayer can demonstrate a reasonable basis for treating workers as other than employees.

In addition, the Act establishes three types of statutory reasonable basis standards which constitute "safe havens," and thus, when met, qualify a taxpayer for exemption from employment tax liability.

The first statutory reasonable basis standard is met if a taxpayer's treatment of an individual as not being an employee for a period was due to reasonable reliance on judicial precedent, published rulings, technical advice with respect to the taxpayer, or a ruling (for example, a "letter ruling," or a "determination letter") issued to the taxpayer.

Under the second statutory "safe haven" standard, a taxpayer shall be treated as satisfying the reasonable basis test for the treatment of an individual for employment tax purposes, by showing reasonable reliance on a past Internal Revenue Service audit of the taxpayer.

The third statutory method for a taxpayer to establish a reasonable basis for the treatment of an individual as other than an employee is to show that such treatment coincided with a long-standing, recognized practice of a significant segment of the industry in which the individual whose status is at issue was engaged.

In order to minimize taxpayers' uncertainty about the proper treatment of workers for employment tax purposes during 1979, when the Congress intends to work to develop a comprehensive, permanent solution to these controversies, the Act also relieves taxpayers prospectively through December 31, 1979, of potential liabilities based on employment status classifications, unless the taxpayers have no reasonable basis for not treating the workers as employees. In order to qualify for prospective relief for 1979, taxpayers must file all required Federal tax returns (including information returns) after December 31, 1978.

In addition, the Act prohibits the Department of the Treasury (including the Internal Revenue Service) from publishing any regulation or Revenue Ruling with respect to individuals' employment tax status under the common law after enactment of this legislation and before January 1, 1980, or the effective date of any legislation clarifying the employment tax status of individuals, whichever is earlier.

This provision of the Act becomes effective upon enactment and terminates after December 31, 1979.

Sec. 531. Tax Treatment of Cooperative Housing Corporations

Under present law, a tenant-stockholder in a cooperative housing corporation is entitled to deduct amounts paid to the corporation which represents his or her proportionate share of allowable real estate taxes and interest relating to the corporation's land and buildings. In addition, to the extent a tenant-stockholder uses depreciable property leased from the cooperative housing corporation in a trade or business or for the production of income, the tenant-stockholder is allowed to take depreciation deductions with respect to the stock the ownership of which gives the tenant-stockholder the right to lease such propery. In general, for an organization to qualify to pass through these deductions to tenant-stockholders, 80 percent or more of the gross income of the cooperative housing corporation must have been derived from individual tenant-stockholders.

The Act provides that if a person (including a corporation) who conveys the houses, apartment building, or leasehold thereof to a cooperative housing corporation acquires stock in the corporation by purchase or foreclosure, together with a lease or right to occupy the house or apartment, such person would be treated as a tenant-stockholder for up to three years from the date of acquisition. This provision would apply even though such person or any purchaser from such person could not occupy the apartment or house without prior approval of the corporation or its managing agent. This provision is effective for stock acquired after the date of enactment.

Sec. 540. Source of Interest Income on Deposits in Puerto Rican Branches of U.S. Savings and Loan Associations

Generally, interest received from a U.S. corporation is treated entirely (or, in some cases, partially) as U.S. source income and thus does not qualify for the special tax treatment for Puerto Rican source income provided to Puerto Rican residents and possessions corporations (under secs. 933 and 936). However, interest on deposits with a foreign branch of a U.S. commercial bank, including a branch located in Puerto Rico, is treated as income from sources within that foreign locality. Consequently, interest paid by Puerto Rican branches of U.S. commercial banks generally qualifies for the special treatment provided Puerto Rican residents and possessions corporations. Under prior law, this exception for foreign branches of U.S. banks did not extend to similar branches of U.S. savings and loan associations. As a result, it was not clear how interest paid by certain savings and loan associations which operate in Puerto Rico but are incorporated in the United States were treated under prior law for purposes of the special Puerto Rican provision.

The Act extends the special source rule for interest on deposits in foreign branches of U.S. commercial banks to interest on deposits in similar branches of U.S. savings and loan associations. This change makes it clear that interest from Puerto Rican branches of U.S. savings and loan associations will be treated as Puerto Rican source income and thus will qualify for special treatment afforded Puerto Rican source income. The amendment is effective for taxable years of recipients of the interest beginning after the date of enactment.

Sec. 541. Taxation of Alaska Native Claims Settlement Act Corporations

Corporations formed pursuant to the Alaska Native Claims Settlement Act (ANCSA) received money from the United States and the right to select Alaskan land. Many of the tax aspects of transactions of these corporations are unclear.

The Act provides that ANCSA corporations (1) do not include in income the value of outside surveys to assist the corporations in making their land selections; (2) may deduct land selection costs; (3) are deemed to have begun business and may therefore deduct ordinary and necessary expenses; and (4) are not personal holding companies. The amendment is effective as of December 18, 1971. The survey income provision would remain in effect until the earlier of 1991 or the date the corporation has received all its land under ANCSA. The personal holding company provision would remain in effect until 1991.

Sec. 542. Involuntary Conversion of Livestock

Under present law, taxpayers may elect not to recognize gain realized on the involuntary conversion of certain property if property similar or related in service or use to the property converted is acquired by the taxpayer within the replacement period. In the case of involuntarily converted livestock, the replacement property satisfies the "similar or related in service or use" requirement for nonrecognition of gain only if the new livestock is functionally the same as that converted.

The Act provides that gain realized on the involuntary conversion of livestock, due to environmental contamination, can be rolled over into other farming property (including farm land). This provision is effective for taxable years beginning after December 31, 1974.

Sec. 543. Exclusion for Certain Cost-Sharing Payments

The Act provides an exclusion from gross income in the case of certain payments received under a number of Federal and State cost-sharing conservation programs. No deduction or credit may be claimed with respect to amounts excluded under the Act, and the basis of any property acquired or improved with these payments would not reflect the excluded amounts. A special rule is provided for the recapture of excluded amounts where the property, or improvements, purchased with the payments are disposed of before the end of the expiration of 20 years. In addition to the above qualifications, a payment (or a portion of a payment) will be excluded from income only if the Secretary of the Treasury determines that the payment will not increase substantially the annual income from the property with respect to which the payment is made.

This provision is effective with respect to grants made after September 30, 1979.

E. TAX STUDIES

Sec. 551. Study of Simplification of Tax Returns

The Act requires the Secretary of the Treasury to conduct a study concerning: (1) provisions of the Internal Revenue Code of 1954 which, due to their complexity, may hamper the ability of individuals to prepare accurate and complete Federal income tax returns, and (2) methods of simplifying Federal income tax return forms and instructions. The Secretary is to establish a task force to assist him in the conduct of this study and may use graphic and communication experts; as many as 10 employees may be appointed by the Secretary to carry out the functions of the task force. The Secretary is required to submit a final report, together with such legislative recommendations he finds necessary, to the Senate Finance Committee and House Ways and Means Committee, no later than two years after the date of enactment of this Act.

Sec. 552. Study of Tax Treatment of Certain Government-Mandated Expenditures

The Act requires the Treasury Department to conduct a study on the appropriateness of providing additional tax incentives (including the feasibility of providing a 5-year amortization period) in the case of expenditures required by the Occupational Safety and Health Act (OSHA), and the Mining Safety and Health Administration of the Department of Labor.

A report on the Treasury study, together with legislative recommendations, is to be submitted, before April 1, 1979, to the House Ways and Means Committee and to the Senate Finance Committee.

Sec. 553. Study of Taxation of Foreign Investors' Transactions in U.S. Real Estate

Under present law, nonresident aliens and foreign corporations are subject to special rules for taxation of income from U.S. real estate investments not connected with an active business in the United States. Under the Code and certain tax treaties, foreign investors generally are subject to little or no U.S. taxes on U.S. real estate transactions.

The Act directs the Treasury Department to submit a study to Congress within 6 months of the date of enactment on the taxation of foreign owners of U.S. property for the purpose of determining the appropriate tax treatment of income or gain from U.S. property.

Sec. 554. Report on Effectiveness of Jobs Credit

The Act requires the Secretaries of Treasury and Labor to submit a report, no later than June 30, 1981, to the House Ways and Means Committee and the Senate Finance Committee, on the effectiveness of the targeted jobs credit in improving the employment situation of the targeted groups, and the types of employers claiming the credit. The report also is to include an evaluation of the effectiveness of the prior law general jobs credit in stimulating employment and enhancing economic growth, and the types of employers claiming such credit.

Sec. 555. Study of Effects of Capital Gains Tax Changes

The Act requires the Secretary of the Treasury to submit to the House Ways and Means Committee and to the Senate Finance Committee a report on the effectiveness of the Act's changes in the tax treatment of capital gains in stimulating investment and increasing the rate of economic growth. The report, which must be submitted not later than September 30, 1981, also is to include an analysis of the effects of these changes on employment growth and income tax revenues.

TITLE VI—GENERAL STOCK OWNERSHIP CORPORATIONS

Sec. 601. Tax Treatment of General Stock Ownership Corporations and Their Shareholders

Under prior law, there were no special provisions relating to the establishment of a private corporation for the benefit of the residents of a State.

The Act authorizes a State to establish a General Stock Ownership Corporation ("GSOC") for the benefit of its citizens. In order to qualify for the special treatment accorded GSOCs, its charter must meet certain statutory requirements, and the GSOC must make an irrevocable election. If a GSOC meets these requirements, it is not subject to Federal income tax. Instead, the shareholders of the GSOC are taxable on their daily prorated share of the GSOC's taxable income. The GSOC computes its taxable income in the same manner as a regular corporation, but it is not eligible for the dividends-received deduction. Also, the GSOC's losses do not flow through to its shareholders. However, such losses are allowed as a 10-year net operating loss carryforward.

The GSOC is also required to distribute to its shareholders 90 percent of its taxable income. Such distributions are tax-free when received by the GSOC shareholders to the extent they have been previously taxed to them. The GSOC is required to withhold 25 percent of every shareholder distribution.

The provisions apply with respect to such corporations chartered after December 31, 1978, and before January 1, 1984.

TITLE VII—TECHNICAL CORRECTIONS TO THE TAX REFORM ACT OF 1976

Secs. 701–703. Technical Corrections to the Tax Reform Act of 1976

The Act makes numerous technical, clerical, conforming, and clarifying amendments with respect to provisions enacted by the Tax Reform Act of 1976.[1] In general, each acendment is effective as of the effective date for the respective provision of the 1976 Act.

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[1] In general, these provisions were contained in a separate bill, H.R. 6715, passed by the House and reported by the Senate Finance Committee. Except for several changes incorporated in the Senate amendment to the Revenue Act of 1978, the relevant legislative history is contained in House Report No. 95–700 and Senate Report No. 95–1263.

TITLE VIII—AMENDMENTS RELATING TO THE SOCIAL SECURITY ACT

Sec. 801. Grants to States for Social Services

Under permanent law, the amount of Federal funding available to the States to match their expenditures for social services under title XX of the Social Security Act is limited to $2.5 billion per fiscal year. This ceiling on Federal funding for the program is allocated among the States on a population basis. For most services, funding is provided on a 75-percent Federal and 25-percent non-Federal basis to the extent possible within the ceiling.

In fiscal years 1977 and 1978, an additional $200 million amount was added to the permanent $2.5 billion ceiling. This additional amount was also allocated on a population basis. It was, however, available only for purposes of funding child care programs and was available on a 100-percent Federal basis (i.e., with no requirement of a non-Federal match).

The Act extends the temporary $200 million additional amount for one more year—through fiscal year 1979. As was the case in fiscal years 1977 and 1978, this $200 million is to be available only for child care and requires no non-Federal match. The Act also provides a further $200 million increase in the ceiling for fiscal 1979 which is available for social services generally and subject to the ordinary matching requirements of title XX.

The net effect of this provision is to raise the ceiling on Federal funding for title XX social services to $2.9 billion for fiscal year 1979. After fiscal year 1979, the ceiling will revert to its permanent level of $2.5 billion in the absence of further legislation.

