Public Law 95-618
Energy Tax Act of 1978

Internal Revenue cumulative bulletin

1978-3

Volume 2

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U.S. Treasury Dept. Internal Revenue Service

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Statement of Principles of Internal Revenue Tax Administration

The function of the Internal Revenue Service is to administer the Internal Revenue Code. Tax policy for raising revenue is determined by Congress.

With this in mind, it is the duty of the Service to carry out that policy by correctly applying the laws enacted by Congress; to determine the reasonable meaning of various Code provisions in light of the Congressional purpose in enacting them; and to perform this work in a fair and impartial manner, with neither a government nor a taxpayer point of view.

At the heart of administration is interpretation of the Code. It is the responsibility of each person in the Service, charged with the duty of interpreting the law, to try to find the true meaning of the statutory provision and not to adopt a strained construction in the belief that he is "protecting the revenue." The revenue is properly protected only when we ascertain and apply the true meaning of the statute.

The Service also has the responsibility of applying and administering the law in a reasonable, practical manner. Issues should only be raised by examining officers when they have merit, never arbitrarily or for trading purposes. At the same time, the examining officer should never hesitate to raise a meritorious issue. It is also important that care be exercised not to raise an issue or to ask a court to adopt a position inconsistent with an established Service position.

Administration should be both reasonable and vigorous. It should be conducted with as little delay as possible and with great courtesy and considerateness. It should never try to overreach, and should be reasonable within the bounds of law and sound administration. It should, however, be vigorous in requiring compliance with law and it should be relentless in its attack on unreal tax devices and fraud.

Introduction

The Internal Revenue Bulletin is the authoritative instrument of the Commissioner of Internal Revenue for announcing official rulings and procedures of the Internal Revenue Service and for publishing Treasury Decisions, Executive Orders, Tax Conventions, legislation, court decisions, and other items of general interest. It is published weekly and may be obtained from the Superintendent of Documents on a subscription basis. Bulletin contents of a permanent nature are consolidated semiannually into Cumulative Bulletins, which are sold on a singe-copy basis. Occasionally an extra volume of the Cumulative Bulletin is required for publication of legislative matters.

It is the policy of the Service to publish in the Bulletin all substantive rulings necessary to promote a uniform application of the tax laws, including all rulings that supersede, revoke, modify, or amend any of those previously published in the Bulletin. All published rulings apply retroactively unless otherwise indicated. Procedures relating solely to matters of internal management are not published; however, statements of internal practices and procedures that affect the rights and duties of taxpayers are published.

Revenue Rulings represent the conclusions of the Service on the application of the law to the entire state of facts involved. In those that are based on positions taken in rulings to taxpayers or technical advice to Service field offices, identifying details and confidential information are deleted to comply with statutory requirements.

Rulings and procedures reported in the Bulletin do not have the force and effect of Treasury Department Regulations, but they may be used as precedents. Unpublished rulings will not be relied on, used, or cited as precedents by Service personnel in the disposition of other cases. In applying published rulings and procedures, the effect of subsequent legislation, regulations, court decisions, rulings, and procedures must be considered, and Service personnel and others concerned are cautioned against reaching the same conclusions in other cases unless the facts and circumstances are substantially the same.

The regulations, rulings, decisions, procedures, Public Laws, etc., published in the weekly Internal Revenue Bulletins 1978-26 through 1978-52 have been consolidated and are published in Internal Revenue Cumulative Bulletin 1978-2.

Cumulative Bulletin 1978-3, Volume 2, is devoted solely to Public Law 95-618, the Energy Tax Act of 1978, and related Committee and Conference reports, which were not published in the Weekly Bulletin.

The Bulletin Index-Digest System, a research and reference service supplementing the Bulletin, may be obtained from the Superintendent of Documents on a subscription basis. It consists of four Services: Service No. 1, Income Tax; Service No. 2, Estate and Gift Taxes; Service No. 3, Employment Taxes; Service No. 4, Excise Taxes. Each Service consists of a basic volume and a cumulative supplement that provide (1) finding lists of items published in the Bulletin, (2) digests of Revenue Rulings, Revenue Procedures, and other published items, and (3) topical indexes of Public Laws, Treasury Decisions, and Tax Conventions.

The contents of this publication are not copyrighted and may be reprinted freely, a citation of the Cumulative Bulletin as the source would be appropriate.

1954 Code Sections Added, Amended, or Repealed by Public Law 95-618

The following sections of the Internal Revenue Code of 1954 are affected by Public Law 95-618. New sections added to the Code and repealed sections are noted as such. Code sections that are renumbered are listed and followed by the redesignated (Red.) Code section in brackets.

1954 Code Sections	Act Sections
39(a)(3)	233(b)(2)(C), 233(d)
44C New	101(a), 101(c)
46(a)(2)	301(a)(1)
46(a)(10) New	301(c)(1)
46(c)(3)(A)	301(a)(2)(A)
46(c)(6) New	241(a)
46(f)(8)	301(a)(2)(B)
47(a)(4) [Red. 47(a)(5)]	241(b)(1), 241(b)(2)
47(a)(4) New	241(b)(1)
47(a)(6)(B)	241(b)(3)
48(a)(1)(A)	301(d)(1), 301(d)(4)
48(a)(10) New	301(d)(2), 301(d)(4)
48(l) [Red. 48(n)]	301(b)
48(l) New	301(b)
48(m) New	301(b)
56(c)	101(b)(2), 101(c)
57(a)(11)	402(b)(1), 402(e)
57(a)(11)(B)(i)	402(b)(2), 402(e)
57(a)(11)(D) New	402(b)(3), 402(e)
124 [Red. 125]	242(a)
124 New	242(a)
167(p) [Red. 167(r)]	301(d)(3), 301(d)(4)
167(p) New	301(d)(3), 301(d)(4)
167(q) New	301(e)(1), 301(e)(2)
263(c)	402(a), 402(e)
465(c)(1)(C)	402(d)(1), 402(e)
465(c)(1)(D)	402(d)(1), 402(e)
465(c)(1)(E) New	402(d)(1), 402(e)
465(c)(2)(C)	402(d)(2), 402(e)
465(c)(2)(D)	402(d)(2), 402(e)
465(c)(2)(E) New	402(d)(2), 402(e)
613(c)(1)	403(a)(2)(A), 403(c)
613(e) New	403(a)(1), 403(c)
613A(b)(1)(A)	403(a)(2)(B)(i), 403(c)
613(A)(b)(1)(B)	403(a)(2)(B)(ii), 403(c)
613A(b)(1)(C) Repealed	403(a)(2)(B)(iii), 403(c)
613A(b)(2) [Red. 613A(b)(3)]	403(b)(1), 403(c)
613A(b)(2) New	403(b)(1), 403(c)
613A(b)(3)(C) New	403(b)(2), 403(c)
614(b)	403(a)(2)(C), 403(c)
614(c)	403(a)(2)(D), 403(c)
751(c)	402(c)(5), 402(e)
1016(a)(21) New	101(b)(3), 101(c)
1016(d) [Red. 1016(e)]	201(b), 201(g)
1016(d) New	201(b), 201(g)
1254	402(c)(3), 402(e)
1254(a)(1)	402(c)(1), 402(e)
1254(a)(2)	402(c)(1), 402(e)
1254(a)(3)	402(c)(2), 402(e)
4041(b)	222(a)(2), 222(b) 233(a)(3)(B), 233(d)
4041(k) New	221(b)(1), 221(b)(2)
4063(a)(6)	231(a), 231(g)(1)
4064 New	201(a), 201(g)
4081(c) New	221(a)(1), 221(a)(2)
4092(a)	404(b), 404(d)
4093	404(a), 404(d)
4217(e) New	201(d), 201(g)
4221(a)	201(c)(1), 201(g)
4221(d)(7) New	233(c)(2), 233(d)
4221(e)(5)	233(c)(1), 233(d)
4221(e)(6) New	232(a), 232(c)
4222(d)	201(e), 201(q) 231(f)(2), 231(g)(1)
4293	201(c)(2), 201(g)
4483(c)	233(a)(3)(C), 233(d)
6096(b)	101(b)(4), 101(c)
6401(d) New	301(c)(2)
6412(a)(1)	231(f)(1), 231(g)(1)
6416(b)(2)	201(c)(3), 201(g)
6416(b)(2)(I)	232(b), 232(c)
6416(b)(2)(L) New	233(c)(3), 233(d)
6416(b)(2)(M) New	233(c)(3), 233(d)
6421(a)	222(a)(1)(A), 222(b)
6421(b)	233(a)(1), 233(d)
6421(d)(2) Repealed	233(a)(3)(A)(i), 233(d)
6421(d)(3) New	222(a)(1)(B), 222(b)
6421(d)(3) [Red. 6421(d)(2)]	233(a)(3)(A)(ii), 233(d)
6424	233(b)(2)(A), 233(d)
6424(a)	222(a)(3), 222(b) 233(b)(1), 233(d)
6427(b)	233(a)(2), 233(d)
6504(9)	233(b)(2)(D), 233(d)
6675(a)	233(b)(2)(D), 233(d)

Public Law 95-618

95th Congress, H.R. 5263

November 9, 1978

An Act

To provide tax incentives for the production and conservation of energy, and for other purposes.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That (a) item 912.05 of the Appendix to the Tariff Schedules of the United States (19 U.S.C. 1202) is amended—

(1) by inserting ", and parts thereof" immediately after "Generator lighting sets for bicycles"; and

(2) by striking out "12/31/76" and inserting in lieu thereof "6/30/80".

SECTION 1. SHORT TITLE; ETC.

(a) SHORT TITLE.—This Act may be cited as the "Energy Tax Act of 1978".

(b) AMENDMENT OF 1954 CODE.—Except as otherwise expressly provided, whenever in this Act an amendment or repeal is expressed in terms of an amendment to, or repeal of, a section or other provision, the reference shall be considered to be made to a section or other provision of the Internal Revenue Code of 1954.

(c) TABLE OF CONTENTS.—

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TITLE I—RESIDENTIAL ENERGY CREDIT

SEC. 101. RESIDENTIAL ENERGY CREDIT.

(a) GENERAL RULE.—Subpart A of part IV of subchapter A of chapter 1 (relating to credits allowable) is amended by inserting after section 44B the following new section:

"SEC. 44C. RESIDENTIAL ENERGY CREDIT.

26 USC 44C.

"(a) GENERAL RULE.—In the case of an individual, there shall be allowed as a credit against the tax imposed by this chapter for the taxable year an amount equal to the sum of—

"(1) the qualified energy conservation expenditures, plus

"(2) the qualified renewable energy source expenditures.

"(b) QUALIFIED EXPENDITURES.—For purposes of subsection (a)—

"(1) ENERGY CONSERVATION.—In the case of any dwelling unit, the qualified energy conservation expenditures are 15 percent of so much of the energy conservation expenditures made by the taxpayer during the taxable year with respect to such unit as does not exceed $2,000.

"(2) RENEWABLE ENERGY SOURCE.—In the case of any dwelling unit, the qualified renewable energy source expenditures are the following percentages of the renewable energy source expenditures made by the taxpayer during the taxable year with respect to such unit:

"(A) 30 percent of so much of such expenditures as does not exceed $2,000, plus

"(B) 20 percent of so much of such expenditures as exceeds $2,000 but does not exceed $10,000.

"(3) PRIOR EXPENDITURES BY TAXPAYER ON SAME RESIDENCE TAKEN INTO ACCOUNT.—If for any prior year a credit was allowed to the taxpayer under this section with respect to any dwelling unit by reason of energy conservation expenditures or renewable energy source expenditures, paragraph (1) or (2) (whichever is appropriate) shall be applied for the taxable year with respect to such dwelling unit by reducing each dollar amount contained in such paragraph by the prior year expenditures taken into account under such paragraph.

"(4) MINIMUM DOLLAR AMOUNT.—No credit shall be allowed under this section with respect to any return for any taxable year if the amount which would (but for this paragraph) be allowed with respect to such return is less than $10.

"(5) APPLICATION WITH OTHER CREDITS.—The credit allowed by subsection (a) shall not exceed the tax imposed by this chapter for the taxable year, reduced by the sum of the credits allowable under a section of this subpart having a lower number or letter designation than this section, other than credits allowable by sections 31, 39, and 43.

26 USC 31, 39, 43.

"(6) CARRYOVER OF UNUSED CREDIT.—

"(A) IN GENERAL.—If the credit allowable under subsection (a) for any taxable year exceeds the limitation imposed by paragraph (5) for such taxable year, such excess shall be carried to the succeeding taxable year and added to the credit allowable under subsection (a) for such succeeding taxable year.

"(B) NO CARRYOVER TO TAXABLE YEARS BEGINNING AFTER DECEMBER 31, 1987.—No amount may be carried under subparagraph (A) to any taxable year beginning after December 31, 1987.

"(c) DEFINITIONS AND SPECIAL RULES.—For purposes of this section—

"(1) ENERGY CONSERVATION EXPENDITURES.—The term 'energy conservation expenditure' means an expenditure made on or after April 20, 1977, by the taxpayer for insulation or any other energy-conserving component (or for the original installation of such insulation or other component) installed in or on a dwelling unit—

"(A) which is located in the United States,

"(B) which is used by the taxpayer as his principal residence, and

"(C) the construction of which was substantially completed before April 20, 1977.

"(2) RENEWABLE ENERGY SOURCE EXPENDITURE.—

"(A) IN GENERAL.—The term 'renewable energy source expenditure' means an expenditure made on or after April 20, 1977, by the taxpayer for renewable energy source property installed in connection with a dwelling unit—

"(i) which is located in the United States, and

"(ii) which is used by the taxpayer as his principal residence.

"(B) CERTAIN LABOR COSTS INCLUDED.—The term 'renewable energy source expenditure' includes expenditures for labor costs properly allocable to the onsite preparation, assembly, or original installation of renewable energy source property.

"(C) SWIMMING POOL, ETC., USED AS STORAGE MEDIUM.—The term 'renewable energy source expenditure' does not include any expenditure properly allocable to a swimming pool used as an energy storage medium or to any other energy storage medium which has a primary function other than the function of such storage.

"(3) INSULATION.—The term 'insulation' means any item—

"(A) which is specifically and primarily designed to reduce when installed in or on a dwelling (or water heater) the heat loss or gain of such dwelling (or water heater),

"(B) the original use of which begins with the taxpayer,

"(C) which can reasonably be expected to remain in operation for at least 3 years, and

"(D) which meets the performance and quality standards (if any) which—

"(i) have been prescribed by the Secretary by regulations, and

"(ii) are in effect at the time of the acquisition of the item.