Sec. 802. Changes in Public Assistance Matching Formula, and Increase in Amount of Public Assistance Dollar Limitations, for Puerto Rico, the Virgin Islands, and Guam in Fiscal Year 1979

Under the Social Security Act, public assistance programs of aid and services to the aged, blind, and disabled, and to families with dependent children are operated in the territories of Guam, Puerto Rico, and the Virgin Islands in accordance with State plans for these programs developed by the territories and approved by the Department of Health, Education, and Welfare. The costs incurred by the territories in carrying out those plans are partially reimbursed by the Federal government according to a matching formula and funding ceiling specified in the law. Under permanent law, the matching formula provides for 50 percent Federal participation up to a maximum per fiscal year of $24 million in Puerto Rico, $800,000 in the Virgin Islands, and $1.1 million in Guam.

The Act increases the matching rate and ceilings in fiscal 1979. The matching rate is increased to 75 percent, up to a maximum amount of Federal funding for the fiscal year of $72 million in Puerto Rico, $2.4 million in the Virgin Islands, and $3.3 million in Guam. In the absence of further legislation, the matching rate and limitations will revert to their permanent-law levels after fiscal year 1979.

APPENDIX I:

REVENUE EFFECTS OF TAX PROVISIONS OF THE REVENUE ACT OF 1978

Table I–1.—Estimated Revenue Effects of Tax Provisions of the Revenue Act of 1978 (H.R. 13511), Calendar Year Liabilities 1979–83*

Part A. Tax Reductions and Revisions

[Millions of dollars]

Provision	Calendar year liabilities				
	1979	1980	1981	1982	1983
Title I—Individual Income Tax Provisions					
A. Individual income tax reductions and extensions:					
Secs. 101 and 106—Widening tax brackets, rate cuts, increase in zero bracket amount	−11, 735	−13, 873	−16, 428	−19, 482	−23, 137
Repeal general tax credit	10, 397	10, 985	11, 618	12, 302	13, 039
Sec. 102—Increase in the personal exemption	−11, 681	−12, 382	−13, 125	−13, 913	−14, 747
Secs. 104 and 105—Increase in and simplification of the earned income credit[3]	−1, 029	−987	−949	−910	−873
B. Itemized deductions; unemployment compensation; credits:					
Sec. 111—Repeal of nonbusiness deduction for State and local taxes on gasoline and other motor fuels	1, 151	1, 358	1, 602	1, 890	2, 231
Sec. 112—Taxation of unemployment compensation benefits at certain income levels	251	261	259	263	268
Sec. 113—Political contributions	−20	−33	−20	−20	−20
Sec. 121—Child care credit for payments to related individuals	−35	−36	−37	−38	−39
C. Deferred compensation provisions:					
Sec. 131—State and local government deferred compensation plans	(4)	(4)	(4)	(4)	(4)
Sec. 132—Certain private deferred compensation plans					
Sec. 133—Deferred compensation payments to independent contractors					

*The revenue estimates in Part A are the tax reductions from levels which would have prevailed had the existing temporary tax cuts been extended. Thus, where the bill merely extends an expiring tax cut, the table does not show any revenue effect; and where the bill replaces an expiring tax cut with a new provision (such as substituting graduated corporate tax rates for the corporate surtax exemption), the revenue loss from the new provision is only the excess of its gross revenue loss over what the revenue loss would have been had the expiring provision been extended. A revenue gain is shown for failing to extend the general tax credit and general jobs tax credit. Part B shows the revenue losses which would have occurred had certain existing temporary tax provisions been extended through 1983, both the provisions actually extended in the bill and the provisions replaced by other provisions.

(Other footnotes are at the end of the table.)

[Millions of dollars]

Provision	Calendar year liabilities				
	1979	1980	1981	1982	1983
D. Employee stock ownership plans:					
Sec. 142—Estate tax exclusion for certain lump sum distributions	(1)	(1)	(1)	(1)	(1)
Sec. 143—Voting rights on employer securities for qualified plans	(1)	(1)	(1)	(1)	(1)
E. Retirement plan provisions:					
Sec. 152—Simplified employee pensions	−15	−25	−35	−45	−55
Sec. 153—Defined benefit plan limits	(2)	(2)	(2)	(2)	(2)
Sec. 154—Custodial accounts for regulated investment company stock	(2)	(2)	(2)	(2)	(2)
Sec. 155—Pension plan reserves	(2)	(2)	(2)	(2)	(2)
Sec. 156—Rollover of distributions from a tax-sheltered annuity	(2)	(2)	(2)	(2)	(2)
Sec. 157—Individual retirement account technical changes	−12	−12	−12	−12	−12
F. Other individual tax provisions:					
Sec. 161(a)—Uniformed Services Health Professions Scholarships	(2)	(2)	(2)	(2)	(2)
Sec. 161(b)—National Research Service Awards	−18	−10	(2)		
Sec. 162—Cancellation of student loans	(2)	(2)	(2)	(2)	(2)
Sec.164—Employer educational assistance	−26	−29	−32	−36	−40
Total, Title I	**−12,772**	**−14,783**	**−17,159**	**−20,001**	**−23,385**
Title II—Tax Shelter and Partnership Provisions					
Tax shelter provisions:					
Sec. 201—Extension of at risk rules to all activities other than real estate	10	7	6	4	4
Sec. 202—Extension of at risk provisions to closely held corporations	3	2	1	1	2
Sec. 203—Recapture of losses where amount at risk is less than zero	(1)	(1)	(1)	(1)	(1)
Total, Title II	**13**	**9**	**7**	**5**	**6**
Title III—Provisions Primarily Affecting Business Income Tax					
A. Corporate rate reduction:					
Sec. 301—Corporate rate reduction	−5,069	−5,551	−6,078	−6,655	−7,288
B. Investment credit provisions:					
Sec. 312—Increase in limitation to 90 percent of tax liability	−287	−629	−1,169	−826	−728
Sec. 313—Increased investment credit for certain pollution control facilities	−8	−25	−53	−91	−112
Sec. 314—Investment credit for single purpose agricultural or horticultural structures	−22	−22	−23	−25	−27
Sec. 315—Investment credit for certain rehabilitated buildings	−166	−193	−210	−229	−249
Sec. 316—Investment credit for cooperatives	−33	−34	−36	−38	−40
Sec. 317—Investment credit recapture under the Conrail reorganization					

Footnotes at end of table.

[Millions of dollars]

Provision	Calendar year liabilities				
	1979	1980	1981	1982	1983
C. Targeted jobs credit; WIN credit:					
Sec. 321—Targeted jobs credit	−388	−608	−705	−86	−86
Sec. 322—Work incentive program (WIN) credit changes	−106	−177	−216	−248	−296
Repeal of general jobs credit	2, 458	2, 458	2, 458	2, 458	2, 458
D. Tax-exempt bonds—Industrial development bond provisions:					
Sec. 331—Increase in limit on small issues	−2	−11	−21	−32	−43
Sec. 332—Local furnishing of electric energy	−2	−8	−14	−21	−26
Sec. 333—Industrial development bonds for water facilities	−5	−24	−46	−68	−95
Sec. 334—Advance refunding of industrial development bonds for certain public projects	(2)	(2)	(2)	(2)	(2)
E. Small business corporation provisions:					
Secs. 341–343—Subchapter S corporation provisions	(1)	(1)	(1)	(1)	(1)
Sec. 345—Small business corporation stock	(2)	(2)	(2)	(2)	(2)
F. Farm accounting rules:					
Sec. 351—Treatment of certain closely held farm corporations for accrual accounting purposes	(2)	(2)	(2)	(2)	(2)
Sec. 352—Accounting for growing crops	(2)	(2)	(2)	(2)	(2)
Sec. 353—Treatment of certain farms for purposes of rule requiring accrual accounting	(2)	(2)	(2)	(2)	(2)
G. Other business tax provisions:					
Sec. 361—Entertainment facility expenses	28	30	33	36	40
Sec. 362—Deficiency dividend procedure for regulated investment companies	(1)	(1)	(1)	(1)	(1)
Sec. 363—Safe harbor rule for Real Estate Investment Trusts	(5)	(5)	(5)	(5)	(5)
Sec. 364—Contributions in aid of construction to regulated electric or gas public utilities [6]	−96	−98	−101	−103	−107
Sec. 365—Liabilities of controlled corporations	(2)	(2)	(2)	(2)	(2)
Sec. 366—Medical expense reimbursement plans	(2)	(2)	(2)	(2)	(2)
Sec. 368—Postponement of effective date for special limitations on net operating loss carryovers	(2)	(2)	(2)	(2)	(2)
Sec. 369—Use of certain expired net operating loss carryovers and redemption of certificates of value in a tax-free reorganization of a transferor railroad	(1)	(1)	(1)	(1)	(1)
Sec. 371—Product liability net operating losses	−2	−10	−10	−9	−9
Sec. 372—Accounting for magazines, paperbacks, and records returned after the close of the taxable year		−11	−12	−13	−14
Sec. 373—Accounting for qualified coupons redeemed after the close of the taxable year	−10	−10	−10	−10	−10
Total, Title III	**−3,710**	**−4,923**	**−6,213**	**−5,960**	**−6,632**

Footnotes at end of table.

[Millions of dollars]

Provision	Calendar year liabilities				
	1979	1980	1981	1982	1983
Title IV—Capital Gains; Minimum Tax; Maximum Tax					
A. Capital gains provisions:					
Sec. 401—Repeal of alternative tax for noncorporate capital gains	133	143	154	166	178
Sec. 402—Increased capital gains deduction for individuals	−1,763	−1,895	−2,037	−2,190	−2,354
Sec. 403—Reduction of corporate alternative capital gains tax	−117	−135	−148	−163	−177
Sec. 404—One-time exclusion of gain on sale of residence	−415	−457	−502	−552	−607
Sec. 405—Rollover of gain on sale of residence incident to a job-related move	−4	−4	−4	−4	−4
Tax increase from induced capital gains realizations [7]	573	535	445	286	128
B. Minimum tax provisions:					
Sec. 421—Repeal certain preferences in the minimum tax	−1,274	−1,401	−1,541	−1,695	−1,865
Sec. 421—Alternative minimum tax for individuals	739	813	894	984	1,082
Sec. 422—Minimum tax treatment of intangible drilling costs	[8]	[8]	[8]	[8]	[8]
Sec. 423—Amendment to definition of foreign source capital gain tax preference	[2]	[2]	[2]	[2]	[2]
C. Maximum tax provision:					
Sec. 441—Capital gain tax preference offset	−52	−57	−63	−69	−76
Sec. 442—Limitation on personal service income	−56	−65	−75	−86	−99
Total, Title IV	−2,236	−2,523	−2,877	−3,323	−3,794
Title V—Other Tax Provisions					
A. Administrative provisions:					
Sec. 501—Reporting requirements with respect to charged tips	[9]	[9]	[9]	[9]	[9]
Sec. 504—Refund adjustments for amounts held under claim of right	[2]	[2]	[2]	[2]	[2]
B. Estate and gift tax provisions:					
Sec. 511—Jointly owned farms and closely held businesses	−41	−43	−46	−48	−51
Sec. 512—Attribution rules for extension of time to pay estate tax	[1]	[1]	[1]	[1]	[1]
Sec. 513—Subordination of special liens for estate tax attributable to special valuation property	[1]	[1]	[1]	[1]	[1]
Sec. 514—Time to amend governing instruments of charitable split interest trusts					
Sec. 515—Deferral of carryover basis rules	−93	−162	−185	−190	−200
C. Excise tax provisions:					
Sec. 520—Reduction of excise tax on private foundation investment income	−40	−40	−40	−40	−40
Sec. 521—Excise tax on certain gaming devices	−4	−6	−7	−7	−7
Sec. 522—Treatment of certain private foundations for purposes of section 4942	[1]	[1]	[1]	[1]	[1]

Footnotes at end of table.

[Millions of dollars]

Provision	1979	1980	1981	1982	1983
D. Other tax provisions:					
Sec. 530—Employment tax status of individuals as independent contractors or employees	(10)	(10)	(10)	------	------
Sec. 531—Tax treatment of cooperative housing corporations	(2)	(2)	(2)	(2)	(2)
Sec. 540—Source of interest income on deposit in Puerto Rican branches of U.S. savings and loan associations	(2)	(2)	(2)	(2)	(2)
Sec. 541—Taxation of Alaskan Native Claims Settlement Act Corporations	(11)	(11)	(11)	(11)	(11)
Sec. 542—Involuntary conversion of livestock	(2)	(2)	(2)	(2)	(2)
Sec. 543—Exclusion for certain cost-sharing payments	−17	−72	−72	−73	−74
Total, Title V	**−195**	**−323**	**−350**	**−358**	**−372**
Title VI—General Stock Ownership Corporations	(12)	(12)	(12)	(12)	(12)
Title VII—Technical Corrections to the Tax Reform Act of 1976	------	(2)	−7	−10	−13
Total, Titles I–VII	**−18,900**	**−22,543**	**−26,599**	**−29,647**	**−34,190**

Footnotes at end of table.