"(4) OTHER ENERGY-CONSERVING COMPONENT.—The term 'other energy-conserving component' means any item (other than insulation)—

"(A) which is—

"(i) a furnace replacement burner designed to achieve a reduction in the amount of fuel consumed as a result of increased combustion efficiency,

"(ii) a device for modifying flue openings designed to increase the efficiency of operation of the heating system,

"(iii) an electrical or mechanical furnace ignition system, which replaces a gas pilot light,

"(iv) a storm or thermal window or door for the exterior of the dwelling,

"(v) an automatic energy-saving setback thermostat,

"(vi) caulking or weatherstripping of an exterior door or window,

"(vii) a meter which displays the cost of energy usage, or

"(viii) an item of the kind which the Secretary specifies by regulations as increasing the energy efficiency of the dwelling,

"(B) the original use of which begins with the taxpayer,

"(C) which can reasonably be expected to remain in operation for at least 3 years, and

"(D) which meets the performance and quality standards (if any) which—

"(i) have been prescribed by the Secretary by regulations, and

"(ii) are in effect at the time of the acquisition of the item.

"(5) RENEWABLE ENERGY SOURCE PROPERTY.—The term 'renewable energy source property' means property—

"(A) which, when installed in connection with a dwelling, transmits or uses—

"(i) solar energy, energy derived from the geothermal deposits (as defined in section 613(e)(3)), or any other form of renewable energy which the Secretary specifies by regulations, for the purpose of heating or cooling such dwelling or providing hot water for use within such dwelling, or

Post, p. 3203.

"(ii) wind energy for nonbusiness residential purposes,

"(B) the original use of which begins with the taxpayer,

"(C) which can reasonably be expected to remain in operation for at least 5 years, and

"(D) which meets the performance and quality standards (if any) which—

"(i) have been prescribed by the Secretary by regulations, and

"(ii) are in effect at the time of the acquisition of the property.

"(6) REGULATIONS.—

"(A) CRITERIA; CERTIFICATION PROCEDURES.—The Secretary shall by regulations—

"(i) establish the criteria which are to be used in (I) prescribing performance and quality standards under paragraphs (3), (4), and (5), or (II) specifying any item under paragraph (4)(A)(viii) or any form of renewable energy under paragraph (5)(A)(i), and

"(ii) establish a procedure under which a manufacturer of an item may request the Secretary to certify that the item will be treated, for purposes of this section, as insulation, an energy-conserving component, or renewable energy source property.

"(B) CONSULTATION.—Performance and quality standards regulations and other regulations shall be prescribed by the Secretary under paragraphs (3), (4), and (5) and under this paragraph only after consultation with the Secretary of Energy, the Secretary of Housing and Urban Development, and other appropriate Federal officers.

"(7) WHEN EXPENDITURES MADE; AMOUNT OF EXPENDITURES.—

"(A) IN GENERAL.—Except as provided in subparagraph (B), an expenditure with respect to an item shall be treated as made when original installation of the item is completed.

"(B) RENEWABLE ENERGY SOURCE EXPENDITURES.—In the case of renewable energy source expenditures in connection with the construction or reconstruction of a dwelling, such expenditures shall be treated as made when the original use of the constructed or reconstructed dwelling by the taxpayer begins.

"(C) AMOUNT.—The amount of any expenditure shall be the cost thereof.

"(D) ALLOCATION IN CERTAIN CASES.—If less than 80 percent of the use of an item is for nonbusiness residential purposes, only that portion of the expenditures for such item which is properly allocable to use for nonbusiness residential purposes shall be taken into account. For purposes of this subparagraph, use for a swimming pool shall be treated as use which is not for residential purposes.

"(8) PRINCIPAL RESIDENCE.—The determination of whether or not a dwelling unit is a taxpayer's principal residence shall be made under principles similar to those applicable to section 1034, except that—

26 USC 1034.

"(A) no ownership requirement shall be imposed, and

"(B) the period for which a dwelling is treated as the principal residence of the taxpayer shall include the 30-day period ending on the first day on which it would (but for this subparagraph) be treated as his principal residence.

"(d) SPECIAL RULES.—For purposes of this section—

"(1) DOLLAR AMOUNTS IN CASE OF JOINT OCCUPANCY.—In the case of any dwelling unit which is jointly occupied and used during any calendar year as a principal residence by 2 or more individuals—

"(A) the amount of the credit allowable under subsection (a) by reason of energy conservation expenditures or by reason of renewable energy source expenditures (as the case may be) made during such calendar year by any of such individuals with respect to such dwelling unit shall be determined by treating all of such individuals as one taxpayer whose taxable year is such calendar year; and

"(B) there shall be allowable with respect to such expenditures to each of such individuals a credit under subsection (a) for the taxable year in which such calendar year ends in an amount which bears the same ratio to the amount determined under subparagraph (A) as the amount of such expenditures made by such individual during such calendar year bears to

the aggregate of such expenditures made by all of such individuals during such calendar year.

"(2) TENANT-STOCKHOLDER IN COOPERATIVE HOUSING CORPORATION.—In the case of an individual who is a tenant-stockholder (as defined in section 216) in a cooperative housing corporation (as defined in such section), such individual shall be treated as having made his tenant-stockholder's proportionate share (as defined in section 216(b)(3)) of any expenditures of such corporation.

26 USC 216.

"(3) CONDOMINIUMS.—

"(A) IN GENERAL.—In the case of an individual who is a member of a condominium management association with respect to a condominium which he owns, such individual shall be treated as having made his proportionate share of any expenditures of such association.

"(B) CONDOMINIUM MANAGEMENT ASSOCIATION.—For purposes of this paragraph, the term 'condominium management association' means an organization which meets the requirements of paragraph (1) of section 528(c) (other than subparagraph (E) thereof) with respect to a condominium project substantially all of the units of which are used as residences.

26 USC 528.

"(4) 1977 EXPENDITURES ALLOWED FOR 1978.—

"(A) NO CREDIT FOR TAXABLE YEARS BEGINNING BEFORE 1978.—No credit shall be allowed under this section for any taxable year beginning before January 1, 1978.

"(B) 1977 EXPENDITURES ALLOWED FOR 1978.—In the case of the taxpayer's first taxable year beginning after December 31, 1977, this section shall be applied by taking into account the period beginning April 20, 1977, and ending on the last day of such first taxable year.

"(e) BASIS ADJUSTMENTS.—For purposes of this subtitle, if a credit is allowed under this section for any expenditure with respect to any property, the increase in the basis of such property which would (but for this subsection) result from such expenditure shall be reduced by the amount of the credit so allowed.

"(f) TERMINATION.—This section shall not apply to expenditures made after December 31, 1985."

(b) TECHNICAL AND CLERICAL AMENDMENTS.—

(1) The table of sections for subpart A of part IV of subchapter A of chapter 1 is amended by inserting after the item relating to section 44B the following new item:

"Sec. 44C. Residential energy credit."

(2) Subsection (c) of section 56 (defining regular tax deduction) is amended by striking out "credits allowable under—" and all that follows and inserting in lieu thereof "credits allowable under subpart A of part IV other than under sections 31, 39, and 43."

26 USC 56.

26 USC 31, 39, 43.

(3) Subsection (a) of section 1016 (relating to adjustments to basis) is amended by inserting after paragraph (20) the following new paragraph:

26 USC 1016.

"(21) to the extent provided in section 44C(e), in the case of property with respect to which a credit has been allowed under section 44C;".

Ante, p. 3175.

26 USC 6096.

(4) Subsection (b) of section 6096 (relating to designation of income tax payments to Presidential Election Campaign Fund) is amended by striking out "and 44B" and inserting in lieu thereof "44B, and 44C".

26 USC 44C note.

(c) EFFECTIVE DATE.— The amendments made by this section shall apply to taxable years ending on or after April 20, 1977.

TITLE II—TRANSPORTATION

PART I—GAS GUZZLER TAX

SEC. 201. GAS GUZZLER TAX.

(a) GENERAL RULE.—Part I of subchapter A of chapter 32 (relating to motor vehicle excise taxes) is amended by adding at the end thereof the following new section:

26 USC 4064.

"SEC. 4064. GAS GUZZLER TAX.

"(a) IMPOSITION OF TAX.—There is hereby imposed on the sale by the manufacturer of each automobile a tax determined in accordance with the following tables:

"(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) DEFINITIONS.—For purposes of this section—

"(1) AUTOMOBILE.—

"(A) IN GENERAL.—The term 'automobile' means any 4-wheeled vehicle propelled by fuel—

"(i) which is manufactured primarily for use on public streets, roads, and highways (except any vehicle operated exclusively on a rail or rails), and

"(ii) which is rated at 6,000 pounds gross vehicle weight or less.

"(B) EXCEPTION FOR CERTAIN VEHICLES.—The term 'automobile' does not include any vehicle which is treated as a nonpassenger automobile under the rules which were prescribed by the Secretary of Transportation for purposes of section 501 of the Motor Vehicle Information and Cost Savings Act (15 U.S.C. 2001) and which were in effect on the date of the enactment of this section.

"(C) EXCEPTION FOR EMERGENCY VEHICLES.—The term 'automobile' does not include any vehicle sold for use and used—

"(i) as an ambulance or combination ambulance-hearse,

"(ii) by the United States or by a State or local government for police or other law enforcement purposes, or

"(iii) for other emergency uses prescribed by the Secretary by regulations.

"(2) FUEL ECONOMY.—The term 'fuel economy' means the average number of miles traveled by an automobile per gallon of gasoline (or equivalent amount of other fuel) consumed, as determined by the EPA Administrator in accordance with procedures established under subsection (c).

"(3) MODEL TYPE.—The term 'model type' means a particular class of automobile as determined by regulation by the EPA Administrator.

"(4) MODEL YEAR.—The term 'model year', with reference to any specific calendar year, means a manufacturer's annual production period (as determined by the EPA Administrator) which includes January 1 of such calendar year. If a manufacturer has no annual production period, the term 'model year' means the calendar year.

"(5) MANUFACTURER.—The term 'manufacturer' includes a producer or importer.

"(6) EPA ADMINISTRATOR.—The term 'EPA Administrator' means the Administrator of the Environmental Protection Agency.

"(7) FUEL.—The term 'fuel' means gasoline and diesel fuel. The Secretary (after consultation with the Secretary of Transportation) may, by regulation, include any product of petroleum or natural gas within the meaning of such term if he determines that such inclusion is consistent with the need of the Nation to conserve energy.

"(c) DETERMINATION OF FUEL ECONOMY.—For purposes of this section—

"(1) IN GENERAL.—Fuel economy for any model type shall be measured in accordance with testing and calculation procedures established by the EPA Administrator by regulation. Procedures so established shall be the procedures utilized by the EPA Administrator for model year 1975 (weighted 55 percent urban cycle, and 45 percent highway cycle), or procedures which yield comparable results. Procedures under this subsection, to the extent practicable, shall require that fuel economy tests be conducted in conjunction with emissions tests conducted under section 206 of the Clean Air Act. The EPA Administrator shall report any measurements of fuel economy to the Secretary.

42 USC 7540.

"(2) SPECIAL RULE FOR FUELS OTHER THAN GASOLINE.—The EPA Administrator shall by regulation determine that quantity of any other fuel which is the equivalent of one gallon of gasoline.

"(3) TIME BY WHICH REGULATIONS MUST BE ISSUED.—Testing and calculation procedures applicable to a model year, and any amendment to such procedures (other than a technical or clerical amendment), shall be promulgated not less than 12 months before the model year to which such procedures apply.

"(d) SPECIAL RULES FOR SMALL MANUFACTURERS.—

"(1) IN GENERAL.—If, on the application of a small manufacturer, the Secretary determines that it is not feasible for such manufacturer to meet the tax-free fuel economy level for the model year with respect to all automobiles produced by such manufacturer or with respect to a model type produced by such manufacturer, the Secretary may by regulation prescribe an alternate rate schedule for such model year for all automobiles produced by such manufacturer or for such model type, as the

case may be. The alternate rate schedule shall be based on the maximum feasible fuel economy level which such manufacturer can meet for such model year with respect to all automobiles or with respect to such model type, as the case may be.

"(2) APPLICATION TO INCLUDE NECESSARY INFORMATION.—An application under this subsection for any model year shall contain such information as the Secretary may by regulations prescribe.

"(3) DETERMINATIONS TO BE MADE ONLY AFTER CONSULTATION.—Determinations under paragraph (1) shall be made by the Secretary only after consultation with the Secretary of Energy, the Secretary of Transportation, and other appropriate Federal officers.

"(4) SMALL MANUFACTURER DEFINED.—

"(A) IN GENERAL.—For purposes of this subsection, the term 'small manufacturer' means any manufacturer—

"(i) who manufactured (whether or not in the United States) fewer than 10,000 automobiles in the second model year preceding the model year for which the determination under paragraph (1) is being made, and

"(ii) who can reasonably be expected to manufacture (whether or not in the United States) fewer than 10,000 automobiles in the model year for which the determination under paragraph (1) is being made.

"(B) SPECIAL RULES.—For purposes of subparagraph (A)—

"(i) MANUFACTURER OF AUTOMOBILES PRODUCED ABROAD DETERMINED WITHOUT REGARD TO IMPORTATION.—The meaning of the term 'manufacturer' shall be determined without regard to subsection (b)(5).

"(ii) CONTROLLED GROUPS.—Persons who are members of the same controlled group of corporations shall be treated as one manufacturer. For purposes of the preceding sentence, the term 'controlled group of corporations' has the meaning given to such term by section 1563(a); except that 'more than 50 percent' shall be substituted for 'at least 80 percent' each place it appears in section 1563(a)."

26 USC 156

(b) REDUCTION IN BASIS OF AUTOMOBILE ON WHICH GAS GUZZLER TAX WAS IMPOSED.—Section 1016 (relating to adjustments to basis) is amended by redesignating subsection (d) as subsection (e) and by inserting after subsection (c) the following new subsection:

26 USC 101

"(d) REDUCTION IN BASIS OF AUTOMOBILE ON WHICH GAS GUZZLER TAX WAS IMPOSED.—If—

"(1) the taxpayer acquires any automobile with respect to which a tax was imposed by section 4064, and

Ante, p. 31

"(2) the use of such automobile by the taxpayer begins not more than 1 year after the date of the first sale for ultimate use of such automobile,

the basis of such automobile shall be reduced by the amount of the tax imposed by section 4064 with respect to such automobile. In the case of importation, if the date of entry or withdrawal from warehouse for consumption is later than the date of the first sale for ultimate use, such later date shall be substituted for the date of such first sale in the preceding sentence."

(c) DENIAL OF CERTAIN EXEMPTIONS AND REFUNDS.—

(1) TAX-FREE SALES.—Subsection (a) of section 4221 (relating to certain tax-free sales) is amended by adding at the end thereof the following new sentence:

26 USC 42

"Paragraphs (4) and (5) shall not apply to the tax imposed by section 4064."

Ante, p. 3180.
26 USC 4293.

(2) UNITED STATES AND POSSESSIONS.—Section 4293 (relating to exemption for United States and possessions) is amended by striking out "tax imposed by section 4121" and inserting in lieu thereof "taxes imposed by sections 4064 and 4121".

26 USC 6416.

(3) DENIAL OF REFUNDS FOR CERTAIN USES.—Paragraph (2) of section 6416(b) (relating to tax payments considered overpayments in the case of specified uses and resales) is amended by adding at the end thereof the following new sentence:

"Subparagraphs (C) and (D) shall not apply in the case of any tax paid under section 4064".

26 USC 4217.

(d) PAYMENT OF TAX IN CASE OF LEASED AUTOMOBILES.—Section 4217 (relating to leases) is amended by adding at the end thereof the following new subsection:

"(e) LEASES OF AUTOMOBILES SUBJECT TO GAS GUZZLER TAX.—

(1) IN GENERAL.—In the case of the lease of an automobile the sale of which by the manufacturer would be taxable under section 4064, the foregoing provisions of this section shall not apply, but, for purposes of this chapter—

"(A) the first lease of such automobile by the manufacturer shall be considered to be a sale, and

"(B) any lease of such automobile by the manufacturer after the first lease of such automobile shall not be considered to be a sale.

"(2) PAYMENT OF TAX.—In the case of a lease described in paragraph (1)(A)—

"(A) there shall be paid by the manufacturer on each lease payment that portion of the total gas guzzler tax which bears the same ratio to such total gas guzzler tax as such payment bears to the total amount to be paid under such lease,

"(B) if such lease is canceled, or the automobile is sold or otherwise disposed of, before the total gas guzzler tax is payable, there shall be paid by the manufacturer on such cancellation, sale, or disposition the difference between the tax imposed under subparagraph (A) on the lease payments and the total gas guzzler tax, and

"(C) if the automobile is sold or otherwise disposed of after the total gas guzzler tax is payable, no tax shall be imposed under section 4064 on such sale or disposition.

"(3) DEFINITIONS.—For purposes of this subsection—

"(A) MANUFACTURER.—The term 'manufacturer' includes a producer or importer.

Ante, p. 3180.

"(B) TOTAL GAS GUZZLER TAX.—The term 'total gas guzzler tax' means the tax imposed by section 4064, computed at the rate in effect on the date of the first lease."

26 USC 4222.

(e) AUTHORITY TO EXTEND REGISTRATION SYSTEM TO EXEMPTION OF EMERGENCY VEHICLES.—Subsection (d) of section 4222 (relating to registration in the case of certain other exemptions) is amended by inserting "4064(b)(1)(C)," after "4063(b),".

(f) CLERICAL AMENDMENT.—The table of sections for part I of subchapter A of chapter 32 is amended by adding at the end thereof the following new item:

"Sec. 4064. Gas guzzler tax."

26 USC 4064 note.
26 USC 4064.

(g) EFFECTIVE DATE.—The amendments made by this section shall apply with respect to 1980 and later model year automobiles (as defined in section 4064(b) of the Internal Revenue Code of 1954).

PART II—MOTOR FUELS

SEC. 221. EXEMPTION FROM MOTOR FUELS EXCISE TAXES FOR CERTAIN ALCOHOL FUELS.

(a) GASOLINE MIXED WITH ALCOHOL.—

(1) IN GENERAL.—Section 4081 (relating to imposition of tax on gasoline) is amended by adding at the end thereof the following new subsection: 26 USC 4081.

"(c) GASOLINE MIXED WITH ALCOHOL.—

"(1) IN GENERAL.—Under regulations prescribed by the Secretary, no tax shall be imposed by this section on the sale of any gasoline—

"(A) in a mixture with alcohol, if at least 10 percent of the mixture is alcohol, or

"(B) for use in producing a mixture at least 10 percent of which is alcohol.

"(2) LATER SEPARATION OF GASOLINE.—If any person separates the gasoline from a mixture of gasoline and alcohol on which tax was not imposed by reason of this subsection, such person shall be treated as the producer of such gasoline.

"(3) ALCOHOL DEFINED.—For purposes of this subsection, the term 'alcohol' includes methanol and ethanol but does not include alcohol produced from petroleum, natural gas, or coal."

(2) EFFECTIVE DATE.—The amendment made by paragraph (1) shall apply to sales after December 31, 1978, and before October 1, 1984. 26 USC 4081 note.

(b) ALCOHOL MIXED WITH SPECIAL FUEL.—

(1) IN GENERAL.—Section 4041 (relating to imposition of tax on special fuels) is amended by adding at the end thereof the following new subsection: 26 USC 4041.

"(k) FUELS CONTAINING ALCOHOL.—

"(1) IN GENERAL.—Under regulations prescribed by the Secretary, no tax shall be imposed by this section on the sale or use of any liquid fuel at least 10 percent of which consists of alcohol (as defined by section 4081(c)(3)).

"(2) LATER SEPARATION.—If any person separates the liquid fuel from a mixture of the liquid fuel and alcohol on which tax was not imposed by reason of this subsection, such separation shall be treated as a sale of the liquid fuel."

(2) EFFECTIVE DATE.—The amendment made by paragraph (1) shall apply to sales or use after December 31, 1978, and before October 1, 1984. 26 USC 4041 note.

(c) REPORTS.— 26 USC 4041 note.

(1) ANNUAL REPORT.—On April 1 of each year, beginning with April 1, 1980, and ending on April 1, 1984, the Secretary of Energy, in consultation with the Secretary of the Treasury and the Secretary of Transportation, shall submit to the Congress a report on the use of alcohol in fuel. The report shall include— Report to Congress.

(A) a description of the firms engaged in the alcohol fuel industry,

(B) the amount of alcohol fuels sold in each State, and the amount of gasoline saved in each State by reason of the use of alcohol fuels,

(C) the revenue loss resulting from the exemptions from tax for alcohol fuels under sections 4041(k) and 4081(c) of the Internal Revenue Code of 1954, and 26 USC 4041, 4081.

(D) the cost of production and the retail cost of alcohol fuels as compared to gasoline and special fuels before the imposition of any Federal excise taxes.

Report to Congress.

(2) REPORT.—The report submitted to the Congress on April 1, 1984, shall contain, in addition to the information required under paragraph (1), an analysis of the effect on the alcohol fuel industry of the termination of the exemption from excise taxes provided under sections 4041(k) and 4081(c) of the Internal Revenue Code of 1954.

26 USC 4041, 4081.
26 USC 4081 note.

(d) EXPEDITION OF CERTAIN ETHANOL PRODUCTION APPLICATIONS.—The Secretary of the Treasury shall expedite, to the maximum extent possible, action on the application of any person with respect to the production of ethanol for use in producing gasoline described in section 4081(c) (or in producing liquid fuel described in section 4041(k)) of the Internal Revenue Code of 1954. Within 6 months after the date of the enactment of this Act, the Secretary shall furnish to the Committee on Finance, United States Senate, and to the Committee on Ways and Means, United States House of Representatives, recommendations for legislation necessary to provide for changes in the provisions of chapter 51 of the Internal Revenue Code of 1954 to provide a simple, expeditious procedure for processing such applications and to simplify the regulation of such persons for purposes of such chapter consistent with adequate safeguards against the use of such applications to avoid or evade compliance with the provisions of such chapter relating to distilled spirits procured, dealt in, or used for other purposes.

Legislative recommendations to congressional committees.

26 USC 5001 *et seq.*

SEC. 222. DENIAL OF CREDIT OR REFUND FOR NONBUSINESS NONHIGHWAY USE OF GASOLINE, SPECIAL MOTOR FUELS, AND LUBRICATING OIL.

(a) IN GENERAL.—

(1) GASOLINE.—

26 USC 6421.

(A) So much of the first sentence of section 6421(a) (relating to nonhighway uses) as precedes "the Secretary" is amended to read as follows: "Except as provided in subsection (i), if gasoline is used in a qualified business use,".

(B) Subsection (d) of section 6421 (relating to definitions) is amended by adding at the end thereof the following new paragraph:

"(3) QUALIFIED BUSINESS USE.—

"(A) IN GENERAL.—The term 'qualified business use' means any use by a person in a trade or business of such person or in an activity of such person described in section 212 (relating to production of income) otherwise than as a fuel in a highway vehicle—

26 USC 212.

"(i) which (at the time of such use), is registered, or is required to be registered, for highway use under the laws of any State or foreign country, or

"(ii) which, in the case of a highway vehicle owned by the United States, is used on the highway.

"(B) EXCEPTION FOR USE IN MOTORBOATS.—The term 'qualified business use' does not include any use in a motorboat.

"(C) COMMERCIAL FISHING VESSELS.—For provisions exempting from tax gasoline, special motor fuels, and lubricating oil used for commercial fishing vessels, see—

26 USC 4221.

"(i) subsections (a)(3) and (d)(3) of section 4221 (relating to certain tax-free sales),

"(ii) section 6416(b)(2)(B) (relating to refund or credit in case of certain uses), and 26 USC 6416.

"(iii) section 4041(g)(1) (relating to exemptions from tax on special fuels)." 26 USC 4041.

(2) SPECIAL MOTOR FUELS.—Subsection (b) of section 4041 (relating to special motor fuels) is amended by striking out the second and third sentences and inserting in lieu thereof the following:

"In the case of a liquid taxable under this subsection sold for use, or used, in a qualified business use, the tax imposed by paragraph (1) or by paragraph (2) shall be 2 cents a gallon. If a liquid on which tax was imposed by paragraph (1) at the rate of 2 cents a gallon by reason of the preceding sentence is used otherwise than in a qualified business use, a tax of 2 cents a gallon shall be imposed under paragraph (2). For purposes of this subsection, the term 'qualified business use' has the meaning given to such term by section 6421(d)(3)." 26 USC 6421.

(3) LUBRICATING OIL.—Subsection (a) of section 6424 (relating to lubricating oil not used in highway motor vehicles) is amended by striking out "is used otherwise than in a highway motor vehicle" and inserting in lieu thereof "is used in a qualified business use (within the meaning of section 6421(d)(3))". 26 USC 6424.

(b) EFFECTIVE DATE.—The amendments made by subsection (a) shall apply with respect to uses after December 31, 1978. 26 USC 4041 note.

PART III—PROVISIONS RELATED TO BUSES

SEC. 231. REMOVAL OF EXCISE TAX ON BUSES.

(a) GENERAL RULE.—Paragraph (6) of section 4063(a) (relating to exemption for local transit buses) is amended to read as follows: 26 USC 4063.

"(6) BUSES.—The tax imposed under section 4061(a) shall not apply in the case of any automobile bus chassis or automobile bus body." 26 USC 4061.

(b) FLOOR STOCKS REFUNDS.— 26 USC 4063 note.

(1) IN GENERAL.—Where, before the day after the date of the enactment of this Act, any tax-repealed article (as defined in subsection (e)) has been sold by the manufacturer, producer, or importer and on such day is held by a dealer and has not been used and is intended for sale, there shall be credited or refunded (without interest) to the manufacturer, producer, or importer an amount equal to the tax paid by such manufacturer, producer, or importer on his sale of the article, if—

(A) claim for such credit or refund is filed with the Secretary of the Treasury before the first day of the 10th calendar month beginning after the day after the date of the enactment of this Act based upon a request submitted to the manufacturer, producer, or importer before the first day of the 7th calendar month beginning after the day after the date of the enactment of this Act by the dealer who held the article in respect of which the credit or refunds is claimed; and

(B) on or before the first day of such 10th calendar month reimbursement has been made to the dealer by the manufacturer, producer, or importer in an amount equal to the tax paid on the article or written consent has been obtained from the dealer to allowance of the credit or refund.

(2) LIMITATION ON ELIGIBILITY FOR CREDIT OR REFUND.—No manufacturer, producer, or importer shall be entitled to credit or refund under paragraph (1) unless he has in his possession such

evidence of the inventories with respect to which the credit or refund is claimed as may be required by regulations prescribed by the Secretary of the Treasury under this subsection.

(3) OTHER LAWS APPLICABLE.—All provisions of law, including penalties, applicable with respect to the taxes imposed by section 4061(a) of the Internal Revenue Code of 1954 shall, insofar as applicable and not inconsistent with paragraphs (1) and (2) of this subsection, apply in respect of the credits and refunds provided for in paragraph (1) to the same extent as if the credits or refunds constituted overpayments of the tax.

26 USC 4061.

(c) REFUNDS WITH RESPECT TO CERTAIN CONSUMER PURCHASES.—

(1) IN GENERAL.—Except as otherwise provided in paragraph (2), where on or after April 20, 1977, and on or before the date of the enactment of this Act, a tax-repealed article (as defined in subsection (e)) has been sold to an ultimate purchaser, there shall be credited or refunded (without interest) to the manufacturer, producer, or importer of such article an amount equal to the tax paid by such manufacturer, producer, or importer on his sale of the article.

(2) LIMITATION ON ELIGIBILITY FOR CREDIT OR REFUND.—No manufacturer, producer, or importer shall be entitled to a credit or refund under paragraph (1) with respect to an article unless—

(A) he has in his possession such evidence of the sale of the article to an ultimate purchaser, and of the reimbursement of the tax to such purchaser, as may be required by regulations prescribed by the Secretary of the Treasury under this subsection;

(B) claim for such credit or refund is filed with the Secretary of the Treasury before the first day of the 10th calendar month beginning after the day after the date of the enactment of this Act based upon information submitted to the manufacturer, producer, or importer before the first day of the 7th calendar month beginning after the day after the date of the enactment of this Act by the person who sold the article (in respect of which the credit or refund is claimed) to the ultimate purchaser; and

(C) on or before the first day of such 10th calendar month reimbursement has been made to the ultimate purchaser in an amount equal to the tax paid on the article.

(3) OTHER LAWS APPLICABLE.—All provisions of laws, including penalties, applicable with respect to the taxes imposed by section 4061(a) of such Code shall, insofar as applicable and not inconsistent with paragraph (1) or (2) of this subsection, apply with respect to the credits and refunds provided for in paragraph (1) to the same extent as if the credits or refunds constituted overpayment of the tax.

(d) CERTAIN USES BY MANUFACTURER, ETC.—Any tax paid by reason of section 4218(a) of such Code (relating to use by manufacturer or importer considered sale) on any tax-repealed article shall be deemed an overpayment of such tax if the tax was imposed on such article by reason of such section 4218(a) on or after April 20, 1977.

26 USC 4218.

(e) DEFINITIONS.—For purposes of this section—

(1) The term "dealer" includes a wholesaler, jobber, distributor, or retailer.