Table I–1.—Estimated Revenue Effects of Tax Provisions of the Revenue Act of 1978 (H.R. 13511), Calendar Year Liabilities 1979–83—Continued

Part B. Revenue Effects of Extending or Making Permanent Temporary Income Tax Reduction Provisions

[Millions of dollars]

Provision	Calendar year liabilities				
	1979	1980	1981	1982	1983
Individual Income Taxes					
Per capita credit [13]	−6,449	−6,642	−6,842	−7,047	−7,258
Optional taxable income credit [13]	−3,949	−4,344	−4,778	−5,256	−5,782
Earned income credit	−1,061	−1,019	−978	−938	−900
Sec. 311—Investment tax credit at 10-percent rate			−722	−773	−829
Sec. 367—Amortization for low-income housing	(1)	−4	−9	−13	−16
Jobs tax credit [14]	−983	−983	−983	−983	−983
Total, individual	**−12,442**	**−12,992**	**−14,312**	**−15,010**	**−15,768**
Corporation Income Taxes					
Rate reductions	−2,060	−2,255	−2,470	−2,704	−2,961
Sec. 311—Investment tax credit at 10-percent rate			−4,000	−5,201	−5,894
Sec. 141—TRASOP investment credit at 1½-percent rate			−396	−508	−592
Sec. 367—Amortization for low-income housing	(1)	−3	−6	−9	−11
Jobs tax credit [14]	−1,475	−1,475	−1,475	−1,475	−1,475
Total, corporate	**−3,535**	**−3,733**	**−8,347**	**−9,897**	**−10,933**
Total, Temporary Tax Reduction Extensions	**−15,977**	**−16,725**	**−22,659**	**−24,907**	**−26,701**
GRAND TOTAL, PARTS A AND B: TAX REDUCTIONS, REVISIONS AND EXTENSIONS	**−34,877**	**−39,268**	**−49,258**	**−54,554**	**−60,891**

[1] Less than $1 million.
[2] Less than $5 million.
[3] This estimate includes both the reduction in revenues and increase in outlays from the changes in the earned income credit. The Congressional Budget Office estimates that these changes will reduce revenues by $36, $91, $48, $50, and $55 mlllion and outlays would be increased by $198, $965, $782, $786, and $792 million in calendar years 1979–1983.
[4] These provisions continue the existing tax treatment of these types of plans, within certain limitations, and therefore have a negligible effect on budget receipts.
[5] No direct revenue effect is expected.

[6] The estimates were derived assuming that the position taken by the IRS is the correct one. The figures do not allow for revenue effects of additional charges the utilities may make in order to get reimbursement for the additional taxes payable under IRS ruling.

[7] The revenue effect from induced capital gains realizations agrees with that from the Congressional Budget Office. Using the Senate Finance Committee methodology, the additional revenue would be $738, $799, $864, $934, and $1,011 million for calendar years 1979–1983.

[8] The revenue loss of this provision has been included in H.R. 5263, the Energy Tax Act of 1978. (See Appendix II, Table II–1.)

[9] This provision has the effect of overturning Revenue Rulings 75–400 and 76–231. If the employer reporting requirements contained in these rulings were to take effect, increases in budget receipts could be substantial, This revenue is not being collected at the present time; therefore, no change in budget receipts is estimated.

[10] The revenue effect cannot be estimated because the provision affects liabilities being contested by taxpayers in administrative and judicial proceedings.

[11] The liabilities cannot be estimated before the contested issues are settled by the courts.

[12] There is not enough information to predict what the responses of the many governmental units will be with respect to this bill. However, this proposal is not expected to have a significant revenue effect over the next few years.

[13] These items are not extended by H.R. 13511, but are allowed to expire after 1978 and are replaced by an increase in the personal exemption from $750 to $1,000.

[14] The expiring general jobs tax credit is not extended and an offsetting entry is shown in part A of this table.

Table I–2.—Estimated Revenue Effects of Tax Provisions of the Revenue Act of 1978 (H.R. 13511), Fiscal Year Receipts 1979–83*

Part A. Tax Reductions and Revisions

[Millions of dollars]

Provision	Fiscal year receipts				
	1979	1980	1981	1982	1983
Title I—Individual Income Tax Provisions					
A. Individual income tax reductions and extensions:					
Secs. 101 and 106—Widening tax brackets, rate cuts, increase in zero bracket amount	−7,317	−13,057	−15,453	−18,317	−21,742
Repeal general tax credit	7,278	10,809	11,428	12,097	12,818
Sec. 102—Increase in the personal exemption [3]	−8,177	−12,171	−12,902	−13,677	−14,497
Secs. 104 and 105—Increase in and simplification of the earned income credit	−82	−1,227	−976	−937	−900
B. Itemized deductions; unemployment compensation; credits:					
Sec. 111—Repeal of nonbusiness deduction for State and local taxes on gasoline and other motor fuels	471	1,237	1,458	1,720	2,029
Sec. 112—Taxation of unemployment compensation benefits at certain income levels	----	251	261	259	263
Sec. 113—Political contributions	----	−20	−33	−20	−20
Sec. 121—Child care credit for payments to related individuals	−5	−38	−39	−40	−39
C. Deferred compensation provisions:					
Sec. 131—State and local government deferred compensation plans Sec. 132—Certain private deferred compensation plans Sec. 133—Deferred compensation payments to independent contractors	(4)	(4)	(4)	(4)	(4)

* The revenue estimates in Part A are the tax reductions from levels which would have prevailed had the existing temporary tax cuts been extended. Thus, where the bill merely extends an expiring tax cut, the table does not show any revenue effect; and where the bill replaces an expiring tax cut with a new provision (such as substituting graduated corporate tax rates for the corporate surtax exemption), the revenue loss from the new provision is only the excess of its gross revenue loss over what the revenue loss would have been had the expiring provision been extended. A revenue gain is shown for failing to extend the general tax credit and general jobs tax credit. Part B shows the revenue losses which would have occurred had certain existing temporary tax provisions been extended through 1983, both the provisions actually extended in the bill and the provisions replaced by other provisions.

(Other footnotes are at the end of the table.)

[Millions of dollars]

Provision	Fiscal year receipts				
	1979	1980	1981	1982	1983
D. Employee stock ownership plans:					
Sec. 142—Estate tax exclusion for certain lump sum distributions	(1)	(1)	(1)	(1)	(1)
Sec. 143—Voting rights on employer securities for qualified plans	(1)	(1)	(1)	(1)	(1)
E. Retirement plan provisions:					
Sec. 152—Simplified employee pensions	−6	−18	−29	−39	−49
Sec. 153—Defined benefit plan limits	(2)	(2)	(2)	(2)	(2)
Sec. 154—Custodial accounts for regulated investment company stock	(2)	(2)	(2)	(2)	(2)
Sec. 155—Pension plan reserves	(2)	(2)	(2)	(2)	(2)
Sec. 156—Rollover of distributions from a tax-sheltered annuity	(2)	(2)	(2)	(2)	(2)
Sec. 157—Individual retirement account technical changes	−25	−12	−12	−12	−12
F. Other individual tax provisions:					
Sec. 161(a)—Uniformed Services Health Professions Scholarships	(2)	(2)	(2)	(2)	(2)
Sec. 161(b)—National Research Service Awards	−52 [5]	−18	−10	(2)	
Sec. 162—Cancellation of student loans	(2)	(2)	(2)	(2)	(2)
Sec. 164—Employer educational assistance	−18	−28	−31	−35	−39
Total, Title I	**−7,933**	**−14,292**	**−16,338**	**−19,001**	**−22,188**
Title II—Tax Shelter and Partnership Provisions					
Tax shelter provisions:					
Sec. 201—Extension of at risk rules to all activities other than real estate	1	10	7	6	4
Sec. 202—Extension of at risk provisions to closely held corporations	1	3	2	1	1
Sec. 203—Recapture of losses where amount at risk is less than zero	(1)	(1)	(1)	(1)	(1)
Total, Title II	**2**	**13**	**9**	**7**	**5**
Title III—Provisions Primarily Affecting Business Income Tax					
A. Corporate rate reduction:					
Sec. 301—Corporate rate reduction	−2,281	−5,286	−5,788	−6,338	−6,940
B. Investment credit provisions:					
Sec. 312—Increase in limitation to 90 percent of tax liability	−129	−441	−872	−1,015	−782
Sec. 313—Increased investment credit for certain pollution control facilities	−6	−18	−42	−76	−104
Sec. 314—Investment credit for single purpose agricultural or horticultural structures	−53 [5]	−33 [5]	−22	−24	−26
Sec. 315—Investment credit for certain rehabilitated buildings	−67	−181	−205	−222	−238
Sec. 316—Investment credit for cooperatives	−20	−33	−35	−37	−39
Sec. 317—Investment credit recapture under the Conrail reorganization	−3 [5]				

Footnotes at end of table.

[Millions of dollars]

Provision	Fiscal year receipts				
	1979	1980	1981	1982	1983
C. Targeted jobs credit; WIN credit:					
Sec. 321—Targeted jobs credit	−141	−483	−651	−426	−86
Sec. 322—Work incentive program (WIN) credit changes	−39	−136	−197	−234	−264
Repeal of general jobs credit	689	2, 458	2, 458	2, 458	2, 458
D. Tax-exempt bonds—Industrial development bond provisions:					
Sec. 331—Increase in limit on small issues	(1)	−3	−14	−26	−37
Sec. 332—Local furnishing of electric energy	(1)	−3	−10	−18	−23
Sec. 333—Industrial development bonds for water facilities	(1)	−7	−31	−59	−78
Sec. 334—Advance refunding of industrial development bonds for certain public projects (sec. 335)	(2)	(2)	(2)	(2)	(2)
E. Small business corporation provisions:					
Sec. 341–343—Subchapter S corporation provisions	(1)	(1)	(1)	(1)	(1)
Sec. 345—Small business corporation stock	(2)	(2)	(2)	(2)	(2)
F. Farm accounting rules:					
Sec. 351—Treatment of certain closely held farm corporations for accrual accounting purposes	(2)	(2)	(2)	(2)	(2)
Sec. 352—Accounting for growing crops	(2)	(2)	(2)	(2)	(2)
Sec. 353—Treatment of certain farms for purposes of rule requiring accrual accounting	(2)	(2)	(2)	(2)	(2)
G. Other business tax provisions:					
Sec. 361—Entertainment facility expenses	13	29	31	34	38
Sec. 362—Deficiency dividend procedure for regulated investment companies	(1)	(1)	(1)	(1)	(1)
Sec. 363—Safe harbor rule for Real Estate Investment Trusts	(6)	(6)	(6)	(6)	(6)
Sec. 364—Contributions in aid of construction to regulated electric or gas public utilities [7]	(2)	−50	−100	−100	−100
Sec. 365—Liabilities of controlled corporations	(2)	(2)	(2)	(2)	(2)
Sec. 366—Medical expense reimbursement plans		(2)	(2)	(2)	(2)
Sec. 368—Postponement of effective date for special limitations on net operating loss carryovers	(2)	(2)	(2)	(2)	(2)
Sec. 369—Use of certain expired net operating loss carryovers and redemption of certificates of value in a tax-free reorganization of a transferor railroad	(1)	(1)	(1)	(1)	(1)
Sec. 371—Product liability net operating losses	(1)	(2)	−7	−8	−9
Sec. 372—Accounting for magazines, paperbacks, and records returned after the close of the taxable year		−5	−11	−12	−13
Sec. 373—Accounting for qualified coupons redeemed after the close of the taxable year [8]		−103	−10	−10	−10
Total, Title III	**−2, 037**	**−4, 295**	**−5, 506**	**−6, 113**	**−6, 253**

Footnotes at end of table.