(2) An article shall be considered as "held by a dealer" if title thereto has passed to such dealer (whether or not delivery to him has been made) and if, for purposes of consumption, title to

such article or possession thereof has not at any time been transferred to any person other than a dealer.

(3) The term "tax-repealed article" means an article on which a tax was imposed by section 4061(a) of such Code (as in effect on the day before the date of the enactment of this Act) and which is exempted from such tax by paragraph (6) of section 4063(a) of such Code (as amended by subsection (a) of this section).

26 USC 4061.

26 USC 4063.

(f) TECHNICAL AND CONFORMING AMENDMENTS.—

(1) The heading for paragraph (1) of section 6412(a) (relating to floor stocks refunds) is amended by striking out "AND BUSES".

26 USC 6412.

(2) Subsection (d) of section 4222 (relating to registration in case of certain other exemptions) is amended by striking out "4063(a) (6) or (7)" and inserting in lieu thereof "4063(a)(7)".

26 USC 4222.

(g) EFFECTIVE DATE.—

26 USC 4063 note.

(1) The amendments made by subsections (a) and (f) shall apply with respect to articles sold after the date of the enactment of this Act.

(2) For purposes of paragraph (1), an article shall not be considered sold on or before the date of the enactment of this Act unless possession or right to possession passes to the purchaser on or before such date.

(3) In the case of—

(A) a lease,

(B) a contract for the sale of an article providing that the price shall be paid by installments and title to the article sold does not pass until a future date notwithstanding partial payment by installments,

(C) a conditional sale, or

(D) a chattel mortgage arrangement providing that the sale price shall be paid in installments,

entered into on or before the date of the enactment of this Act, payments made after such date with respect to the article leased or sold shall, for purposes of this subsection, be considered as payments made with respect to an article sold after such date, if the lessor or vendor establishes that the amount of payments payable after such date with respect to such article has been reduced by an amount equal to that portion of the tax applicable with respect to the lease or sale of such article which is due and payable after such date. If the lessor or vendor does not establish that the payments have been so reduced, they shall be treated as payments made in respect of an article sold on or before the date of the enactment of this Act.

SEC. 232. REMOVAL OF EXCISE TAX ON BUS PARTS.

(a) EXEMPT SALES.—Subsection (e) of section 4221 (relating to special rules for certain tax-free sales) is amended by adding at the end thereof the following new paragraph:

26 USC 4221.

"(6) BUS PARTS AND ACCESSORIES.—Under regulations prescribed by the Secretary, the tax imposed by section 4061(b) shall not apply to any part or accessory which is sold for use by the purchaser on or in connection with an automobile bus."

(b) REFUND FOR CERTAIN SALES OF BUS PARTS.—Subparagraph (I) of section 6416(b)(2) (relating to refund for specified uses and resales) is amended to read as follows:

26 USC 6416.

"(I) in the case of any article taxable under section 4061 (b), sold for use by the purchaser on or in connection with an automobile bus;".

26 USC 4221 note.

(c) EFFECTIVE DATE.—The amendments made by this section shall apply to sales on or after the first day of the first calendar month beginning more than 10 days after the date of the enactment of this Act.

SEC. 233. REMOVAL OF EXCISE TAX ON FUEL, OIL, AND TIRES USED IN CONNECTION WITH INTERCITY, LOCAL, AND SCHOOL BUSES.

(a) REPAYMENT OF TAX ON GASOLINE AND OTHER MOTOR FUELS USED BY INTERCITY, LOCAL, OR SCHOOL BUSES.—

26 USC 6421.

(1) GASOLINE.—Subsection (b) of section 6421 (relating to local transit systems) is amended to read as follows:

"(b) INTERCITY, LOCAL, OR SCHOOL BUSES.—

"(1) ALLOWANCE.—Except as provided in paragraph (2) and subsection (i), if gasoline is used in an automobile bus while engaged in—

"(A) furnishing (for compensation) passenger land transportation available to the general public, or

26 USC 4221.

"(B) the transportation of students and employees of schools (as defined in the last sentence of section 4221(d)(7)(C)),

the Secretary shall pay (without interest) to the ultimate purchaser of such gasoline an amount equal to the product of the number of gallons of gasoline so used multiplied by the rate at which tax was imposed on such gasoline by section 4081.

26 USC 4081.

"(2) LIMITATION IN CASE OF NONSCHEDULED INTERCITY OR LOCAL BUSES.—Paragraph (1)(A) shall not apply in respect of gasoline used in any automobile bus while engaged in furnishing transportation which is not scheduled and not along regular routes unless the seating capacity of such bus is at least 20 adults (not including the driver)."

26 USC 6427.

(2) OTHER FUELS.—Subsection (b) of section 6427 (relating to local transit systems) is amended to read as follows:

"(b) INTERCITY, LOCAL, OR SCHOOL BUSES.—

"(1) ALLOWANCE.—Except as provided in paragraph (2) and subsection (g), if any fuel on the sale of which tax was imposed by subsection (a) or (b) of section 4041 is used in an automobile bus while engaged in—

26 USC 4041.

"(A) furnishing (for compensation) passenger land transportation available to the general public, or

"(B) the transportation of students and employees of schools (as defined in the last sentence of section 4221(d)(7)(C)),

the Secretary shall pay (without interest) to the ultimate purchaser of such fuel an amount equal to the product of the number of gallons of such fuel so used multiplied by the rate at which tax was imposed on such fuel by subsection (a) or (b) of section 4041.

"(2) LIMITATION IN CASE OF NONSCHEDULED INTERCITY OR LOCAL BUSES.—Paragraph (1)(A) shall not apply in respect of fuel used in any automobile bus while engaged in furnishing transportation which is not scheduled and not along regular routes unless the seating capacity of such bus is at least 20 adults (not including the driver)."

(3) TECHNICAL AMENDMENTS.—

26 USC 6421.

(A) Subsection (d) of section 6421 is amended—

(i) by striking out paragraph (2), and

(ii) by redesignating paragraph (3) (as added by section 222(a)(1)(B)) as paragraph (2).

Ante, p. 3186.

(B) The last sentence of section 4041(b) (as added by section 222(a)(2)) is amended by striking out "6421(d)(3)" and inserting in lieu thereof "6421(d)(2)". 26 USC 4041.

(C) Subsection (c) of section 4483 is amended by inserting "(as in effect on the day before the date of the enactment of the Energy Tax Act of 1978)" after "section 6421(b)(2)". 26 USC 4483.

(b) REPAYMENT OF TAX ON LUBRICATING OIL USED IN INTERCITY, LOCAL, OR SCHOOL BUSES.—

(1) IN GENERAL.—Subsection (a) of section 6424 (relating to lubricating oil not used in highway motor vehicles) is amended to read as follows: 26 USC 6424.

"(a) PAYMENTS.—Except as provided in subsection (f), if lubricating oil (other than cutting oils, as defined in section 4092(b), and other than oil which has previously been used) is used— 26 USC 4092.

(1) in a qualified business use (as defined in section 6421(d)(2)), or 26 USC 6421.

"(2) in a qualified bus (as defined in section 4221(d)(7)), 26 USC 4221.

the Secretary shall pay (without interest) to the ultimate purchaser of such lubricating oil an amount equal to 6 cents for each gallon of lubricating oil so used."

(2) TECHNICAL AND CONFORMING AMENDMENTS.—

(A) The section heading for section 6424 is amended by striking out "NOT USED IN HIGHWAY MOTOR VEHICLES" and inserting in lieu thereof "USED FOR CERTAIN NONTAXABLE PURPOSES". 26 USC 6424.

(B) The table of sections for subchapter B of chapter 65 (relating to rules of special application) is amended by striking out "not used in highway motor vehicles" in the item relating to section 6424 and inserting in lieu thereof "used for certain nontaxable purposes". 26 USC 6411.

(C) Paragraph (3) of section 39(a) (relating to certain uses of gasoline, special fuels, and lubricating oil) is amended by striking out "otherwise than in a highway motor vehicle" and inserting in lieu thereof "for certain nontaxable purposes". 26 USC 39.

(D) Sections 6504(9) and 6675(a) are each amended by striking out "not used in highway motor vehicles" and inserting in lieu thereof "used for certain nontaxable purposes". 26 USC 6504, 6675.

(E) Paragraph (3) of section 209(f) of the Highway Revenue Act of 1956 is amended by striking out "lubricating oil not used in highway motor vehicles" and inserting in lieu thereof "lubricating oil used for certain nontaxable purposes". 23 USC 120 note.

(c) TIRES, TUBES, AND TREAD RUBBER.—

(1) IN GENERAL.—Paragraph (5) of section 4221(e) (relating to school buses) is amended to read as follows: 26 USC 4221.

"(5) TIRES, TUBES, AND TREAD RUBBER USED ON INTERCITY, LOCAL, AND SCHOOL BUSES.—Under regulations prescribed by the Secretary—

"(A) the taxes imposed by paragraphs (1) and (3) of section 4071(a) shall not apply in the case of tires or inner tubes for tires sold for use by the purchaser on or in connection with a qualified bus, and 26 USC 4071.

"(B) the tax imposed by paragraph (4) of section 4071(a) shall not apply in the case of tread rubber sold for use by the purchaser in the recapping or retreading of any tire to

be used by the purchaser on or in connection with a qualified bus."

26 USC 4221.

(2) QUALIFIED BUS DEFINED.—Subsection (d) of section 4221 (relating to definitions) is amended by adding at the end thereof the following new paragraph:

"(7) QUALIFIED BUS.—

"(A) IN GENERAL.—The term 'qualified bus' means—

"(i) an intercity or local bus, and

"(ii) a school bus.

"(B) INTERCITY OR LOCAL BUS.—The term 'intercity or local bus' means any automobile bus which is used predominantly in furnishing (for compensation) passenger land transportation available to the general public if—

"(i) such transportation is scheduled and along regular routes, or

"(ii) the seating capacity of such bus is at least 20 adults (not including the driver).

"(C) SCHOOL BUS.—The term 'school bus' means any automobile bus substantially all the use of which is in transporting students and employees of schools. For purposes of the preceding sentence, the term 'school' means an educational organization which normally maintains a regular faculty and curriculum and normally has a regularly enrolled body of pupils or students in attendance at the place where its educational activities are carried on."

26 USC 6416.

(3) TECHNICAL AMENDMENT.—Paragraph (2) of section 6416 (b) (relating to specified uses and resales) is amended by striking out the period at the end of subparagraph (K) and inserting in lieu thereof a semicolon and by inserting after subparagraph (K) the following new subparagraphs:

26 USC 4071.

"(L) in the case of any tire or inner tube taxable under paragraph (1) or (3) of section 4071(a), sold to any person for use as described in section 4221(e)(5)(A); or

"(M) in the case of tread rubber taxable under paragraph (4) of section 4071(a), used in the recapping or retreading of a tire sold to any person for use on or in connection with a qualified bus (as defined in section 4221(d)(7))."

26 USC 39 note.

(d) EFFECTIVE DATE.—The amendments made by this section shall take effect on the first day of the first calendar month which begins more than 10 days after the date of the enactment of this Act.

PART IV—INCENTIVES FOR VAN POOLING

SEC. 241. FULL INVESTMENT CREDIT FOR CERTAIN COMMUTER VEHICLES.

26 USC 46.

(a) IN GENERAL.—Subsection (c) of section 46 (relating to qualified investment) is amended by adding at the end thereof the following new paragraph:

"(6) SPECIAL RULE FOR COMMUTER HIGHWAY VEHICLES.—

"(A) IN GENERAL.—Notwithstanding paragraph (2), in the case of a commuter highway vehicle the useful life of which is 3 years or more, the applicable percentage for purposes of paragraph (1) shall be 100 percent.

"(B) DEFINITION OF COMMUTER HIGHWAY VEHICLE.—For purposes of subparagraph (A), the term 'commuter highway vehicle' means a highway vehicle—

"(i) the seating capacity of which is at least 8 adults (not including the driver),

"(ii) at least 80 percent of the mileage use of which can reasonably be expected to be (I) for purposes of transporting the taxpayer's employees between their residences and their place of employment, and (II) on trips during which the number of employees transported for such purposes is at least one-half of the adult seating capacity of such vehicle (not including the driver),

"(iii) which is acquired by the taxpayer on or after the date of the enactment of the Energy Tax Act of 1978, and placed in service by the taxpayer before January 1, 1986, and

Ante, p. 3174.

"(iv) with respect to which the taxpayer makes an election under this paragraph on his return for the taxable year in which such vehicle is placed in service."

(b) Amendments of the Recapture Rules.—

(1) Subsection (a) of section 47 (relating to recapture in case of certain dispositions, etc., of section 38 property) is amended by redesignating paragraph (4) as paragraph (5) and by inserting after paragraph (3) the following new paragraph:

26 USC 47.

"(4) Special rules for commuter highway vehicles.—

"(A) Useful life.—For purposes of this subsection, 3 years shall be treated as the useful life which was taken into account in computing the credit under section 38 with respect to any commuter highway vehicle (as defined in section 46 (c)(6)(B)).

26 USC 38.
Ante, p. 3192.

"(B) Change in use.—If less than 80 percent of the mileage use of any commuter highway vehicle by the taxpayer during that portion of any taxable year which is within the first 36 months of the operation of such vehicle by the taxpayer meets the requirements of section 46(c)(6)(B), then the tax under this chapter for such taxable year shall be increased by an amount equal to the aggregate decrease in the credits allowed under section 38 for all prior taxable years which would have resulted solely from treating such vehicle, for purposes of determining qualified investment, as not being a commuter highway vehicle. If the application of this subparagraph to any property is followed by the application of paragraph (1) to such property, proper adjustment shall be made in applying paragraph (1)."

(2) Paragraph (5) of section 47(a) (as redesignated by subparagraph (A)) is amended by striking out "paragraph (2)" and inserting in lieu thereof "paragraph (2) or (4)".

(3) Subparagraph (B) of section 47(a)(6) is amended by striking out "paragraph (4)" and inserting in lieu thereof "paragraph (5)".

SEC. 242. EXCLUSION FROM GROSS INCOME OF VALUE OF QUALIFIED TRANSPORTATION PROVIDED BY EMPLOYER.

(a) In General.—Part III of subchapter B of chapter 1 (relating to items specifically excluded from gross income) is amended by redesignating section 124 as 125, and by inserting after section 123 the following new section:

26 USC 101.
26 USC 124, 125.

"SEC. 124. QUALIFIED TRANSPORTATION PROVIDED BY EMPLOYER.

26 USC 124.

"(a) General Rule.—Gross income of an employee does not include the value of qualified transportation provided by the employer between the employee's residence and place of employment.