[Millions of dollars]

Provision	Fiscal year receipts				
	1979	1980	1981	1982	1983
Title IV—Capital Gains; Minimum Tax; Maximum Tax					
A. Capital gains provisions:					
Sec. 401—Repeal of alternative tax for noncorporate capital gains	20	133	143	154	166
Sec. 402—Increased capital gains deduction for individuals	−131	−1, 763	−1, 895	−2, 037	−2, 190
Sec. 403—Reduction of corporate alternative capital gains tax	−53	−125	−141	−155	−170
Sec. 404—One-time exclusion of gain on sale of residence	−165	−415	−457	−502	−552
Sec. 405—Rollover of gain on sale of residence incident to a job-related move	−3	−4	−4	−4	−4
Tax increase from induced capital gains realizations [9]	68	573	535	445	286
B. Minimum tax provisions:					
Sec. 421—Repeal certain preferences in the minimum tax	------	−1, 274	−1, 401	−1, 541	−1, 695
Sec. 421—Alternative minimum tax for individuals	------	739	813	894	984
Sec. 422—Minimum tax treatment of intangible drilling costs	[10]	[10]	[10]	[10]	[10]
Sec. 423—Amendment to definition of foreign source capital gain tax preference	−5 [5]	[1]	[1]	[1]	[1]
C. Maximum tax provisions:					
Sec. 441—Capital gain tax preference offset	−6	−52	−57	−63	−69
Sec. 442—Limitation on personal service income	−21	−59	−69	−79	−91
Total, Title IV	**−296**	**−2, 247**	**−2, 533**	**−2, 888**	**−3, 335**
Title V—Other Tax Provisions					
A. Administrative provisions:					
Sec. 501—Reporting requirements with respect to charged tips	[11]	[11]	[11]	[11]	[11]
Sec. 504—Refund adjustments for amounts held under claim of right	[2]	[2]	[2]	[2]	[2]
B. Estate and gift tax provisions:					
Sec. 511—Jointly owned farms and closely held businesses	[1]	−41	−43	−46	−48
Sec. 512—Attribution rules for extension of time to pay estate tax	[1]	[1]	[1]	[1]	[1]
Sec. 513—Subordination of special liens for estate tax attributable to special valuation property	[1]	[1]	[1]	[1]	[1]
Sec. 514—Time to amend governing instruments of charitable split interest trusts	−15 [5]	------			
Sec. 515—Deferral of carryover basis rules	−36	−93	−162	−185	−190
C. Excise tax provisions:					
Sec. 520—Reduction of excise tax on private foundation investment income	−40	−40	−40	−40	−40
Sec. 521—Excise tax on certain gaming devices	−5 [5]	−6	−7	−7	−7
Sec. 522—Treatment of certain private foundations for purposes of section 4942	[1]	[1]	[1]	[1]	[1]

Footnotes at end of table.

[Millions of dollars]

Provision	Fiscal year receipts				
	1979	1980	1981	1982	1983
D. Other tax provisions:					
Sec. 530—Employment tax status of individuals as independent contractors or employees	(12)	(12)	(12)		
Sec. 531—Tax treatment of cooperative housing corporations	(2)	(2)	(2)	(2)	(2)
Sec. 540—Source of interest income on deposit in Puerto Rican branches of U.S. savings and loan associations	(2)	(2)	(2)	(2)	(2)
Sec. 541—Taxation of Alaskan Native Claims Settlement Act Corporations	(13)	(13)	(13)	(13)	(13)
Sec. 542—Involuntary conversion of livestock	(2)	(2)	(2)	(2)	(2)
Sec. 543—Exclusion for certain cost-sharing payments		−28	−77	−78	−79
Total, Title V	**−96**	**−208**	**−329**	**−356**	**−364**
Title VI—General Stock Ownership Corporations	(14)	(14)	(14)	(14)	(14)
Title VII—Technical Corrections to the Tax Reform Act of 1976	−8		(1)	−7	−10
Total, Titles I–VII	**−10,368**	**−21,029**	**−24,697**	**−28,358**	**−32,145**

Footnotes at end of table.

Table I–2.—Estimated Revenue Effects of Tax Provisions of the Revenue Act of 1978 (H.R. 13511), Fiscal Year Receipts 1979–83—Continued

Part B. Revenue Effect of Extending or Making Permanent Temporary Income Tax Reduction Provisions

[Millions of dollars]

	Fiscal year receipts				
	1979	1980	1981	1982	1983
Individual Income Taxes					
Per capita credit [15]	−4,514	−6,583	−6,780	−6,984	−7,194
Optional taxable income credit [15]	−2,764	−4,226	−4,648	−5,113	−5,624
Sec. 103—Extension of earned income credit		−1,061	−1,019	−978	−938
Sec. 311—Investment tax credit at 10-percent rate			−271	−741	−794
Sec. 367—Amortization for low-income housing	(1)	−2	−6	−11	−14
Jobs tax credit [16]	−125	−983	−983	−983	−983
Total, individual	**−7,403**	**−12,855**	**−13,707**	**−14,810**	**−15,547**
Corporation Income Taxes					
Rate reductions	−927	−2,148	−2,352	−2,575	−2,819
Sec. 311—Investment tax credit at 10-percent rate			−1,800	−4,460	−5,489
Sec. 141—TRASOP investment credit at 1½-percent rate			−178	−446	−545
Sec. 367—Amortization for low-income housing	(1)	−2	−5	−8	−10
Jobs tax credit [16]	−564	−1,475	−1,475	−1,475	−1,475
Total, corporate	**−1,491**	**−3,625**	**−5,810**	**−8,964**	**−10,338**
Total, Temporary Tax Reduction Extensions	**−8,894**	**−16,480**	**−19,517**	**−23,774**	**−25,885**
GRAND TOTAL, PARTS A AND B: TAX REDUCTIONS, REVISIONS AND EXTENSIONS	**−19,262**	**−37,509**	**−44,214**	**−52,132**	**−58,030**

[1] Less than $1 million.
[2] Less than $5 million.
[3] This estimate includes both the reduction in revenues and increase in outlays from the changes in the earned income credit. The Congressional Budget Office estimates that these changes will reduce revenues by $19, $113, $48, $51, and $54 million and outlays would be increased by $100, $1,071, $788, $790, and $791 million in fiscal years 1979–1983.
[4] These provisions continue existing tax treatment of these types of plans, within certain limitations, and therefore have a negligible effect on budget receipts.
[5] Includes liabilities of prior years.
[6] No direct revenue effect is expected.

[7] The estimates were derived assuming that the position taken by the IRS is the correct one. The figures do not allow for revenue effects of additional charges the utilities may make in order to get reimbursement for the additional taxes payable under IRS ruling.

[8] It is assumed the Service's position will be upheld by the courts in 1980.

[9] The revenue effect from induced capital gains realizations agrees with that from the Congressional Budget Office. Using the Senate Finance Committee methodology, the additional revenue would be $37, $738, $799, $864, and $934 million for fiscal years 1979–1983.

[10] The revenue loss of this provision has been included in H.R. 5263, The Energy Tax Act of 1978 (See Appendix II, Table II–1.)

[11] This provision has the effect of overturning Revenue Rulings 75–400 and 76–231. If the employer reporting requirements contained in these rulings were to take effect, increases in budget receipts could be substantial. This revenue is not being collected at the present time; therefore, no change in budget receipts is estimated.

[12] The revenue effect cannot be estimated because the provision affects liabilities being contested by taxpayers in administrative and judicial proceedings.

[13] Settlement of the contested issues is not expected to result in a significant impact on budget receipts through 1983.

[14] There is not enough information to predict what the responses of the many governmental units will be with respect to this bill. However, this proposal is not expected to have a significant revenue effect over the next few years.

[15] These items are not extended by H.R. 13511, but are allowed to expire after 1978 and are replaced by an increase in the personal exemption from $750 to $1,000.

[16] The expiring general jobs tax credit is not extended and an offsetting entry is shown in part A of this table.

Table I–3.—Distribution of Individual Income Tax Provisions of the Revenue Act of 1978 (H.R. 13511) by Income Class [1]

(1978 Income Levels)

Expanded income (thousands)	Tax decrease			Tax increase			Net tax change		
	Returns (thousands)	Amount (millions)	Average (actual)	Returns (thousands)	Amount (millions)	Average (actual)	Amount (millions)	Percent of total	Percent of present law tax
Below $5	5,503	−$210	−$38	55	$1	$25	−$208	1.6	36.0
$5 to $10	17,431	−1,557	−89	426	5	12	−1,552	11.6	18.8
$10 to $15	13,227	−1,055	−80	613	9	15	−1,045	7.8	6.1
$15 to $20	11,366	−1,543	−136	208	3	16	−1,540	11.6	6.4
$20 to $30	12,916	−3,086	−239	18	1	54	−3,085	23.1	6.9
$30 to $50	5,824	−2,669	−458	8	2	219	−2,667	20.0	6.8
$50 to $100	1,424	−1,643	−1,153	4	5	1,264	−1,638	12.3	6.8
$100 to $200	294	−657	−2,235	5	19	3,830	−638	4.8	4.9
$200 and over	75	−1,031	−13,691	3	76	29,834	−956	7.2	7.0
Total	68,060	−13,451	−198	1,338	121	91	−13,330	100.0	7.2

[1] Includes the earned income credit, increase in the zero bracket amount, bracket widening, rate reductions, $1,000 personal exemption, repeal of the general tax credit, repeal of the gas tax deduction, capital gains changes except the principal residence exclusion, and the maximum, minimum, and alternative tax changes.

Table I–4.—Federal Individual Income Tax Burden* for a Single Person and Married Couples With No, 1, 2, and 4 Dependents

(Assuming Deductible Personal Expenses of 23 Percent of Income)

Income**	Tax liability														
	Single person			Married couple with no dependents			Married couple with 1 dependent			Married couple with 2 dependents			Married couple with 4 dependents		
	Under present law	Under H.R. 13511	Reduction	Under present law	Under H.R. 13511	Reduction	Under present law	Under H.R. 13511	Reduction	Under present law	Under H.R. 13511	Reduction	Under present law	Under H.R. 13511	Reduction
$3,000	0	0	0	0	0	0	−300	−300	0	−300	−300	0	−300	−300	0
$5,000	279	250	29	0	0	0	−300	−500	200	−300	−500	200	−300	−500	200
$6,000	449	422	27	115	84	31	−200	−500	300	−200	−500	300	−200	−500	300
$8,000	810	787	23	431	374	57	273	−26	299	120	−166	286	0	−250	250
$10,000	1,199	1,177	22	761	702	59	620	534	86	446	374	72	128	84	44
$12,500	1,631	1,585	46	1,186	1,152	34	1,059	972	87	917	792	125	562	454	108
$15,000	2,126	2,047	79	1,651	1,625	27	1,486	1,415	72	1,330	1,233	97	990	873	117
$17,500	2,660	2,547	114	2,075	2,029	46	1,910	1,819	91	1,745	1,609	136	1,385	1,220	165
$20,000	3,232	3,115	117	2,555	2,457	98	2,368	2,223	145	2,180	2,013	167	1,808	1,593	215
$25,000	4,510	4,364	146	3,570	3,399	171	3,360	3,141	219	3,150	2,901	249	2,738	2,421	317
$30,000	5,950	5,718	232	4,712	4,477	235	4,472	4,197	275	4,232	3,917	315	3,778	3,357	421
$35,000	7,500	7,220	281	6,002	5,705	297	5,732	5,385	347	5,464	5,065	399	4,954	4,435	519
$40,000	9,233	8,886	347	7,427	7,052	375	7,135	6,682	453	6,848	6,312	536	6,278	5,657	621
$50,000	12,985	12,559	426	10,610	10,183	427	10,273	9,753	520	9,950	9,323	627	9,290	8,463	827
$60,000	16,835	16,392	443	14,230	13,602	628	13,856	13,112	744	13,496	12,634	862	12,746	11,774	972
$70,000	20,685	20,242	443	18,080	17,375	705	17,705	16,885	820	17,330	16,395	935	16,550	15,415	1,135
$80,000	24,535	24,092	443	21,930	21,178	752	21,555	20,678	877	21,180	20,178	1,002	20,400	19,188	1,212
$90,000	28,385	27,942	443	25,780	25,028	752	25,405	24,528	877	25,030	24,028	1,002	24,250	23,028	1,222
$100,000	32,235	31,792	443	29,630	28,878	752	29,255	28,378	877	28,880	27,878	1,002	28,100	26,878	1,222

NOTE.—Details may not add to totals because of rounding.