"(b) QUALIFIED TRANSPORTATION.—For purposes of this section, the term 'qualified transportation' means transportation in a commuter highway vehicle (as defined in section 46(c)(6)(B) but without regard to clause (iii) or (iv) thereof).

26 USC 46.

"(c) ADDITIONAL REQUIREMENTS.—Subsection (a) does not apply to the value of transportation provided by an employer unless—

"(1) such transportation is provided under a separate written plan of the employer which does not discriminate in favor of employees who are officers, shareholders, or highly compensated employees, and

"(2) the plan provides that the value of such transportation is provided in addition to (and not in lieu of) any compensation otherwise payable to the employee.

"(d) DEFINITIONS.—For purposes of this section—

"(1) PROVIDED BY THE EMPLOYER.—Transportation shall be considered to be provided by an employer if the transportation is furnished in a commuter highway vehicle (described in subsection (b)) operated by or for the employer.

"(2) EMPLOYEE.—The term 'employee' does not include an individual who is an employee (within the meaning of section 401(c)(1)).

26 USC 401.

"(e) EFFECTIVE DATE.—Subsection (a) applies with respect to qualified transportation provided in taxable years beginning after December 31, 1978, and before January 1, 1986".

(b) CLERICAL AMENDMENT.—The table of sections for such part is amended by striking out the last item and inserting in lieu thereof the following:

"Sec. 124. Qualified transportation provided by employer.
"Sec. 125. Cross references to other Acts."

26 USC 124 note. *Supra.*

(c) TRANSITION RULE.—The plan requirements of section 124(c) of the Internal Revenue Code of 1954 shall be considered to be met with respect to transportation provided before July 1, 1979, if there is a plan meeting such requirements of the employer in effect on that date.

TITLE III—CHANGES IN BUSINESS INVESTMENT CREDIT TO ENCOURAGE CONSERVATION OF, OR CONVERSION FROM, OIL AND GAS OR TO ENCOURAGE NEW ENERGY TECHNOLOGY

SEC. 301. CHANGES IN BUSINESS INVESTMENT CREDIT.

(a) AMOUNT OF CREDIT; ALLOWANCE OF ENERGY PERCENTAGE.—

26 USC 46.

(1) IN GENERAL.—Paragraph (2) of section 46(a) (relating to amount of credit for current taxable year) is amended to read as follows:

"(2) AMOUNT OF CREDIT.—

"(A) IN GENERAL.—The amount of the credit determined under this paragraph for the taxable year shall be an amount equal to the sum of the following percentages of the qualified investment (as determined under subsections (c) and (d)):

"(i) the regular percentage,

"(ii) in the case of energy property, the energy percentage, and

"(iii) the ESOP percentage.

"(B) REGULAR PERCENTAGE.—For purposes of this paragraph, the regular percentage is—

"(i) 10 percent with respect to the period beginning on January 21, 1975, and ending on December 31, 1980, or

"(ii) 7 percent with respect to the period beginning on January 1, 1981.

"(C) ENERGY PERCENTAGE.—For purposes of this paragraph, the energy percentage is—

"(i) 10 percent with respect to the period beginning on October 1, 1978, and ending on December 31, 1982, or

"(ii) zero with respect to any other period.

"(D) SPECIAL RULE FOR CERTAIN ENERGY PROPERTY.—For purposes of this paragraph, the regular percentage shall not apply to any energy property which, but for section 48(l)(1), would not be section 38 property.

26 USC 48.
26 USC 38.

"(E) ESOP PERCENTAGE.—For purposes of this paragraph, the ESOP percentage is—

"(i) with respect to the period beginning on January 21, 1975, and ending on December 31, 1980, 1 percent, and

"(ii) with respect to the period beginning on January 1, 1977, and ending on December 31, 1980, an additional percentage (not in excess of ½ of 1 percent) which results in an amount equal to the amount determined under section 301(e) of the Tax Reduction Act of 1975.

26 USC 46 note.

This subparagraph shall apply to a corporation only if it meets the requirements of section 301(d) of the Tax Reduction Act of 1975 and only if it elects (at such time, in such form, and in such manner as the Secretary prescribes) to have this subparagraph apply."

26 USC 46 note.

(2) CONFORMING AMENDMENTS.—

(A) Subparagraph (A) of section 46(c)(3) (relating to public utility property) is amended to read as follows:

26 USC 46.

"(A) For the period beginning on January 1, 1981, in the case of any property which is public utility property, the amount of the qualified investment shall be 4/7 of the amount determined under paragraph (1). The preceding sentence shall not apply for purposes of applying the energy percentage."

(B) The first sentence of section 46(f)(8) (relating to prohibition of immediate flow through) is amended by striking out "and the Tax Reform Act of 1976" and inserting in lieu thereof ", the Tax Reform Act of 1976, and the Energy Tax Act of 1978".

26 USC 1 note.
Ante, p. 3174.
26 USC 48.

(b) DEFINITIONS AND TRANSITIONAL RULES.—Section 48 (relating to definitions and special rules) is amended by redesignating subsection (l) as subsection (n) and by inserting after subsection (k) the following new subsections:

"(l) ENERGY PROPERTY.—For purposes of this subpart—

"(1) TREATMENT AS SECTION 38 PROPERTY.—For the period beginning on October 1, 1978, and ending on December 31, 1982—

"(A) any energy property shall be treated as meeting the requirements of paragraph (1) of subsection (a), and

"(B) paragraph (3) of subsection (a) shall not apply to any energy property.

"(2) ENERGY PROPERTY DEFINED.—The term 'energy property' means property—

"(A) which is—

"(i) alternative energy property,

"(ii) solar wind energy property,

"(iii) specially defined energy property,

"(iv) recycling equipment,

"(v) shale oil equipment, or

"(vi) equipment for producing natural gas from geopressured brine.

"(B)(i) the construction, reconstruction, or erection of which is completed by the taxpayer after September 30, 1978, or

"(ii) which is acquired after September 30, 1978, if the original use of such property commences with the taxpayer and commences after such date, and

"(C) with respect to which depreciation (or amortization in lieu of depreciation) is allowable, and which has a useful life (determined as of the time such property is placed in service) of 3 years or more.

"(3) ALTERNATIVE ENERGY PROPERTY.—

"(A) IN GENERAL.—The term 'alternative energy property' means—

"(i) a boiler the primary fuel for which will be an alternate substance,

"(ii) a burner (including necessary on-site equipment to bring the alternate substance to the burner) for a combustor other than a boiler if the primary fuel for such burner will be an alternate substance,

"(iii) equipment for converting an alternate substance into a synthetic liquid, gaseous, or solid fuel (other than coke or coke gas),

"(iv) equipment designed to modify existing equipment which uses oil or natural gas as a fuel or as feedstock so that such equipment will use either a substance other than oil and natural gas, or oil mixed with a substance other than oil and natural gas (where such other substance will provide not less than 25 percent of the fuel or feedstock),

"(v) equipment which uses coal (including lignite) as a feedstock for the manufacture of chemicals or other products (other than coke or coke gas),

"(vi) pollution control equipment required (by Federal, State, or local regulations) to be installed on or in connection with equipment described in clause (i), (ii), (iii), (iv), or (v),

"(vii) equipment used for the unloading, transfer, storage, reclaiming from storage, and preparation (including, but not limited to, washing, crushing, drying, and weighing) at the point of use of an alternate substance for use in equipment described in clause (i), (ii), (iii), (iv), (v), or (vi), and

"(viii) equipment used to produce, distribute, or use energy derived from a geothermal deposit (within the meaning of section 613(e)(3)), but only, in the case of electricity generated by geothermal power, up to (but not including) the electrical transmission stage.

Post, p. 3203.

"(B) Exclusion for public utility property.—The terms 'alternative energy property', 'solar or wind energy property', and 'recycling equipment' do not include property which is public utility property (within the meaning of section 46(f)(5)).

26 USC 46.

"(C) Alternate substance.—The term 'alternate substance' means any substance other than—

"(i) oil and natural gas, and

"(ii) any product of oil and natural gas.

"(D) Special rule for certain pollution control equipment.—The term 'pollution control equipment' does not include any equipment which—

"(i) is installed on or in connection with property which, as of October 1, 1978, was using coal (including lignite), and

"(ii) was required to be installed by Federal, State, or local regulations in effect on such date.

"(4) Solar or wind energy property.—The term 'solar or wind energy property' means any equipment which uses solar or wind energy—

"(A) to generate electricity, or

"(B) to heat or cool (or provide hot water for use in) a structure.

"(5) Specially defined energy property.—The term 'specially defined energy property' means—

"(A) a recuperator,

"(B) a heat wheel,

"(C) a regenerator,

"(D) a heat exchanger,

"(E) a waste heat boiler,

"(F) a heat pipe,

"(G) an automatic energy control system,

"(H) a turbulator,

"(I) a preheater,

"(J) a combustible gas recovery system,

"(K) an economizer, or

"(L) any other property of a kind specified by the Secretary by regulations,

the principal purpose of which is reducing the amount of energy consumed in any existing industrial or commercial process and which is installed in connection with an existing industrial or commercial facility.

"(6) Recycling equipment.—

"(A) In general.—The term 'recycling equipment' means any equipment which is used exclusively—

"(i) to sort and prepare solid waste for recycling, or

"(ii) in the recycling of solid waste.

"(B) Certain equipment not included.—The term 'recycling equipment' does not include—

"(i) any equipment used in a process after the first marketable product is produced, or

"(ii) in the case of recycling iron or steel, any equipment used to reduce the waste to a molten state and in any process thereafter.

"(C) 10 percent virgin material allowed.—Any equipment used in the recycling of material which

includes some virgin materials shall not be treated as failing to meet the exclusive use requirements of subparagraph (A) if the amount of such virgin materials is 10 percent or less.

"(D) CERTAIN EQUIPMENT INCLUDED.—The term 'recycling equipment' includes any equipment which is used in the conversion of solid waste into a fuel or into useful energy such as steam, electricity, or hot water.

"(7) SHALE OIL EQUIPMENT.—The term 'shale oil equipment' means equipment for producing or extracting oil from oil-bearing shale rock but does not include equipment for hydrogenation, refining, or other process subsequent to retorting.

"(8) EQUIPMENT FOR PRODUCING NATURAL GAS FROM GEOPRESSURED BRINE.—The term 'equipment for producing natural gas from geopressured brine' means equipment which is used exclusively to extract natural gas described in section 613A(b)(3)(C)(i).

26 USC 613A.

"(9) EQUIPMENT MUST MEET CERTAIN STANDARDS TO QUALIFY.—Equipment qualifies under paragraph (3), (4), (5), (6), (7), or (8) only if it meets the performance and quality standards (if any) which—

"(A) have been prescribed by the Secretary by regulations (after consultation with the Secretary of Energy), and

"(B) are in effect at the time of the acquisition of the property.

"(10) EXISTING.—For purposes of this subsection, the term 'existing' means—

"(A) when used in connection with a facility, 50 percent or more of the basis of such facility is attributable to construction, reconstruction, or erection before October 1, 1978, or

"(B) when used in connection with an industrial or commercial process, such process was carried on in the facility as of October 1, 1978.

"(11) SPECIAL RULE FOR PROPERTY FINANCED BY INDUSTRIAL DEVELOPMENT BONDS.—In the case of property which is financed in whole or in part by the proceeds of an industrial development bond (within the meaning of section 103(b)(2)) the interest on which is exempt from tax under section 103, the energy percentage shall be 5 percent.

26 USC 103.

"(12) INDUSTRIAL INCLUDES AGRICULTURAL.—The term 'industrial' includes agricultural.

"(m) APPLICATION OF CERTAIN TRANSITIONAL RULES.—Where the application of any provision of subsection (l) of this section or subsection (a)(2) or (c)(3) of section 46 is expressed in terms of a period, such provision shall apply only to—

26 USC 46.

"(1) property to which section 46(d) does not apply, the construction, reconstruction, or erection of which is completed by the taxpayer on or after the first day of such period, but only to the extent of the basis thereof attributable to the construction, reconstruction, or erection during such period,

"(2) property to which section 46(d) does not apply, acquired by the taxpayer during such period and placed in service by the taxpayer during such period, and

"(3) property to which section 46(d) applies, but only to the extent of the qualified investment (as determined under subsec-

tions (c) and (d) of section 46) with respect to qualified progress expenditures made during such period." 26 USC 46.

(c) SPECIAL RULES FOR APPLYING LIMITATION BASED ON TAX LIABILITY—

(1) Subsection (a) of section 46 is amended by adding at the end thereof the following new paragraph:

"(10) SPECIAL RULES IN THE CASE OF ENERGY PROPERTY.—Under regulations prescribed by the Secretary— Regulations.

"(A) IN GENERAL.—This subsection and subsection (b) shall be applied separately—

"(i) first with respect to so much of the credit allowed by section 38 as is not attributable to the energy percentage, 26 USC 38.

"(ii) second with respect to so much of the credit allowed by section 38 as is attributable to the application of the energy percentage to energy property (other than solar or wind energy property), and

"(iii) then with respect to so much of the credit allowed by section 38 as is attributable to the application of the energy percentage to solar or wind energy property.

"(B) RULES OF APPLICATION FOR ENERGY PROPERTY OTHER THAN SOLAR OR WIND ENERGY PROPERTY.—In applying this subsection and subsection (b) for taxable years ending after September 30, 1978, with respect to so much of the credit allowed by section 38 as is described in subparagraph (A)(ii)—

"(i) paragraph (3)(C) shall be applied by substituting '100 percent' for '50 percent',

"(ii) paragraphs (7), (8), and (9) shall not apply, and

"(iii) the liability for tax shall be the amount determined under paragraph (4) reduced by so much of the credit allowed by section 38 as is described in subparagraph (A)(i).

"(C) REFUNDABLE CREDIT FOR SOLAR OR WIND ENERGY PROPERTY.—In the case of so much of the credit allowed by section 38 as is described in subparagraph (A)(iii)—

"(i) paragraph (3) shall not apply, and

"(ii) for purposes of this title (other than section 38, this subpart, and chapter 63), such credit shall be treated as if it were allowed by section 39 and not by section 38." 26 USC 31, 6201. 26 USC 39.

(2) Section 6401 (relating to amounts treated as overpayments) is amended by adding at the end thereof the following new subsection: 26 USC 6401.

"(d) CROSS REFERENCE.—

"For rule allowing refund for excess investment credit attributable to solar or wind energy property, see section 46(a)(10)(C)."

(d) DENIAL OF INVESTMENT TAX CREDIT FOR CERTAIN PROPERTY.—

(1) AIR CONDITIONING, SPACE HEATERS, ETC.—Subparagraph (A) of section 48(a)(1) (defining section 38 property) is amended to read as follows: 26 USC 48.

"(A) tangible personal property (other than an air conditioning or heating unit), or".

26 USC 48.

(2) BOILERS FUELED BY OIL OR GAS.—Subsection (a) of section 48 (defining section 38 property) is amended by adding at the end thereof the following new paragraph:

"(10) BOILERS FUELED BY OIL OR GAS.—

"(A) IN GENERAL.—The term 'section 38 property' does not include any boiler primarily fueled by petroleum or petroleum products (including natural gas) unless the use of coal is precluded by Federal air pollution regulations (or by State air pollution regulations in effect on October 1, 1978) or unless the use of such boiler will be an exempt use within the meaning of subparagraph (B).

"(B) EXEMPT USE DEFINED.—For purposes of subparagraph (A), the term 'exempt use' means—

"(i) use in an apartment, hotel, motel, or other residential facility,

"(ii) use in a vehicle, aircraft, or vessel, or in transportation by pipeline,

26 USC 6420.

"(iii) use on a farm for farming purposes (within the meaning of section 6420(c)),

"(iv) use in—

"(I) a shopping center,

"(II) an office building,

"(III) a wholesale or retail establishment,

"(IV) any other facility which is not an integral part of manufacturing, processing, or mining, or

"(V) any facility for the production of electric power having a heat rate of less than 9,500 Btu's per kilowatt hour and which is capable of converting to synthetic fuels (as certified by the Secretary),

"(v) use in the exploration for, or the development, extraction, transmission, or storage of, crude oil, natural gas, or natural gas liquids, and

"(vi) use in Hawaii.

Except as provided in clauses (iv) (V) and (vi) of the preceding sentence, the term 'exempt use' does not include use of a boiler which is public utility property (within the meaning of section 46(f)(51))."

26 USC 46.

(3) DENIAL OF RAPID DEPRECIATION FOR BOILERS FUELED BY OIL OR GAS.—Section 167 (relating to depreciation) is amended by redesignating subsection (p) as subsection (r) and by inserting after subsection (o) the following new subsection:

26 USC 167.

"(p) STRAIGHT LINE METHOD FOR BOILERS FUELED BY OIL OR GAS.—In the case of any boiler which, by reason of section 48(a)(10), is not section 38 property—

26 USC 48.

"(1) subsections (b), (j), and (l) shall not apply, and

"(2) the term 'reasonable allowance' as used in subsection (a) shall mean only an allowance computed under the straight line method using a useful life equal to the class life prescribed by the Secretary under subsection (m) which is applicable to such property (determined without regard to the last sentence of subsection (m)(1))."

26 USC 48 note.

(4) EFFECTIVE DATE.—

(A) IN GENERAL.—The amendments made by this subsection shall apply to property which is placed in service after September 30, 1978.

(B) BINDING CONTRACTS.—The amendments made by this subsection shall not apply to property which is constructed, reconstructed, erected, or acquired pursuant to a contract which, on October 1, 1978, and at all times thereafter, was binding on the taxpayer.

(e) DEPRECIATION ALLOWANCE IN CASE OF RETIREMENT OR REPLACEMENT OF CERTAIN OIL AND GAS BOILERS, ETC.—

(1) IN GENERAL.—Section 167 is amended by inserting after subsection (p) the following new subsection:

26 USC 167.

"(q) RETIREMENT OR REPLACEMENT OF CERTAIN BOILERS, ETC., FUELED BY OIL OR GAS.—

"(1) IN GENERAL.—If—

"(A) a boiler or other combustor was in use on October 1, 1978, and as of such date the principal fuel for such combustor was petroleum or petroleum products (including natural gas), and

"(B) the taxpayer establishes to the satisfaction of the Secretary that such combustor will be retired or replaced on or before the date specified by the taxpayer,

then for the period beginning with the taxable year in which subparagraph (B) is satisfied, the term 'reasonable allowance' as used in subsection (a) includes an allowance under the straight line method using a useful life equal to the period ending with the date established under subparagraph (B).

"(2) INTEREST.—If the retirement or replacement of any combustor does not occur on or before the date referred to in paragraph (1)(B)—

"(A) this subsection shall cease to apply with respect to such combustor as of such date, and

"(B) interest at the rate determined under section 6621 on the amount of the tax benefit arising from the application of this subsection with respect to such combustor shall be due and payable for the period during which such tax benefit was available to the taxpayer and ending on the date referred to in paragraph (1)(B)."

26 USC 6621.

(2) EFFECTIVE DATE.—The amendment made by paragraph (1) shall apply to taxable years ending after the date of the enactment of this Act.

26 USC 167 note.

TITLE IV—MISCELLANEOUS PROVISIONS

SEC. 401. TREATMENT OF INTANGIBLE DRILLING COSTS FOR PURPOSES OF THE MINIMUM TAX.

Subsection (b) of section 308 of the Tax Reduction and Simplification Act of 1977 is amended by striking out ", and before January 1, 1978".

26 USC 57 note.

SEC. 402. OPTION TO DEDUCT INTANGIBLE DRILLING COSTS IN THE CASE OF GEOTHERMAL DEPOSITS.

(a) IN GENERAL.—Subsection (c) of section 263 (relating to intangible drilling and and development costs in the case of oil and gas wells) is amended—

26 USC 263.

(1) by adding at the end thereof the following new sentence: "Such regulations shall also grant the option to deduct as expenses intangible drilling and development costs in the case of wells drilled for any geothermal deposit (as defined in section 613(e)

Post, p. 3203.

(3)) to the same extent and in the same manner as such expenses are deductible in the case of oil and gas wells.", and

(2) by amending the subsection heading to read as follows:

"(c) INTANGIBLE DRILLING AND DEVELOPMENT COSTS IN THE CASE OF OIL AND GAS WELLS AND GEOTHERMAL WELLS.—".

(b) MINIMUM TAX ON INTANGIBLE DRILLING COSTS IN THE CASE OF GEOTHERMAL WELLS.—

26 USC 57.

(1) Paragraph (11) of section 57(a) (relating to intangible drilling costs) is amended by striking out "oil and gas properties" each place it appears (including in the heading of subparagraph (C)) and inserting in lieu thereof "oil, gas, and geothermal properties".

(2) Clause (i) of section 57(a)(11)(B) is amended by striking out "oil and gas wells" and inserting in lieu thereof "oil, gas, and geothermal wells".

(3) Paragraph (11) of section 57(a) is amended by adding at the end thereof the following new subparagraph:

"(D) PARAGRAPH APPLIED SEPARATELY WITH RESPECT TO GEOTHERMAL PROPERTIES AND OIL AND GAS PROPERTIES.—This paragraph shall be applied separately with respect to—

"(i) all oil and gas properties which are not described in clause (ii), and

"(ii) all properties which are geothermal deposits (as defined in section 613(e)(3))."

Post, p. 3203.

(c) GAIN FROM DISPOSITION OF INTERESTS IN GEOTHERMAL WELLS.—

26 USC 1254.

(1) Paragraphs (1) and (2) of section 1254(a) (relating to gain from disposition of interest in oil or gas property) are each amended by striking out "oil or gas property" each place it appears and inserting in lieu thereof "oil, gas, or geothermal property".

(2) Paragraph (3) of section 1254(a) (defining oil or gas property) is amended to read as follows:

"(3) OIL, GAS, OR GEOTHERMAL PROPERTY.—The term 'oil, gas, or geothermal property' means any property (within the meaning of section 614) with respect to which any expenditures described in paragraph (1)(A) are properly chargeable."

26 USC 614.

(3) The section heading of section 1254 is amended by striking out "OIL OR GAS" and inserting in lieu thereof "OIL, GAS, OR GEOTHERMAL".

(4) The table of sections for part IV of subchapter P of chapter 1 is amended by striking out "oil or gas" in the item relating to section 1254 and inserting in lieu thereof "oil, gas, or geothermal".

26 USC 1231.

(5) Subsection (c) of section 751 (relating to unrealized receivables) is amended by striking out "oil and gas property" and inserting in lieu thereof "oil, gas, or geothermal property".

26 USC 751.

(d) APPLICATION OF AT RISK RULES TO GEOTHERMAL DEPOSITS.—

26 USC 465.

(1) Paragraph (1) of section 465(c) (defining activities to which at risk rules apply) is amended by striking out "or" at the end of subparagraph (C), by adding ", or" at the end of subparagraph (D), and by inserting after subparagraph (D) the following new subparagraph:

"(E) exploring for, or exploiting, geothermal deposits (as defined in section 613(e)(3))".

(2) Paragraph (2) of section 465(c) is amended by striking out "or" at the end of subparagraph (C), by adding "or" at the end of subparagraph (D), and by inserting after subparagraph (D) the following new subparagraph:

"(E) geothermal property (as determined under section 614)",. 26 USC 614.

(e) EFFECTIVE DATE.— 26 USC 263 note.

(1) IN GENERAL.—The amendments made by this section shall apply with respect to wells commenced on or after October 1, 1978, in taxable years ending on or after such date.

(2) ELECTION.—The taxpayer may elect to capitalize or deduct any costs to which section 263(c) of the Internal Revenue Code of 1954 applies by reason of the amendments made by this section. Any such election shall be made before the expiration of the time for filing claim for credit or refund of any overpayment of tax imposed by chapter 1 of such Code with respect to the taxpayer's first taxable year to which the amendments made by this section apply and for which he pays or incurs costs to which such section 263(c) applies by reason of the amendments made by this section. Any election under this paragraph may be changed or revoked at any time before the expiration of the time referred to in the preceding sentence, but after the expiration of such time such election may not be changed or revoked. 26 USC 263.

SEC. 403. DEPLETION FOR GEOTHERMAL DEPOSITS AND NATURAL GAS FROM GEOPRESSURED BRINE.

(a) GEOTHERMAL DEPOSITS.—

(1) IN GENERAL.—Section 613 (relating to percentage depletion) is amended by adding at the end thereof the following new subsection: 26 USC 613.

"(e) PERCENTAGE DEPLETION FOR GEOTHERMAL DEPOSITS.—

"(1) IN GENERAL.—In the case of geothermal deposits located in the United States or in a possession of the United States, for purposes of subsection (a)—

"(A) such deposits shall be treated as listed in subsection (b), and

"(B) the applicable percentage (determined under the table contained in paragraph (2)) shall be deemed to be the percentage specified in subsection (b).

"(2) APPLICABLE PERCENTAGE.—For purposes of paragraph (1)—

"In the case of taxable years beginning in calendar year—	The applicable percentage is—
1978, 1979, or 1980	22
1981	20
1982	18
1983	16
1984 and thereafter	15

"(3) GEOTHERMAL DEPOSIT DEFINED.—For purposes of paragraph (1), the term 'geothermal deposit' means a geothermal reservoir consisting of natural heat which is stored in rocks or in an aqueous liquid or vapor (whether or not under pressure). Such a deposit shall in no case be treated as a gas well for purposes of this section or section 613A, and this section shall not apply to a geothermal deposit which is located outside the United States or its possessions." 26 USC 613A.

(2) TECHNICAL AMENDMENTS.—

(A) Paragraph (1) of section 613(c) (defining gross income from the property) is amended by inserting "and other than a geothermal deposit" after "oil or gas well".

26 USC 613A.

(B) Paragraph (1) of section 613A(b) is amended—

(i) by inserting "and" at the end of subparagraph (A),

(ii) by striking out "and" at the end of subparagraph (B), and

(iii) by striking out subparagraph (C).

26 USC 614.

(C) Subsection (b) of section 614 (relating to special rules as to operating mineral interest in oil and gas wells) is amended—

(i) by inserting "OR GEOTHERMAL DEPOSITS" after "GAS WELLS" in the subsection heading, and

(ii) by inserting "or geothermal deposits" after "gas wells" in so much of the text as precedes paragraph (1) thereof.

(D) Subsection (c) of section 614 is amended by striking out "oil and gas wells" each place it appears and inserting in lieu thereof "oil and gas wells and geothermal deposits".

(b) NATURAL GAS FROM GEOPRESSURED BRINE.—

26 USC 613A.

(1) IN GENERAL.—Subsection (b) of section 613A (relating to exemption for certain domestic gas wells) is amended by redesignating paragraph (2) as paragraph (3) and by inserting after paragraph (1) the following new paragraph:

26 USC 611.

26 USC 613.

"(2) NATURAL GAS FROM GEOPRESSURED BRINE.—The allowance for depletion under section 611 shall be computed in accordance with section 613 with respect to any qualified natural gas from geopressured brine, and 10 percent shall be deemed to be specified in subsection (b) of section 613 for purposes of subsection (a) of such section."

Supra.

(2) QUALIFIED NATURAL GAS FROM GEOPRESSURED BRINE.—Paragraph (3) of section 613A(b) (as redesignated by paragraph (1)) is amended by adding at the end thereof the following new subparagraph:

"(C) QUALIFIED NATURAL GAS FROM GEOPRESSURED BRINE.—The term 'qualified natural gas from geopressured brine' means any natural gas—

Post, p. 3397.

"(i) which is determined in accordance with section 503 of the Natural Gas Policy Act of 1978 to be produced from geopressured brine, and

"(ii) which is produced from any well the drilling of which began after September 30, 1978, and before January 1, 1984."

26 USC 613 note.

(c) EFFECTIVE DATE.—The amendments made by this section shall take effect on October 1, 1978, and shall apply to taxable years ending on or after such date.

26 USC 613A note.

(d) COORDINATION WITH OTHER PROVISION.—Any allowance for depletion allowed by reason of the amendments made by subsection (b) shall not be treated as a credit, exemption, deduction, or comparable adjustment applicable to the computation of any Federal tax which is specifically allowable with respect to any high-cost natural gas (or category thereof) for purposes of section 107(d) of the Natural Gas Policy Act of 1978.

Post, p. 3366.

SEC. 404. REREFINED LUBRICATING OIL.

26 USC 4093.

(a) IN GENERAL.—Section 4093 (relating to exemption of sales to producers) is amended to read as follows:

"SEC. 4093. EXEMPTIONS.

"(a) SALES TO MANUFACTURERS OR PRODUCERS FOR RESALE.—Under regulations prescribed by the Secretary, no tax shall be imposed by section 4091 on lubricating oils sold to a manufacturer or producer of lubricating oils for resale by him.

26 USC 4091.

"(b) USE IN PRODUCING REREFINED OIL.—

"(1) SALES TO REREFINERS.—Under regulations prescribed by the Secretary, no tax shall be imposed by section 4091 on lubricating oil sold for use in mixing with used or waste lubricating oil which has been cleaned, renovated, or rerefined. Any person to whom lubricating oil is sold tax-free under this paragraph shall be treated as the producer of such lubricating oil.

"(2) USE IN PRODUCING REREFINED OIL.—Under regulations prescribed by the Secretary, no tax shall be imposed by section 4091 on lubricating oil used in producing rerefined oil to the extent that the amount of such lubricating oil does not exceed 55 percent of such rerefined oil.