*Computed without reference to the tax tables.

**Wage or salary and/or self-employment income.

APPENDIX II:

NEW INDIVIDUAL INCOME TAX RATE SCHEDULE

RATE REDUCTION.—Section 1 of the Code (relating to tax imposed) is amended to read as follows:

"SECTION 1. TAX IMPOSED.

"(a) **Married Individuals Filing Joint Returns and Surviving Spouses.**—There is hereby imposed on the taxable income of—

"(1) every married individual (as defined in section 143) who makes a single return jointly with his spouse under section 6013, and

"(2) every surviving spouse (as defined in section 2(a)),

a tax determined in accordance with the following table:

"If taxable income is:	The tax is:
Not over $3,400	No tax.
Over $3,400 but not over $5,500	14% of excess over $3,400.
Over $5,500 but not over $7,600	$294 plus 16% of excess over $5,500.
Over $7,600 but not over $11,900	$630, plus 18% of excess over $7,600.
Over $11,900 but not over $16,000	$1,404, plus 21% of excess over $11,900.
Over $16,000 but not over $20,200	$2,265, plus 24% of excess over $16,000.
Over $20,200 but not over $24,600	$3,273, plus 28% of excess over $20,200.
Over $24,600 but not over $29,900	$4,505, plus 32% of excess over $24,600.
Over $29,900 but not over $35,200	$6,201, plus 37% of excess over $29,900.
Over $35,200 but not over $45,800	$8.162, plus 43% of excess over $35,200.
Over $45,800 but not over $60,000	$12,720, plus 49% of excess over $45,800.
Over $60,000 but not over $85,600	$19,678, plus 54% of excess over $60,000.
Over $85,600 but not over $109,400	$33,502, plus 59% of excess over $85,600.
Over $109,400 but not over $162,400	$47,544, plus 64% of excess over $109,400.
Over $162,400 but not over $215,400	$81,464, plus 68% of excess over $162,400.
Over $215,400	$117,504, plus 70% of excess over $215,400.

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

"If taxable income is:	The tax is:
Not over $2,300	No tax.
Over $2,300 but not over $4,400	14% of excess over $2,300.
Over $4,400 but not over $6,500	$294, plus 16% of excess over $4,400.
Over $6,500 but not over $8,700	$630, plus 18% of excess over $6,500.
Over $8,700 but not over $11,800	$1,026, plus 22% of excess over $8,700.
Over $11,800 but not over $15,000	$1,708, plus 24% of excess over $11,800.
Over $15,000 but not over $18,200	$2,476, plus 26% of excess over $15,000.
Over $18,200 but not over $23,500	$3,308, plus 31% of excess over $18,200.
Over $23,500 but not over $28,800	$4,951, plus 36% of excess over $23,500.
Over $28,800 but not over $34,100	$6,859, plus 42% of excess over $28,800.
Over $34,100 but not over $44,700	$9,085, plus 46% of excess over $34,100.
Over $44,700 but not over $60,600	$13,961, plus 54% of excess over $44,700.
Over $60,600 but not over $81,800	$22,547, plus 59% of excess over $60,600.
Over $81,800 but not over $108,300	$35,055, plus 63% of excess over $81,800.
Over $108,300 but not over $161,300	$51,750, plus 68% of excess over $108,300.
Over $161,300	$87,790, plus 70% of excess over $161,300.

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"(c) **Unmarried Individuals (Other Than Surviving Spouses and Heads of Households.**—There is hereby imposed on the taxable income of every individual (other than a surviving spouse as defined in section 2(a) or the head of a household as defined in section 2(b)) who is not a married individual (as defined in section 143) a tax determined in accordance with the following table:

"If taxable income is:	The tax is:
Not over $2,300	No tax.
Over $2,300 but not over $3,400	14% of excess over $2,300.
Over $3,400 but not over $4,400	$154, plus 16% of excess over $3,400.
Over $4,400 but not over $6,500	$314, plus 18% of excess over $4,400.
Over $6,500 but not over $8,500	$692, plus 19% of excess over $6,500.
Over $8,500 but not over $10,800	$1,072, plus 21% of excess over $8,500.
Over $10,800 but not over $12,900	$1,555, plus 24% of excess over $10,800.
Over $12,900 but not over $15,000	$2,059, plus 26% of excess over $12,900.
Over $15,000 but not over $18,200	$2,605, plus 30% of excess over $15,000.
Over 18,200 but not over $23,500	$3,565, plus 34% of excess over $18,200.
Over $23,500 but not over $28,800	$5,367, plus 39% of excess over $23,500.
Over $28,800 but not over $34,100	$7,434, plus 44% of exces over $28,800.
Over $34,100 but not over $41,500	$9,766, plus 49% of excess over $34,100.
Over $41,500 but not over $55,300	$13,392, plus 55% of excess over $41,500.
Over $55,300 but not over $81,800	$20,982, plus 63% of excess over $55,300.
Over $81,800 but not over $108,300	$37,687, plus 68% of excess over $81,800.
Over $108,300	$55,697, plus 70% of excess over $108,300.

"(d) **Married Individuals Filing Separate Returns.**—There is hereby imposed on the taxable income of every married individual (as defined in section 143) who does not make a single return jointly with his spouse under section 6013 a tax determined in accordance with the following table:

"If taxable income is:	The tax is:
Not over $1,700	No tax.
Over $1,700 but not over $2,750	14% of excess over $1,700.
Over $2,750 but not over $3,800	$147, plus 16% of excess over $2,750.
Over $3,800 but not over $5,950	$315, plus 18% of excess over $3,800.
Over $5,950 but not over $8,000	$702, plus 21% of excess over $5,950.
Over $8,000 but not over $10,100	$1,132.50, plus 24% of excess over $8,000.
Over $10,100 but not over $12,300	$1,636.50, plus 28% of excess over $10,100.
Over $12,300 but not over $14,950	$2,252.50, plus 32% of excess over $12,300.
Over $14,950 but not over $17,600	$3,100.50, plus 37% of excess over $14,950.
Over $17,600 but not over $22,900	$4,081, plus 43% of excess over $17,600.
Over $22,900 but not over $30,000	$6,360, plus 49% of excess over $22,900.
Over $30,000 but not over $42,800	$9,839, plus 54% of excess over $30,000.
Over $42,800 but not over $54,700	$16,751, plus 59% of excess over $42,800.
Over $54,700 but not over $81,200	$23,772, plus 64% of excess over $54,700.
Over $81,200 but not over $107,700	$40,732, plus 68% of excess over $81,200.
Over $107,700	$58,752, plus 70% of excess over $107,700.

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

"If taxable income is:	The tax is:
Not over $1,050	14% of taxable income.
Over $1,050 but not over $2,100	$147, plus 16% of excess over $1,050.
Over $2,100 but not over $4,250	$315, plus 18% of excess over $2,100.
Over $4,250 but not over $6,300	$702, plus 21% of excess over $4,250.
Over $6,300 but not over $8,400	$1,132.50, plus 24% of excess over $6,300.
Over $8,400 but not over $10,600	$1,636.50, plus 28% of excess over $8,400.
Over $10,600 but not over $13,250	$2,252.50, plus 32% of excess over $10,600.
Over $13,250 but not over $15,900	$3,100.50, plus 37% of excess over $13,250.
Over $15,900 but not over $21,200	$4,081, plus 43% of excess over $15,900.
Over $21,200 but not over $28,300	$6,360, plus 49% of excess over $21,200.
Over $28,300 but not over $41,100	$9,839, plus 54% of excess over $28,300.
Over $41,100 but not over $53,000	$16,751, plus 59% of excess over $41,100.
Over $53,000 but not over $79,500	$23,772, plus 64% of excess over $53,000.
Over $79,500 but not over $106,000	$40,732, plus 68% of excess over $79.500.
Over $106,000	$58,752, plus 70% of excess over $106,000.".

SUMMARY OF ENERGY TAX ACT OF 1978

(P.L. 95–618; H.R. 5263)

TITLE I—RESIDENTIAL ENERGY CREDIT

Sec. 101. Residential Energy Credit

1. Insulation and other energy-conserving items

The Act provides a new 15-percent credit on the first $2,000 of qualifying expenditures, for a maximum credit of $300. It is available for installations made after April 19, 1977, and before January 1, 1986, with respect to a taxpayer's principal residence, if the residence was in existence on April 19, 1977. Principal residences include condominiums and cooperative housing. The credit is available to homeowners and renters. The credit will be allowed for installation of (1) insulation, (2) a replacement burner for oil and gas fired furnaces, (3) a device to modify flue openings, (4) an electrical or mechanical furnace ignition system, (5) an exterior storm or thermal door or window, (6) an automatic energy-saving thermostat, (7) caulking or weatherstripping for an exterior door or window, and (8) an energy usage display meter. In addition, the Secretary of the Treasury may, by regulation, add items which increase the energy efficiency of a dwelling.

Credits for installations in 1977 (after April 19, 1977) must be claimed on 1978 tax returns. In years when credits exceed tax liability, the credits may be carried over to subsequent years through 1987, i.e., 2 years after expiration of the credit.

2. Renewable energy source equipment

The Act provides a credit of 30 percent on the first $2,000 and 20 percent on the next $8,000 of expenditures, for a maximum total credit of $2,200, for installations of (1) solar, (2) wind or (3) geothermal energy equipment in connection with a principal residence. Other renewable energy source equipment used for heating or cooling the dwelling or providing hot water for use within the dwelling may be added by the Secretary of Treasury by regulation, if use of the equipment results in overall energy savings. The credits apply to expenditures made after April 19, 1977, and before January 1, 1986, for both existing and new residences. Principal residences include condominiums and cooperative housing. The credit is available to homeowners and renters.

Credits for installations in 1977 (after April 19, 1977) must be claimed on 1978 returns. In years when credits exceed tax liability, the credits may be carried over to subsequent years through 1987, i.e., 2 years after expiration of the credit.

TITLE II—TRANSPORTATION TAX PROVISIONS

A. GAS GUZZLER TAX

Sec. 201. Gas Guzzler Tax

The Act imposes a new manufacturers excise tax, starting with model year 1980 automobiles, on the sale or initial lease of automobiles whose fuel economy fails to meet certain fuel efficiency standards. The fuel efficiency standards upon which the tax is based generally start from 4 to 6.5 miles per gallon below the fleetwide average standards of the Energy Production and Conservation Act. (A table relating taxes and fuel efficiency levels appears below.) The fuel economy of an automobile for purposes of this tax is that established by EPA on the combined urban-rural driving cycle. The tax is not to be included in basis for any purposes where the use by the taxpayer begins not more than 1 year after the first retail sale of the vehicle.

The tax will apply to 1980 and later model year automobiles which weigh 6,000 pounds or less. The tax does not apply to automobiles which are classified as nonpassenger automobiles under rules prescribed by the Secretary of Transportation for purposes of section 501 of the Motor Vehicles Information and Cost Savings Act and which were in effect on November 9, 1978.

Other exemptions from the tax apply to emergency vehicles used (1) as ambulances or combination ambulance-hearses, (2) as police or law-enforcement vehicles, or (3) for any other emergency use prescribed by the Secretary of Treasury by regulations. Small manufacturers of automobiles (those who produce less than 10,000 vehicles a year) may apply to the Secretary of Treasury for special treatment for a model year, if it is not possible for the manufacturer to meet the applicable tax-free fuel economy standards with respect to some or all of its models for that year.

The table below shows the tax for the applicable fuel economy standards in each model year.