"(3) REREFINED OIL DEFINED.—For purposes of this subsection, the term 'rerefined oil' means oil 25 percent or more of which is used or waste lubricating oil which has been cleaned, renovated, or rerefined."

(b) CONFORMING AMENDMENT.—Section 4092(a) is amended by striking out "4093" and inserting in lieu thereof "4093(a)".

26 USC 4092.

(c) CLERICAL AMENDMENT.—The table of sections for subpart B of part III of subchapter A of chapter 32 is amended by striking out the item relating to section 4093 and inserting in lieu thereof the following:

26 USC 4091.

"Sec. 4093. Exemptions."

(d) EFFECTIVE DATE.—The amendments made by this section shall apply to sales on or after the first day of the first calendar month beginning more than 10 days after the date of the enactment of this Act.

26 USC 4093 note.

Approved November 9, 1978.

LEGISLATIVE HISTORY:

HOUSE REPORTS: No. 95-435 (Comm. on Ways and Means) and No. 95-1773 (Comm. of Conference).

SENATE REPORTS: No. 95-529 (Comm. on Finance) and No. 95-1324 (Comm. of Conference).

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WEEKLY COMPILATION OF PRESIDENTIAL DOCUMENTS:

Vol. 14, No. 45: Nov. 9, Presidential statement.

95TH CONGRESS 1st Session } HOUSE OF REPRESENTATIVES { REPT. NO. 95-543 VOLUME I

NATIONAL ENERGY ACT

REPORT

OF THE

AD HOC COMMITTEE ON ENERGY
U.S. HOUSE OF REPRESENTATIVES

TOGETHER WITH SUPPLEMENTAL, MINORITY, AND ADDITIONAL VIEWS

[Including Cost Estimate of the Congressional Budget Office]

ON

H.R. 8444

JULY 27, 1977.—Committed to the Committee of the Whole House on the State of the Union and ordered to be printed

U.S. GOVERNMENT PRINTING OFFICE

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(II)

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95TH CONGRESS } HOUSE OF REPRESENTATIVES { REPT. 95-
1st Session } { 543, VOL. I

(Numerals at top of page indicate official report page numbers)

NATIONAL ENERGY ACT

JULY 27, 1977.—Committed to the Committee of the Whole House on the State of the Union and ordered to be printed

Mr. ASHLEY, from the Ad Hoc Committee on Energy, submitted the following

REPORT

together with

SUPPLEMENTAL, MINORITY, AND ADDITIONAL VIEWS

[Including Cost Estimate of the Congressional Budget Office]

[To accompany H.R. 8444]

The Ad Hoc Committee on Energy, to whom was referred the bill (H.R. 8444) to establish a comprehensive national energy policy, having considered the same, reports favorably thereon with amendments and recommends that the bill as amended do pass.

The amendments are shown in the reported bill, with the matter proposed to be stricken shown in linetype and the matter proposed to be inserted shown in italic type.

(1)

I. INTRODUCTION

The Ad Hoc Committee on Energy is unique in the history of the House of Representatives. Never before has the House seen fit to establish a special committee designed to reconcile the recommendations of the standing committees, and fashion a comprehensive legislative package. It is especially appropriate that the House has undertaken such an experiment with respect to the National Energy Act.

This legislation is essential to our nation's immediate future. Of necessity, it is broad ranging—cutting across jurisdictional lines and involving many controversial issues. The Ad Hoc Committee has provided a forum for review of the standing committees' recommendations with respect to the 113 legislative initiatives proposed by the President. It has provided a forum to ensure that the pieces do fit together into a sensible whole. It has provided a forum to focus consideration on the controversial issues.

In discharging its responsibilities, the Ad Hoc Committee has been sensitive to the constraints and limitations under which it operates. The Ad Hoc Committee is not a permanent committee. It has authority only to recommend committee amendments for consideration on the House floor.

The Ad Hoc Committee has used H.R. 8444 as a vehicle for consideration of the National Energy Act. H.R. 8444 is a clean bill incorporating the standing committees' legislative responses to H.R. 6831, the President's bill. All of the legislative history developed by the standing committees with respect to H.R. 6831 attaches to H.R. 8444.

In the past month, the Ad Hoc Committee has worked long and hard: early in the morning, and into the evening. We hope that our efforts will help avoid the bitterness that so often characterizes the consideration of energy legislation in the House. We hope that our efforts will focus the controversy on germane, major national and regional issues. Most of all, we hope that our efforts will contribute to enactment of a sensible, comprehensive national energy policy.

II. OVERVIEW OF AND NEED FOR AN ENERGY PROGRAM

The fundamental problem for U.S. energy policy is the insecurity of its oil supply. Domestic demand for oil has been growing, while total domestic production, except that from the Outer Continental Shelf and from Alaska, has been declining. The Nation's oil imports have consequently increased to the point where the United States is expected to import between 45 percent and 50 percent of its oil supplies in 1977, up from 23 percent in 1970 when domestic oil production peaked.

Demand for Petroleum and Oil Imports

Table 1 shows the U.S. supply and demand for petroleum, along with the level of imports, between 1955 and 1976. Since 1955, demand has approximately doubled—from 8.5 million barrels per day to 17.4 million barrels per day. U.S. production of crude oil and natural gas liquids did rise between 1955 and 1970, but at a slower rate than demand; therefore, there was a gradual rise in imports. After 1965, we were no longer self-sufficient in oil as U.S. oil imports began to exceed spare capacity within the United States. Since the 1970 peak in U.S. oil production, imports have grown at an especially rapid rate. In 1976 imports were 7.3 million barrels per day, or 42 percent of U.S. oil demand. Thus, except when energy consumption was sharply reduced by the severe recession, there has been a steady growth in oil demand. Moreover, domestic onshore production in the lower 48 States has continued to decline.

The United States cannot continue to consume energy as if it had plenty of spare capacity of oil production and could expect further growth in domestic oil supplies. Since the best that can be reasonably expected is a slowdown in the rate of decline in U.S. oil production, we have to adapt ourselves to the reality that oil consumption cannot be permitted to continue to grow rapidly. Even the production from the large Alaskan oil fields will only serve to raise U.S. production back to the 1970 level.

Our reliance on imported oil is expected to increase dramatically if present practices and policies are continued. The Federal Energy Administration predicts that, under current policy, oil demand will rise from 17.4 million barrels per day (mmbd) in 1976 to 21.1 mmbd in 1980, 22.8 mmbd in 1985 and 24.9 mmbd in 1990. These levels of demand will imply imports of 10.2 mmbd in 1980 (48 percent of consumption), 11.5 mmbd in 1985 (50 percent of consumption), and 14.5 mmbd in 1990 (58 percent of consumption). These alarming FEA estimates are consistent with most private forecasts.

Such an increase in our reliance on oil imports would greatly constrain our foreign policy and could do considerable damage to our economy.

Table 1.—U.S. oil demand, supply and imports, 1955–76

[In millions of barrels per day]

Year	U.S. demand for petroleum	U.S. production of crude oil	U.S. production of natural gas liquids	U.S. spare capacity for crude oil	U.S. oil imports
1955	8.49	6.81	.77	1.78	1.25
1956	8.82	7.15	.80	2.08	1.44
1957	8.86	7.17	.81	2.78	1.57
1958	9.15	6.71	.81	2.60	1.70
1959	9.49	7.05	.88	2.67	1.78
1960	9.81	7.04	.93	2.71	1.82
1961	9.99	7.18	.99	2.75	1.92
1962	10.41	7.33	1.02	2.63	2.08
1963	10.75	7.54	1.10	2.67	2.12
1964	11.03	7.61	1.16	2.73	2.26
1965	11.52	7.80	1.21	2.45	2.47
1966	12.10	8.30	1.28	2.24	2.57
1967	12.57	8.81	1.41	2.12	2.54
1968	13.40	9.10	1.50	1.90	2.84
1969	14.15	9.24	1.59	1.38	3.17
1970	14.71	9.64	1.66	1.33	3.42
1971	15.23	9.46	1.69	.69	3.93
1972	16.37	9.44	1.74	.20	4.74
1973	17.30	9.21	1.74	----	6.26
1974	16.65	8.77	1.69	----	6.11
1975	16.32	8.38	1.63	----	6.06
1976	17.44	8.12	1.69	----	7.29

Source: Independent Petroleum Association of America (1955–71) and *Monthly Energy Review* (1972–76).

Future World Oil Markets

Further, there is widespread agreement that a continuation of present world oil consumption trends, even with significantly higher world oil prices, will lead to a very tight world oil market in the mid-1980's. At that point, the world's oil supply will be straining to meet world demand with very serious implications for both international security and the world economy. Sudden disruptive price increases, accompanied by arbitrary curtailments of supply, will generate shocks to the national security and economic stability of each oil importing country. This is a development that each country should strive to avoid.

The choice for the United States is evident: We must begin now, while there still is time to make adjustments, to change the way Americans use energy and avoid the disruption that could be suddenly thrust upon us from external sources. Such disruptions occurred in 1973, when the Arab oil embargo was accompanied by the quadrupling of OPEC (Organization of Petroleum Exporting Countries) oil prices over a short period of three months.

This shock was transmitted through the prices of oil and its products, many of which appear in other sectors of the economy as feed-

stocks and raw materials. Manufacturers throughout the industrial world participated in an inflationary process of bidding for inventories of these materials. Foreign exchange rates of all countries also underwent dramatic change in the process. These events, combined with a coincidence of timing with other unfortunate economic events, e.g., severe shortfalls in food production in several regions of the world, helped to precipitate the most serious worldwide economic recession since the 1930's. That recession was so severe that industrial countries only recently have begun to approach previous economic output levels. Nevertheless, the inflation still persists throughout the world.

In addition, natural gas supplies and demand are seriously out of balance. Demand has continued to grow, while production peaked in 1973 and reserve additions since 1970 have been insufficient to make up for yearly production decline from these reserves. Natural gas has been underpriced, leading to excess demand for all uses, but especially for industrial and utility boiler uses. In these cases, the use of alternative fuels often is feasible. Because of this, last winter's widespread industrial curtailments of natural gas, despite more than 5 years of warnings over impending natural gas shortages, made industries seriously contemplate using other fuels. Unfortunately, the marginal cost of additional oil and gas consumption to the American economy is the cost of the additional oil which must be imported. Only when oil and gas resources are priced to reflect that reality to industrial consumers who most easily can conserve and convert coal will it become economically attractive to increase the use of these alternative fuels.

The Need for Transition

The United States faces the problem of making the transition from an era of cheap abundant energy to relative scarcity of expensive energy supplies. Further, because of the long lead times involved, the transition must be started now, so as to avoid serious future shocks to the Nation and to its economy from energy shortages. The benefits of having a more secure energy supply for the long term should more than justify the short term costs of a transitional program.

Further energy conservation and vigorous economic growth are not incompatible goals. Table 2 compares U.S. energy consumption in 1974 with that of other industrial countries. (The measure of energy in table 2 is coal-equivalents; that is, other sources of energy are converted to the amount of coal that would produce the same amount of energy.) The United States consumes at least twice as much energy per capita as any other country listed in the table. Although Sweden and Switzerland each have a higher gross national product per capita than the United States, U.S. energy consumption per capita is 1.97 times that of Sweden and 3.18 times that of Switzerland. Germany has a per capita GNP approximately equal to that of the United States, but it uses only half as much energy per capita.

Half of the difference in consumption levels can be attributed to the transportation sector, about evenly divided between the higher efficiency of the European automobile fleets and the generally more expensive use—partly because of greater distances—of automobiles and trucks in the United States. About a quarter of the difference in overall energy consumption is related to differences in the energy consumption in residences, even after making adjustment for differences in

climate. Residences in Sweden, Germany, and Switzerland tend to be built with better insulation. In the United States, there is a far greater proportion of single family residences; the rooms are larger; there are more rooms in a residence; the average room temperature is higher; and the whole house is heated. Air conditioning is not used extensively in Europe. European industry is also more energy-efficient than American industry.

Those statistics show that it is possible to maintain a high standard of living, such as exists in such countries as France, Germany, Sweden, and Switzerland, while consuming considerably less energy per capita than does the United States. They indicate that the energy goals embodied in this bill can be achieved over time—if tax and other national policies are adjusted to give our people the appropriate incentives to conserve energy.

Table 2.—Energy consumption per capita in various countries, 1974

Country	Consumption of energy—coal equivalent [1]	Consumption of energy per capita [2]
United States	2,433.5	11,485
Germany	353.0	5,689
United Kingdom	306.5	5,464
France	227.6	4,330
Italy	178.6	3,227
Japan	421.0	3,839
Sweden	47.4	5,804
Switzerland	23.3	3,608
World total	7,953.0	2,100

[1] Million metric tons.
[2] Kilograms of coal—equivalent.

Source: *Statistical Abstract of the United States* 1976.

The National Energy Act as a Set of Strategies

The National Energy Act represents an effort to adopt a comprehensive set of policies which will allow the U.S. economy the time to make an orderly transition to an era of expensive energy resources, in particular oil and gas resources, from a past characterized by very inexpensive energy resources. And because energy use is so capital intensive, a full transition will take a long time. However, the incentives and penalties must be put in place now, with appropriate phase-ins, to ensure the timely and steady transition away from oil and gas resources, and toward the greater use of coal, uranium, renewable, and other energy resources.

One of the more important themes of the National Energy Act is to foster greater conservation in the use of energy resources. The Nation must substantially improve the efficiency with which it consumes its limited supplies of energy. Energy conservation can help stem the future rate of increase in energy demand. Second, because coal is the single most abundant domestic fossil fuel resource, it can replace

much of the future demand for oil and gas. We must find economically and environmentally desirable ways in which to use our abundant coal supplies.

Despite vigorous energy conservation and coal conversion programs, our Nation will continue to consume substantial amounts of oil and natural gas. The Nation must, therefore, encourage increased exploration and development of our remaining oil and natural gas resources. However, because consumption of these fuels is central to the health of the Nation's economy, allowing price increases which do not produce additional supplies would not be sound policy. Such price increases would be inflationary, while simultaneously imposing recessionary pressures by reducing the level of consumer dollars available to purchase goods and services, other than for essential energy supplies. Oil taxing and natural gas pricing policy must encourage development of new resources while limiting price increases on previously developed resources in order to insulate the economy from the shock which substantial price increases for such resources would otherwise produce.

The legislative program recommended by this committee seeks to implement such an energy policy.