(1) In the case of a 1980 model year automobile:

If the fuel economy of the model type in which the automobile falls is:	***The tax is:***
At least 15	*0*
At least 14 but less than 15	*$200*
At least 13 but less than 14	*300*
Less than 13	*550*

(2) in the case of a 1981 model year automobile:

If the fuel economy of the model type in which the automobile falls is:	***The tax is:***
At least 17	*0*
At least 16 but less than 17	*$200*
At least 15 but less than 16	*350*
At least 14 but less than 15	*450*
At least 13 but less than 14	*550*
Less than 13	*650*

(3) *In the case of a 1982 model year automobile:*

If the fuel economy of the model type in which the automobile falls is:	The tax is:
At least 18.5	0
At least 17.5 but less than 18.5	$200
At least 16.5 but less than 17.5	350
At least 15.5 but less than 16.5	450
At least 14.5 but less than 15.5	600
At least 13.5 but less than 14.5	750
At least 12.5 but less than 13.5	950
Less than 12.5	1,200

(4) *In the case of a 1983 model year automobile:*

If the fuel economy of the model type in which the automobile falls is:	The tax is:
At least 19	0
At least 18 but less than 19	$350
At least 17 but less than 18	500
At least 16 but less than 17	650
At least 15 but less than 16	800
At least 14 but less than 15	1,000
At least 13 but less than 14	1,250
Less than 13	1,550

(5) *In the case of a 1984 model year automobile:*

If the fuel economy of the model type in which the automobile falls is:	The tax is:
At least 19.5	0
At least 18.5 but less than 19.5	$450
At least 17.5 but less than 18.5	600
At least 16.5 but less than 17.5	750
At least 15.5 but less than 16.5	950
At least 14.5 but less than 15.5	1,150
At least 13.5 but less than 14.5	1,450
At least 12.5 but less than 13.5	1,750
Less than 12.5	2,150

(6) *In the case of a 1985 model year automobile:*

If the fuel economy of the model type in which the automobile falls is:	The tax is:
At least 21	0
At least 20 but less than 21	$500
At least 19 but less than 20	600
At least 18 but less than 19	800
At least 17 but less than 18	1,000
At least 16 but less than 17	1,200
At least 15 but less than 16	1,500
At least 14 but less than 15	1,800
At least 13 but less than 14	2,200
Less than 13	2,650

(7) *In the case of a 1986 or later model year automobile:*

If the fuel economy of the model type in which the automobile falls is:	The tax is:
At least 22.5	0
At least 21.5 but less than 22.5	$500
At least 20.5 but less than 21.5	650
At least 19.5 but less than 20.5	850
At least 18.5 but less than 19.5	1,050
At least 17.5 but less than 18.5	1,300
At least 16.5 but less than 17.5	1,500
At least 15.5 but less than 16.5	1,850
At least 14.5 but less than 15.5	2,250
At least 13.5 but less than 14.5	2,700
At least 12.5 but less than 13.5	3,200
Less than 12.5	3,850

B. MOTOR FUELS

Sec. 221. Exemption From Motor Fuels Excise Taxes for Certain Alcohol Fuels

Gasohol, which is a blend of motor fuel and alcohol, will be exempt from the Federal excise taxes on motor fuels, if the blend contains at least 10 percent alcohol (including ethanol, methanol or other alcohol), other than alcohol produced from petroleum, natural gas or coal. The exemption applies to sales of fuel after December 31, 1978, and before October 1, 1984.

Sec. 222. Denial of Refund or Credit for Excise Taxes on Motor Fuels and Lubricating Oil for Nonbusiness, Nonhighway Uses

Under the Act, the 2-cents-a-gallon reduction in the excise taxes on gasoline and special motor fuels and the 6-cents-a-gallon reduction in the excise taxes on lubricating oil will not be allowed after December 31, 1978. These reductions, which were available in the form of a refund, credit or exemption, were allowed for motor fuels and lubricating oil used (1) for nonbusiness, nonhighway purposes (such as lawnmowers, snowmobiles, etc.) and (2) in motorboats (whether or not used in business).

This amendment does not affect other provisions of present law which make it clear that articles sold as supplies for vessels employed in the fisheries or whaling business are not subject to the excise taxes on fuels or lubricating oil. Where the sale of these items is made other than by the manufacturer, producer or importer, the Code provides for a refund (or credit) of the tax when the item is sold for use or is used as supplies for such vessels.

C. PROVISIONS RELATED TO BUSES

Sec. 231. Removal of Excise Tax on Buses

The Act repeals the 10-percent manufacturers excise tax imposed on the sale of buses having a gross vehicle weight of more than 10,000 pounds; lighter weight buses were exempted from the tax by the Revenue Act of 1971. The repeal of the tax is effective for sales of buses to the ultimate purchaser after November 9, 1978. Refunds or credits are provided for sales of buses after April 19, 1977, and before November 10, 1978, provided the manufacturer has reimbursed the ultimate purchaser for the amount of the tax. Refunds or credits of the tax to dealers are provided also for floor stocks on which the tax had been paid and which were held by the dealers on November 9, 1978.

Sec. 232. Removal of Excise Tax on Bus Parts

The Act repeals the 8-percent manufacturers excise tax on bus parts and accessories. The repeal is effective for sales after November 30, 1978.

Sec. 233. Removal of Excise Tax on Certain Items Used on or in Connection with Intercity, Local or School Buses

The Act removes the excise taxes on highway tires, inner tubes, tread rubber, gasoline, other motor fuels and lubricating oil for private intercity, local and school bus operations. Tires, inner tubes, tread rubber and special motor fuels may be sold free of tax to a qualified bus operator. Where the tax has been paid, provision is made for reimbursement. The repeal is effective after November 30, 1978.

D. INCENTIVES FOR VAN POOLING

Sec. 241 Full Investment Credit for Certain Commuter Vehicles

Under the Act, an employer is entitled to the full investment credit on the purchase of a new van or bus, if the vehicle has a useful life of at least 3 years, seats 9 or more persons (including the driver), and will be used 80 percent or more for transporting employees to or from work. The credit is available for vehicles purchased after November 8, 1978, and placed in service by the taxpayer before January 1, 1986.

Sec. 242. Exclusion From Income of Certain Employer-Furnished Transportation

The Act provides that gross income will not include the value in excess of the employee's cost of transportation to or from work which is furnished by an employer if such transportation is in a commuter van or bus. This provision applies to transportation furnished in taxable years beginning after December 31, 1978, and before January 1, 1986. In general, to qualify, (1) the transportation must be furnished under a plan established in writing by the employer which meets the anti-discrimination requirements generally applicable to tax-exempt pension plans, and (2) the transportation must be by a commuter highway vehicle. That is, it must be a vehicle which could qualify for the special investment credit if an election were made and the vehicle were acquired during the period for which the full investment tax credit is available.

The exclusion does not apply unless the plan provides that the value of any transportation is furnished in addition to, and not in lieu of, any compensation otherwise payable to the employee. The provision does not apply to self-employed individuals (such as partners or proprietors) or former employees even though such individuals or former employees are treated as employees for other purposes.

TITLE III—BUSINESS ENERGY TAX PROVISIONS

Sec. 301(a)–(c). Business Energy Investment Credits

The Act provides an investment tax credit of 10 percent for investment in certain types of energy property. This credit is in addition to the regular 10-percent investment credit for which such property also may be eligible under existing law. The energy credit is generally available for costs incurred for qualifying property after September 30, 1978, and before January 1, 1983.

Energy property is defined to include boilers and burners which use a substance other than oil or natural gas, i.e., an alternate substance, as a fuel, plus related on-site fuel handling and pollution control equipment. Equipment to convert an alternate substance into a synthetic fuel or industrial feedstock and costs to modify existing oil or gas burning equipment to use an alternate substance as a partial fuel or feedstock also are covered. In addition, related equipment for fuel or feedstock handling and pollution control are eligible. Energy property also includes geothermal energy equipment, solar and wind energy equipment, recycling equipment, shale oil equipment, equipment to produce natural gas from geopressured brine and certain specially defined equipment which reduces energy consumption in an existing commercial or industrial facility or process. Eligible property must have a useful life of at least 3 years and meet prescribed performance and quality standards in order to qualify.

Generally the additional investment credit is not available for public utility property within the meaning of Code section 46(f)(5). However, the credit is available for eligible property, e.g., geothermal equipment, which is not used by a public utility.

The general rules for applying the regular investment credit are also made applicable to the energy investment credit, with several exceptions. The structural components (sec. 48(a)(1)) and lodging (sec. 48(a)(3)) limitations are not applicable to the energy credits. In addition, energy credits may be used against 100 percent of income tax liability.

The credits for solar and wind energy equipment are refundable to the extent they exceed tax liability, and special stacking rules are provided for the energy credits and the regular investment credit to allow the maximum use of energy credits under these rules.

Sec. 301(d). Denial of Investment Credit and Accelerated Depreciation Methods for Certain Property

The Act denies the regular investment credit for portable air conditioning and heating units. In addition, both the regular investment credit and accelerated methods of depreciation are denied for new boilers which use oil or natural gas as a fuel. Exceptions from the denial of these tax benefits are generally provided where the use of coal is precluded by air pollution regulations or where the oil or gas

boiler is not used in manufacturing, processing or mining. This provision applies to property placed in service after September 30, 1978, except for property acquired under the terms of a binding contract in effect on October 1, 1978.

Sec. 301(e). Depreciation of Existing Oil or Gas Boilers

Where a taxpayer expects to retire an existing oil or gas fueled boiler or combustor before the end of its intended useful life, the Act allows the useful life of this equipment to be redetermined, and the taxpayer may use straightline depreciation on the equipment over the remainder of its redetermined useful life. This amendment applies to taxable years ending after November 9, 1978.

TITLE IV—MISCELLANEOUS PROVISIONS

Sec. 401. Treatment of Intangible Drilling Costs for Oil and Gas Wells for Purposes of the Minimum Tax

The Act makes permanent the 1977 rules for applying the minimum tax to intangible drilling costs (IDCs). Thus, a taxpayer's IDC preference is the amount by which the amount of excess IDCs arising in the taxable year is greater than the amount of the taxpayer's net income from oil and gas properties for the taxable year. The amount of the excess IDCs arising in the taxable year is the excess of (i) the IDCs paid or incurred in connection with oil and gas wells (other than the cost incurred in drilling a nonproductive well) allowable for the taxable year over (ii) the amount of those costs which would have been allowable for the taxable year if such costs had been capitalized and straight line recovery of intangibles had been used with respect to such costs. Income from oil and gas properties is to be determined first with regard to the rules for determining gross income from oil and gas properties for purposes of percentage depletion (under section 613(a) of the Code without regard to the limitations of section 613A). Net income from oil and gas properties is gross income from those properties reduced by the amount of deductions (other than IDCs subject to the tax on preferences) properly attributable to that gross income. Deductions attributable to properties with no gross income are not taken into account for purposes of computing net income from oil and gas properties. The term straight line recovery of intangibles means, except as described below, ratable amortization of IDCs over the 120-month period beginning with the month in which production from the well begins. Alternatively, at the taxpayer's election, straight line recovery of intangibles means any method which would be permitted for purposes of determining cost depletion with respect to such well and which is selected by the taxpayer for purposes of determining the IDC preference.

(The Revenue Act of 1978, P.L. 95–600, contains a provision which is identical to section 401 of the Energy Tax Act. The Revenue Act clarifies that net income from oil and gas properties is not to be reduced, for purposes of the minimum tax offset, by dry hole costs incurred on properties with no oil or gas income. H. Rep. 95–1800, 95th Cong., 2d Sess. 268 (1978).)

Sec. 402. Deduction of Intangible Drilling Costs for Geothermal Deposits

a. Option to deduct intangible drilling costs

The Act allows producers an election to deduct IDCs for geothermal wells. The election with respect to geothermal wells is separate from the election for oil and gas wells. The Act does not change present law with respect to wells producing natural gas from geopressured brine, so that these will continue to be treated as natural gas wells for purposes of the IDC election.

Because the Act does not change the IDC treatment of wells producing natural gas from geopressurized brine, this provision is not to be construed to be a special tax provision or comparable adjustment under section 107(d) of the Natural Gas Policy Act of 1978.

b. Application of the minimum tax to intangible drilling costs

The Act generally treats geothermal IDCs the same as oil and gas IDCs for minimum tax purposes. Thus, a taxpayer's IDC preference is the amount by which the amount of excess IDCs arising in the taxable year is greater than the amount of the taxpayer's net income from geothermal properties for the taxable year. The amount of the excess IDCs arising in the taxable year is the excess of (i) the IDCs paid or incurred in connection with geothermal wells (other than the cost incurred in drilling a nonproductive well) allowable for the taxable year over (ii) the amount of those costs which would have been allowable for the taxable year if such costs had been capitalized and straight line recovery of intangibles had been used with respect to such costs. The amount of the taxpayer's net income from geothermal properties for the taxable year is the excess of (i) the aggregate amount of gross income (within the meaning of section 613(a)) from all geothermal properties of the taxpayer received or accrued during the taxable year over (ii) the amount of any deductions allocable to such properties reduced by excess IDCs for that taxable year. The term straight line recovery of intangibles means, except as described below, ratable amortization of IDCs over the 120-month period beginning with the month in which production from the well begins. Alternatively, at the taxpayer's election, straight line recovery of intangibles means any method which would be permitted for purposes of determining cost depletion with respect to such well and which is selected by the taxpayer for purposes of determining the IDC preference.

This section of the Act takes effect on October 1, 1978, and applies to taxable years ending after September 30, 1978. In addition, the Act continues the present law treatment of wells producing natural gas from geopressured brine as natural gas wells.

c. Recapture of intangible drilling costs

The Act extends present law on the recapture of IDCs for geothermal properties and applies it separately from recapture with respect to oil and gas properties. Under present law, the total of IDCs deducted, reduced by the amount of IDCs which would have been deductible had those costs been capitalized and deducted through cost depletion, is subject to recapture upon disposition of an oil and gas property. Geopressured natural gas wells are to be treated as natural gas wells as under present law.

d. At risk limitation applied to intangible drilling costs

The Act extends present law to geothermal properties and treats developing those properties as an activity separate from developing oil and gas properties. However, natural gas from geopressured brine is to be aggregated with oil and gas as one activity.

e. Effective date

The amendments made by section 402 apply with respect to wells commenced after September 30, 1978, in taxable years ending after that date.

Sec. 403(a). Depletion for Geothermal Deposits

The Act provides percentage depletion for geothermal resources located in the United States or its possessions.

The percentage of gross income from each property which can be deducted as percentage depletion is 22 percent for production in calendar years 1978 through 1980, 20 percent for 1981, 18 percent for 1982, 16 percent for 1983, and 15 percent for all years thereafter. Percentage depletion for geothermal resources is not subject to the various limitations and restrictions relating specifically to oil and gas which were enacted in the Tax Reduction Act of 1975. However, present law restrictions which apply to percentage depletion for all minerals also apply to percentage depletion for geothermal resources. For example, depletion in excess of basis is an item of tax preference for purposes of the minimum tax, and percentage depletion on any property is to be limited to 50 percent of the taxable income from that property (computed without regard to the deduction for depletion). There is no basis limitation on the amount of allowable depletion deductions.

This provision is effective on October 1, 1978, and applies to taxable years ending after September 30, 1978. Thus, percentage depletion for geothermal resources is to be allowed with respect to production after September 30, 1978.

Sec. 403(b). Depletion for Natural Gas from Geopressured Brine

The Act provides a 10-percent deduction for percentage depletion for natural gas produced from geopressured brine in the United States or its possessions. The percentage depletion for such gas is not limited to the taxpayer's adjusted basis in the property, nor is it subject to the various restrictions which apply to percentage depletion for oil and gas, i.e., the limitation on depletion deductions for integrated oil and gas companies, the per barrel limitation, or the 65 percent of taxable income limitation. However, the allowable deduction is subject to the generally applicable restrictions on percentage depletion. The allowable deduction with respect to any geopressured brine property cannot exceed 50 percent of taxable income from the property (computed without regard to the deduction for depletion), and depletion in excess of adjusted basis is treated as an item of tax preference for purposes of the minimum tax.

The 10-percent depletion allowance for natural gas produced from geopressured brine is to be allowed only where drilling began after September 30, 1978, and before January 1, 1984. Wells drilled within this period will continue to be entitled to percentage depletion for their entire producing lives. However, wells drilled before and after these dates will be treated as natural gas wells as under present law. This section of the Act takes effect on October 1, 1978, and applies to taxable years ending on or after October 1, 1978.

The Act also provides that the term natural gas produced from geopressured brine is to mean the same gas that is eligible for the special treatment under section 107(c)(2) of the Natural Gas Policy Act of 1978 and defined pursuant to section 503 of that Act. Because percentage depletion is not limited to natural gas produced from geopressured brine but is available to a wide range of minerals, this provision is not to be construed to be a special tax provision or comparable adjustment under section 107(d) of that Act.

Sec. 404. Removal of Excise Tax on Rerefined Lubricating Oil

The Act exempts the sale of lubricating oil from the 6-cent-per-gallon manufacturers excise tax, if the lubricating oil sold is a mixture of new oil and previously used or waste lubricating oil which has been cleaned, renovated or rerefined.

For the exemption to apply, the blend of old and new oil must consist of 25 percent or more of waste or rerefined oil. All of the new oil in a mixture is to be exempt from the excise tax if the blend contains 55 percent or less new oil. If the mixture contains more than 55 percent new oil, the excise tax exemption applies only to new oil equal to 55 percent of the mixture. That is, where new oil constitutes 55 to 75 percent of the mixture, the exemption applies only to the amount of new oil equal to 55 percent of the mixture.

The provision is effective for sales after November 30, 1978.

APPENDIX III:
REVENUE EFFECTS OF THE ENERGY TAX ACT OF 1978

Table III–1.—Revenue Effects of the Energy Tax Act of 1978

[In millions of dollars]

Item	Fiscal year receipts				
	1979*	1980	1981	1982	1983
Title I—Residential energy credits					
Credit for insulation and other energy-conserving items	−635	−370	−392	−415	−440
Credit for solar and wind energy expenditures	−81	−64	−72	−89	−115
Total, Title I	**−716**	**−434**	**−464**	**−504**	**−555**
Title II—Transportation tax provisions					
Gas guzzler tax		(2)	45	50	100
Exemption from motor fuels excise taxes for certain alcohol fuels	(2)	(2)	(2)	(2)	−6
Denial of credit or refund for nonbusiness, nonhighway use of gasoline, special motor fuels and lubricating oil	(1)	4	4	4	4
Removal of excise tax on buses	−22	−9	−9	−9	−9
Removal of excis tax on bus parts	−2	−3	−3	−3	−3
Removal of excise tax on certain items used in connection with intercity, local and school buses	−11	−13	−13	−13	−13
Vanpooling tax incentives	(1)	(1)	(1)	(1)	(1)
Total, Title II	**−35**	**−21**	**24**	**29**	**73**
Title III—Changes in business investment credit to encourage conservation of, or conversion from, oil and gas or to encourage new energy technology					
Alternative, conservation and new technology credits	−221	−391	−496	−597	−458
Investment credit denied and depreciation limited to straight-line on oil or gas boilers, portable air-conditioners and space heaters	42	98	99	93	96
Total, Title III	**−179**	**−293**	**−397**	**−504**	**−362**

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Table III–1.—Revenue Effects of the Energy Tax Act of 1978—Continued

[In millions of dollars]

Item	Fiscal year receipts				
	1979*	1980	1981	1982	1983
Title IV—Miscellaneous Provisions					
Tax incentives relating to alternative fuel sources:					
Percentage depletion:					
Geothermal	(1)	(1)	−2	−4	−6
Geopressured natural gas		−1	−3	−5	−8
Option to deduct intangible drilling costs:					
Geothermal	−10	−18	−21	−26	−30
Geopressured natural gas	−11	−16	−17	−18	−19
Subtotal	−21	−35	−43	−53	−63
Other provisions:					
Treatment of oil and gas intangible drilling costs for purposes of minimum tax	−51	−61	−73	−84	−97
Removal of excise tax on re-refined lubricating oil	−2	−3	−3	−3	−3
Subtotal	−53	−64	−76	−87	−100
Total, Title IV	**−74**	**−99**	**−119**	**−140**	**−163**
TOTAL, TITLES I–IV	**−1,004**	**−847**	**−956**	**−1,119**	**−1,007**

[1] Less than $1,000,000.
[2] Less than $5,000,000.

*Figures may reflect liabilities of prior years.

Table III–2.—Estimated Revenue Effects of the Tax Credits [1] for Business Qualified Property, by Type of Property, Fiscal Years 1979–83

[In millions of dollars]

Credit provision	1979	1980	1981	1982	1983
Alternative energy property [2]	−36	−90	−156	−227	−191
Specially defined energy property [3]	−145	−236	−261	−278	−207
Shale oil equipment	−7	−15	−21	−27	−20
Geopressured natural gas equipment	−6	−9	−9	−9	−6
Solar and wind energy property	−7	−10	−15	−19	−13
Recycling equipment [3]	−20	−31	−34	−37	−21
Total	**−221**	**−391**	**−496**	**−597**	**−458**

[1] 10-percent nonrefundable credit effective after Sept. 30, 1978.
[2] Industrial (nonutility) equipment, primarily for use as other than oil or gas-burning boilers, combustors, and pollution control and handling equipment.
[3] Only if applied to or within a structure in existence before Oct. 1, 1979.

SUMMARY OF FOREIGN EARNED INCOME ACT OF 1978

(P.L. 95–615; H.R. 9251)

I. TAX TREATMENT OF AMERICANS WORKING ABROAD

Sec. 4. [1] Delay of Effective Date of 1976 Act

The Act delays the effective date of the changes made by the 1976 Act to the taxation of individuals working abroad so that the law in effect prior to the 1976 Act applies to taxable years beginning prior to January 1, 1978. The section also extends through 1977, but only for those individuals who are entitled to the exclusion, the pre-1976 Act rule that they may not claim both the foreign tax credit and the zero bracket amount (i.e., the standard deduction) in 1977.

Sec. 202. Individuals Residing in Camps

The Act provides an election for employees in camps in hardship areas (places where U.S. Government employees receive a hardship post differential of 15 percent or more) to claim an exclusion (under sec. 119) for the value of their lodging and an annual exclusion (under sec. 911) of $20,000 in lieu of the excess foreign living expense deductions. A camp for this purpose refers to substandard housing provided in enclaves in remote areas close to the job site where alternative housing is not available on the open market. Employees who elect the benefits of this provision are ineligible for the deductions for excess foreign living costs provided by the Act.

No foreign tax credit is allowed for foreign taxes allocable to the exclusion. As under prior law, deductions are not allowed for amounts allocable to the exclusion, but the deduction for moving expenses allocable to the exclusion will no longer be disallowed.

Sec. 203. Deduction for Excess Foreign Living Costs

The Act provides for a new deduction for excess foreign living costs. Those persons eligible for the deduction are individuals who are *bona fide* residents of a foreign country for an entire taxable year or who are present (including resident aliens) in a foreign country 17 out of 18 months. The excess foreign living cost deduction is a deduction from gross income in determining adjusted gross income, and, accordingly, a taxpayer may claim the deduction without being required to itemize deductions.

The specific terms of the deduction are as follows:

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[1] The other sections of title I, except for sections 4 and 5, were made noneffective by section 210 of the Act as of the day after the date of enactment of this Act. These other provisions were dealt with in other legislation: (1) prohibition on commuting expense regulations (sec. 2); (2) prohibition on fringe benefits regulations (sec. 3); (3) application of Code section 117 to certain education programs for members of the Uniformed Services (sec. 6); (4) extensions of 5-year amortization for low-income rental housing (sec. 7); and (5) postponement of 1976 Act rules for certain net operating loss carryovers (sec. 8).

a. Excess cost of living

This element of the deduction consists of an amount determined under IRS tables showing the excess cost of living in various foreign places for families of various sizes. It is based on the excess of costs in the foreign place over costs in the highest cost metropolitan area in the continental United States (excluding Alaska) and is determined with reference to the spendable income of a person paid the salary of a GS–14, step 1 (currently $32,442), regardless of the taxpayer's actual income.

b. Excess housing costs

This element of the deduction is an amount equal to the excess of the individual's housing expenses over the individual's base housing amount. The individual's base housing amount is one-sixth of his net earned income—that is, one-sixth of the excess of his earned income (minus certain allocable business deductions) over his deductible excess foreign living costs.

Since net earned income is itself a function of the amount allowed as a deduction for excess housing costs, in order to avoid circularity in the computation of the deduction, the base housing amount is computed by taking one-fifth of the excess of the taxpayer's earned income (minus certain allocable business deductions) over the sum of (1) his deductible excess foreign living costs other than the housing element and (2) the *full* cost of the taxpayer's housing. This amount is the mathematical equivalent of one-sixth of net earned income.

The computation of the housing deduction may be illustrated by the following example of an individual with earned income for the year of $45,000 whose deductible education, home leave, and cost of living expenses are $10,000 and whose total housing costs are $15,000. The taxpayer's base housing amount would be $4,000—one-fifth of the $20,000 excess of the taxpayer's $45,000 earned income over (i) his $10,000 of deductible foreign living costs other than the housing element and (ii) the $15,000 spent on housing. Thus, the excess housing cost element of the deduction would be $11,000 (the excess of the $15,000 housing costs over the $4,000 base housing amount), leaving the taxpayer with net earned income of $24,000 ($45,000 less deductible excess living costs of $21,000). The taxable $4,000 base housing amount is one-sixth of net earned income.

A deduction is allowed for the full cost of the taxpayer's own housing rather than just the excess over his base amount if (1) the individual maintains a separate household for his spouse and dependents because of living conditions which are dangerous, unhealthful, or otherwise adverse, (2) the taxpayer's tax home (generally, his principal place of work) is in a hardship area, and (3) the taxpayer's family does not live in the United States. In addition, the taxpayer receives a deduction for the excess costs of maintaining the qualified second household.

c. Educational costs

This element of the deduction consists of the reasonable schooling expenses for the education of the taxpayer's dependents at the elementary and secondary level. Generally, the cost of tuition, fees, books, and local transportation and of other expenses required by the school are deductible.

Reasonable schooling expenses are determined with reference to the least expensive adequate U.S.-type school, if any, available within a reasonable commuting distance of the individual's tax home. (The dependent may attend school elsewhere, including the United States, but the deduction is limited to that amount.) If an adequate United States-type school is not available within a reasonable commuting distance, deductible schooling expenses include room and board and transportation costs.

d. Home leave transportation

This element of the deduction consists of the reasonable costs of one round trip annually for the taxpayer, his spouse, and each dependent from the location of his tax home outside the United States to the location of the taxpayer's last principal residence in the U.S. or, if there is none, to the nearest port of entry in the continental U.S. (other than Alaska). The deduction is generally limited to coach fare when available.

e. Hardship area deduction

The Act provides a hardship deduction of $5,000 a year for employees working in hardship areas. Hardship areas are those areas where United States Government employees would qualify for a hardship post differential of 15 percent or more of salary.

f. Special rules for separate households

Special rules apply if the taxpayer maintains a separate household for his spouse and dependents in a foreign country at a place other than his tax home because of living conditions at his tax home which are dangerous, unhealthful, or otherwise adverse. In general, the special rules base the computations of the various elements of the deduction on the qualified second household, rather than the tax home.

Sec. 204. Deduction for Moving Expenses

In the case of moves to foreign work locations, the Act increases the period during which the costs of temporary living arrangements are allowed as deductible moving expenses from 30 days to 90 days, and raises the ceiling on those temporary living costs from $1,500 to $4,500. Under this provision, moving expenses include the cost of storing goods while abroad. The moving expense deduction is also expanded to permit *bona fide* retirees returning to the United States after working abroad and survivors of Americans who die while working overseas to deduct the cost of moving back to the United States, subject to the regular moving expense limitations.

Sec. 205. Meals or Lodging Furnished to Employees Under Certain Conditions

One of the requirements for exclusion of the value of meals and lodging provided by the taxpayer's employer is that they be furnished to the taxpayer by his employer for the convenience of the employer. The Act modifies the wording of the requirement so that the exclusion applies to the taxpayer, his spouse and dependents and the excluded item may be furnished by or on behalf of the employer. All the other requirements for exclusion must be met for any item of income to be excluded under this revised wording.

Sec. 206. Suspension of Period to Reinvest Proceeds From Sale of Home

The Act provides that, in general, the running of the 18- or 24-month time periods during which the taxpayer may reinvest the proceeds from the sale of his home and defer recognition of the gain is to be suspended during any time that the taxpayer has a tax home outside the United States. However, the suspension period is not to extend more than 4 years after the date of the sale of the old residence.

Sec. 207. Withholding, Filing and Reporting Requirements

The Act permits adjustment of withholding on wages paid to employees to take account of deductions allowable under new section 913 for excess foreign living costs.

The Act also authorizes the Treasury to require by regulations that civilian employees of the U.S. Government provide information on their tax returns disclosing the amount and type of any allowances they receive which are excluded from gross income under section 912.

Sec. 208. Reports by Treasury on Exclusions and Deductions of Private and Civilian Government Employees Working Abroad

The Act requires that, as soon as possible after the close of 1979 and after the close of every second year thereafter, the Secretary of the Treasury submit a report to the tax-writing committees of Congress setting forth the number of, and the countries of residence of, persons benefiting from the provisions dealing with the taxation of Americans working abroad (sections 911, 912, and 913 of the Code) and the revenue cost and the economic effects of those provisions.

Sec. 209. Effective Date

The Act provides that the law prior to the 1976 Act is extended through taxable years beginning in 1977. The other changes in the tax treatment of Americans working abroad are generally effective for taxable years beginning after December 31, 1977. However, for taxable years beginning in 1978, taxpayers may elect to be taxed under the law in effect prior to November 7, 1978 (that is, the law as amended by the Tax Reform Act of 1976).

Sec. 210. Certain Provisions of Title I of the Act Made Inapplicable

This provision makes Title I of the Act (except for sections 4 and 5, as noted above) inapplicable as of the day after the date of enactment of this Act because these other provisions of Title I were dealt with in other legislation. (See the footnote to section 4 above.)

II. SALARY REDUCTION PLANS, CASH OR DEFERRED PROFIT-SHARING PLANS, AND CAFETERIA PLANS (SECS. 5 and 210)

On December 6, 1972, the IRS issued proposed regulations which would have changed the tax treatment of employees under salary reduction plans, and which called into question the tax treatment of employees under cash or deferred profit-sharing plans and so-called "cafeteria" plans. The Employee Retirement Income Security Act of 1974 (ERISA) froze the tax treatment of these plans for 2 years, and the Tax Reform Act of 1976 extended the freeze until December 31, 1977.

The Act extends the "freeze" on existing tax treatment of salary reduction plans, cash or deferred profit-sharing plans and "cafeteria" plans until January 1, 1980; however, under section 210 of this Act, the freeze is not to apply to any type of plan for any period for which rules for that type of plan are provided by the Revenue Act of 1978.

III. REVENUE EFFECT

The provisions of the Foreign Earned Income Act of 1978 are estimated to have the following revenue effect for fiscal years 1978–83:

(millions of dollars)

1979	1980	1981	1982	1983
−255[1]	−254	−275	−297	−310

[1] The fiscal 1979 revenue effect reflects no loss of revenue from the one-year delay of the 1976 Act on 1977 tax liability because that loss is properly allocable to fiscal year 1978 receipts.

SUMMARY OF FRINGE BENEFITS ACT

(P.L. 95–427; H.R. 12841)

Sec. 1. Employee Fringe Benefits

Section 61 of the Internal Revenue Code defines gross income as including "all income from whatever source derived" and specifies that it includes "compensation for services". The regulations (§ 1.61–2 (a)(1)) provide that income includes compensation for services paid for other than in money. Further, the Supreme Court has stated that section 61 "is broad enough to include in taxable income any economic or financial benefit conferred on the employee as compensation whatever the form or mode by which it is effected." In actual practice, however, the "economic benefit" test has not been rigidly followed. Thus, where compensation is paid in some form other than cash, the issue as to taxability generally has been resolved by statutes, regulations, and administrative rulings which take account of several different factors.

In 1975, the Treasury Department issued a discussion draft of proposed regulations which contained a number of proposed rules for determining whether various fringe benefits constitute taxable compensation. Under the principles contained in the discussion draft, some employee fringe benefits which, as a matter of prior administrative practice, had not been considered to be taxable compensation would have been treated as subject to tax. Other benefits which might be viewed as taxable compensation would not have been taxed under the discussion draft's proposed rules. The discussion draft was withdrawn by the Treasury Department on December 28, 1976. Thus, the question of whether, and what, fringe benefits result in taxable income to employees generally continues to depend on the facts and circumstances in each individual case.

The Act provides that the Treasury Department (Internal Revenue Service) is precluded from issuing final regulations, under section 61, which would govern the income tax treatment of fringe benefits prior to 1980. In addition, no regulations relating to the treatment of fringe benefits under section 61 are to be proposed which would be effective prior to 1980.

Sec. 2. Commuting Expenses

In general, a taxpayer is al'owed a deduction for ordinary and necessary expenses paid or incurred in carrying on a trade or business. This includes transportation expenses incurred in the pursuit of a trade or business. However, no deduction is allowed for personal, living, or family expenses, including the cost of commuting to and from work. Problems have arisen in delineating between transportation expenses which are considered to be nondeductible personal commuting expenses and other transportation expenses which are deductible business expenses. Generally, transportation expenses are not deductible if the taxpayer is going to his principal place of work from his residence or is returning to his home from his principal place of work. On the other hand, transportation expenses to temporary worksites other than the taxpayer's principal place of work often are deductible as a business expense.

On November 22, 1976, the IRS published Revenue Ruling 76–453 which stated that a taxpayer's transportation expenses incurred in traveling between the taxpayer's residence and place of work, even though temporary, would be nondeductible commuting expenses, regardless of the nature of the work performed, the distance traveled, the mode of transport, or the degree of necessity. In addition, the ruling stated that reimbursement of such expenses would be considered "wages" for purposes of employment taxes, and income tax withholding. The ruling was originally effective for transportation costs paid or incurred after December 31, 1976. The Service three times postponed the effective date of this ru'ing, and on September 23, 1977, announced that the ruling was suspended indefinitely and that proposed regulations inviting public comment would be issued shortly. Proposed regulations have not as yet been issued.

This Act requires that the application of the income tax, employment taxes, and withholding provisions relating to the treatment of transportation expenses paid or incurred after 1976 and before January 1, 1980, in traveling between a taxpayer's residence and place of work shall be made fully in accordance with the rules in effect prior to the issuance of Revenue Ruling 76–453 on November 22, 1976. The IRS shall not issue any ruling or final regulation prior to January 1, 1980, changing the tax treatment of these transportation expenses paid or incurred prior to that date.

Sec. 3. Subsistence Allowances for State Police Officers

Section 119 of the Code, which was enacted in 1954, excludes from an employee's gross income the value of employer-furnished meals if they are provided for the employer's convenience, on its business premises, and for substantially noncompensatory reasons. The legislative history of section 119 indicates that its exclusion applies only to the value of meals furnished in kind.

On November 29, 1977, the Supreme Court decided *Commissioner* v. *Kowalski*, 98 S. Ct. 315 (1977), which held that cash meal allowances paid to a State trooper were includable in income since the section 119 exclusion applied only to meals furnished in kind. This decision resolved a conflict among the various appellate courts as to the taxability of cash meal allowances.

The Act applies the Supreme Court's *Kowalski* decision to State police officers on a prospective basis only. It allows an exclusion from gross income for subsistence allowances received by an officer during the years 1970 through 1976, to the extent that the allowances were not included in income on the officer's income tax return. In addition, the Act excludes from gross income all subsistence allowances received by State police officers during 1977. However, the Act generally does not authorize the refund of taxes paid where statutory subsistence allowances were included in income on the officer's tax return or where the officer elects not to have the exclusion apply. For purposes of the Act, a State police officer is a police officer, or highway patrolman, employed by a State or the District of Columbia on a full-time basis with the power to arrest. The Act applies to statutory subsistence allowances received after December 31, 1969, and before January 1, 1978.

Sec. 4. Meals Furnished to Employees

Under present law, meals furnished by an employer to an employee are not included in an employee's income so long as the meals are furnished on the employer's premises and for the employer's convenience (Sec. 119 of the Code). However, the Treasury regulations provide that meals do not qualify for the exclusion if an employee must pay something for meals which he may or may not purchase.

The Act overrules the portion of the Treasury regulations which provide that the exclusion for employer-furnished meals is automatically inapplicable if the employee must bear some charge for the meals which he has the option to purchase. The Act allows an exclusion for the value of meals in excess of any amount charged if the other requirements for exclusion are satisfied. The Act also provides for an exclusion for amounts an employer is required to pay for his meals on a periodic basis if the payments are required whether or not the meal is accepted or declined. The Act does not change present law in any other respect. It is effective for all years to which the Internal Revenue Code of 1954 applies.

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