The National Energy Act thus has three principal themes: energy conservation, conversion to coal, and incentives to production. The act also establishes six goals to be achieved by 1985:

1. To reduce the average growth rate of energy consumption to 2 percent per annum.
2. To reduce the oil imports level to less than 6 million barrels a day.
3. To achieve a 10 percent reduction in gasoline consumption from the 1977 level.
4. To retrofit for energy conservation purposes 90 percent of the residential and commercial buildings in the United States.
5. To increase coal production by at least 400 million tons annually over 1976 levels.
6. To use solar energy in more than 2½ million homes.

The National Energy Act contains a set of strategies designed to help meet these goals. The goals are ambitious and they may not be achievable. However, what is important is that the Nation begin the process now, and that we periodically reexamine our progress toward achieving these goals, to see whether stronger action is necessary or desirable. The strategies contained in the National Energy Act can be listed under seven broad categories:

1. *Residential and Commercial Conservation* (including Federal buildings).—The bill provides for energy conservation programs for existing residential buildings including a tax credit program, and loan and grant programs for low income families and a retrofit program for public housing units; for energy conservation grants for schools and hospitals, and for technical assistance for local municipal buildings; for conservation and solar demonstration programs in Federal buildings; and for tax credits for business energy conservation.

2. *Transportation*.—The bill provides for gasoline conservation through extension of the present 4 cents a gallon excise taxes through 1985, an additional 4 cents a gallon tax on gasoline and other motor fuels for highway and general aviation use, creation of a trust fund to help States finance highway maintenance, and Federal outlays for

mass transit, the strategic petroleum reserve, energy technology research and development, and carpooling and vanpooling.

3. *Crude Oil Equalization Tax and Rebate.*—The bill provides that domestic prices for crude oil and its products will equal the world price for oil after a 3 year phasein. Safeguards are built in to protect the U.S. economy from the adverse effects of a too rapid rate of increase in world crude oil prices. Tax refunds will be given for use of heating oil in residences, schools, universities, hospitals and churches. Taxpayers and adult nontaxpayers will receive rebates of the tax.

4. *Natural Gas Pricing.*—The natural gas pricing policy adopted by the Committee establishes a single, uniform price policy for natural gas produced in the United States. This policy recognizes the impracticability of deregulating natural gas prices as long as a substantial supply/demand imbalance exists. With respect to supplies of new natural gas, an incentive price is provided which is related to delivered domestic crude oil prices. This price begins at a level of $1.75 per million Btu's (Mcf) and climbs upward rapidly as crude oil costs increase at approximately 10 percent per year.

A flexible special pricing authority is granted to the Federal Power Commission under which it may approve higher prices where needed. This provision assures that maximum price incentives are focused on those areas where the greatest potential exists that the incentives will be effective and encourage production of hard to produce natural gas.

The regulatory burdens imposed upon producers by the Natural Gas Act are avoided under the Committee's program. Sales of natural gas subject to the provisions of this legislation, with the singular exception of interstate sales of old natural gas under existing contracts, are "deregulated" from the provisions of the Natural Gas Act. The Federal Power Commission is granted substitute regulatory powers, with respect to such deregulated sales, the scope of which is more limited than the regulatory powers of the Commission under the Natural Gas Act.

5. *Business Use Tax. Credits and Additional Investment Tax Credit.*—The bill provides for a use tax on business consumption of oil or natural gas that will be imposed in three levels: (1) where conservation in fuel consumption is feasible; (2) where conversion to alternate fuels is feasible; and (3) electric utilities and industrial cogenerators (this tax beginning in 1983). The tax may be offset by investment in qualified alternative energy property. An additional 10 percent investment tax credit is made available for investment in equipment for conversion to fuel other than oil and natural gas and for a broad range of energy conservation equipment.

6. *Public Utility Regulatory Policies.*—The bill provides for a method to move the Nation's electric utilities toward pricing policies which price electricity at the true cost of providing service to each class of electric consumers, so as to encourage conservation in the production and use of electricity. It also provides for stronger coordination of bulk power supply facilities.

7. *Miscellaneous Provisions.*—The bill provides for tax incentives for geothermal and oil and gas drilling ventures. It also provides for mandatory efficiency standards for various appliances.

In the next section, a summary of these provisions is presented according to titles (and parts) of the bill.

The following sections of the report have been omitted:
III—Summary of the Bill
A. Findings, Goals, Etc. (page 11)
B. Title I—Pricing, Regulatory, and Other Nontax Provisions (pages 11-24)

C. Title II—Tax Provsions

Part I—Residential Energy Credit

Residential insulation and energy conservation credit

The bill provides a credit of 20 percent on the first $2,000 of cumulative expenditures on home insulation and other energy conserving components, for a maximum credit of $400. The credit would be available for installations made from April 20, 1977, through December 31, 1984. (The Ways and Means Committee bill would terminate the credit on December 31, 1982.)

Insulation means materials that will reduce the heat loss or heat gain of a residence. Attic, floor and wall insulation made of fiberglass, rock wool, cellulose or styrofoam are examples of insulating materials. Energy conserving components include a replacement burner for a furnace that provides increased combustion efficiency, devices to modify flue openings, automatic ignition systems that replace a gas pilot light, exterior storm or thermal doors or windows, a clock thermostat and exterior caulking or weatherstripping.

The expenditures must be made for a principal residence that was in existence on April 20, 1977. Vacation homes and other residences do not qualify for the credit. If a taxpayer moves to another principal residence after taking the credit on a previous principal residence, qualifying expenditures on the other residence would be eligible for the $400 credit.

Owners and renters will be eligible for the credit. Cooperative and condominium housing owners are each eligible for the $400 credit on their proportionate shares of the common qualifying expenditures. The credit is allocated among joint occupants of a principal residence.

Residential solar and wind energy equipment credit

A credit up to $2,150 would be available on the first $10,000 of expenditures on solar and wind energy equipment. The credit is 30 percent of the first $1,500 spent and 20 percent of the next $8,500 spent for installations of this equipment from April 20, 1977, through December 31, 1984. (The Ways and Means Committee bill would terminate the credit on December 31, 1982.)

Eligible equipment covers equipment that uses solar energy to heat or cool, or to provide hot water for a principal residence, and equipment that uses wind to generate electricity and other forms of energy. Solar and wind energy equipment only need to be installed in connection with a residence rather than in or on it, but they do not include backup systems of conventional heating or cooling equipment.

For solar and wind energy equipment, the principal residence may be either an existing or newly constructed residence. Owners and renters are eligible for the credit. Members of cooperative and con-

dominium associations are each eligible for the $2,150 credit for their proportionate shares of the common qualifying expenditures. The credit is allocated among joint occupants of a principal residence.

Part II—Transportation Tax Provisions

Subpart A—Gas guzzler tax

Imposition of the tax

A gas guzzler tax would be imposed on each sale or initial lease by the manufacturer of an automobile that falls below efficiency standards established for each model year. The efficiency standards increase for each model year 1979 through 1985. The standards start from 3 to 5.5 miles per gallon below the fleetwide average standards imposed under the Energy Policy and Conservation Act (EPCA). The tax applies to automobiles weighing no more than 6,000 pounds; it does not apply to trucks with a cargo capacity of at least 1,000 pounds.

A separate tax table applies to each model year 1979 through 1985; the table for 1985 applies to later model years as well. The lowest tax increases from $339 for an automobile with an efficiency rating of 15 miles per gallon in 1979 to $397 for an automobile with an efficiency rating of 23.5 miles per gallon in 1985 and later years. The highest tax for each model year applies to vehicles with efficiency ratings at or below 12.5 or 13 miles per gallon and increases from $553 in 1979 to $3,856 in 1985 and later model years.

The tax will also apply to new and used imported cars, according to their model years, and the tax is to be imposed on the importer.

The basis of the automobile is to be reduced by the amount of the gas guzzler tax. In other words, the amount of this tax is not to be taken into account in computing depreciation, the investment tax credit or gain or loss on resale.

Trust fund

The bill establishes a Public Debt Retirement Trust Fund into which the proceeds of the gas guzzler tax will be deposited. The proceeds are to be used to retire obligations of the United States that are included in the public debt.

Subpart B—Motor fuels

Repeal of personal deduction for State gasoline taxes

The bill repeals the personal deduction for State and local government taxes imposed on gasoline, diesel fuel and other motor fuels, used for nonbusiness purposes, effective for purchases after December 31, 1977.

Extension of excise tax on gasoline and other motor fuels

The current Federal excise taxes of 4 cents a gallon on gasoline and other motor fuels will be continued at that rate through September 30, 1985. These taxes are currently scheduled to be reduced to one and one-half cents a gallon after September 30, 1979. No action is taken at this time on the Highway Trust Fund, which will continue to receive these funds under present law through September 30, 1979.

Repeal of refund of motorboat fuel tax

The 2-cents-a-gallon reduction (through refund, credit or exemption) of the excise taxes on gasoline and special motor fuels used in a motorboat is repealed. The increased taxes on motorboat fuel will go into the Land and Water Conservation Fund as user taxes on motorboat operators (as do the present 2-cents-a-gallon taxes).

Subpart C—Provision related to buses

Repeal of excise taxes on buses and bus parts

The 10-percent excise tax on buses and the 8-percent excise tax on bus parts and accessories will be repealed. Parts and accessories that may be interchangeable between trucks and buses will be taxed on sale unless the purchaser provides the manufacturer with an exemption certificate which indicates that the part or accessory is purchased for use on a bus. If tax-paid parts are acquired from a dealer and are used on a bus, a credit or refund will be available.

Removal of excise taxes on items used with certain buses

The bill removes the excise taxes on tires, inner tubes, tread rubber, and lubricating oil sold for use on or in connection with privately owned intercity, local, and school buses.

It also provides a credit or refund for the taxes imposed on gasoline and other motor fuels to the extent the fuels are used in qualified operations of privately owned intercity, local, and school buses.

Subpart D—Credit for electric motor vehicles

New electric cars purchased for personal use on or after April 20, 1977, and before January 1, 1983, will be eligible for a tax credit equal to the first $300 of the purchase price. A qualified electric motor vehicle is a 4-wheeled vehicle manufactured for use on public roads that is powered by an electric motor which receives electric current from rechargeable storage batteries or other portable sources.

Ad Hoc Committee Amendments—Tax on Gasoline and Other Motor Fuels

Increased gasoline and motor fuel taxes; Energy conservation and conversion trust fund

The Ways and Means Committee bill did not impose new taxes on gasoline or other motor fuels and did not provide a trust fund to be used for energy conversion and conservation or for payments to the States to reimburse them for anticipated loss of revenues from motor fuels taxes.

The Ad Hoc Committee amendment would impose a fuel conservation tax on gasoline, diesel fuel, and special motor fuels in addition to the present 4-cents-a-gallon tax. This tax would be imposed at a rate of 2-cents-a-gallon in 1978, and would be increased to 4-cents-a-gallon in 1979 and for subsequent years.[1]

The Ad Hoc Committee amendment would also establish an Energy Conservation and Conversion Trust Fund in which the net revenues

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[1] Under this amendment, these taxes would not apply to fuel used in general aviation (but would apply under a separate committee amendment).

from the fuel conservation taxes are to be deposited. In general, this trust fund is to be divided into three accounts. One-eighth (12.5 percent) of the funds deposited into the trust fund is to be transferred to a "States Account." The amounts in this account are to be allocated among the States based on fuel consumption within the States. The States are required to use these payments in transportation programs, including the maintenance and rebuilding of highways. One-half (50 percent) of the amounts deposited into the trust fund is to be transferred to the "Energy Program Account," which is to be used for energy programs generally, such as, the maintenance of the Strategic Petroleum Reserve and for research and development of new energy technology. Three-eighths (37.5 percent) of the amount deposited into the trust fund is to be transferred to a "Mass Transportation Account." The Mass Transportation Account is to be used for mass transportation by bus, rail, and so forth; for exclusive or preferential lanes for buses, vans and cars; and for car and van pooling. The amounts in each of the accounts are to be expended only as appropriated by the committees of Congress having jurisdiction over the matters involved.

Increase in tax on fuels used in noncommercial aviation

The Ways and Means Committee bill did not increase the taxes on fuels used in general (noncommercial) aviation (presently, a tax of 7 cents a gallon). However, the Ad Hoc Committee amendment would impose additional taxes on general aviation fuel (including gasoline). These taxes would be imposed at the rate of 2 cents a gallon in 1978 and 4 cents a gallon in 1979 and later years. The revenues from these taxes would be deposited in the Energy Conservation and Conversion Trust Fund.

Part III—Crude Oil Equalization Taxes

Subpart A—Imposition of taxes

Crude oil equalization tax

Under the bill, an excise tax is imposed on the first purchase (generally by the refiner) of price controlled, domestically produced crude oil. The tax increases the cost of all crude oil to the world price by 1980. The termination date of the tax is September 30, 1981.

The tax is imposed in three stages. In 1978, a tax of $3.50 per barrel is imposed on lower tier oil (old oil under current regulations). In 1979, the tax on lower tier oil will be raised so that the national average refiner acquisition cost will be identical for lower tier and upper tier oil. In 1980, and for the duration of the tax, the tax will equal the difference between the wellhead prices of uncontrolled and controlled crude oil of the same classification. As a result, the cost of controlled oil plus the tax will be raised to the world price of oil in 1980. If the price control regulations are modified to provide new tiers of price-controlled oil, the tax will automatically adjust so that the rate equals the difference between the controlled price in the new tier and the price of uncontrolled oil of the same classification.

The Ways and Means Committee bill provided a special tax rate for new new oil which may not exceed the difference between the uncontrolled price and highest controlled price for crude oil of the same

classification. The Ways and Means Committee bill also provided a special definition of "new new oil" for purposes of the tax, but an ad hoc committee amendment deleted this definition.[2] As a result, new new oil will be treated in the same manner for both pricing and tax purposes.

There are exemptions from the tax for oil used to extract oil and natural gas and for oil used to produce natural gas liquids.

Natural gas liquids equalization tax

The tax is imposed on sales to end users of natural gas liquids, and it is based upon the difference (the price gap) between the controlled price of the liquid and the wholesale price for No. 2 distillate in the region, adjusted for differences in Btu content. The tax will be equal to one-third of the price gap in 1978, two-thirds of the gap in 1979, and equal to the entire gap in 1980 and later years.

There are exemptions from the tax for natural gas liquids used in residences, on farms and in churches, schools and hospitals.

Presidential authority to suspend the tax

The President is granted authority to suspend any or all of any increase in the equalization tax, if he determines that there has been a significant increase in the world price of oil that will result in a higher equalization tax and will have a substantial adverse economic effect. A suspension plan would have to be submitted to Congress and would be subject to a veto by either House within 15 days of submission.

Subpart B—Return of crude oil equalization taxes

Taxpayer credits.—The net receipts from the equalization taxes will be apportioned equally and returned to each taxpayer in 1978 through a new tax credit. Single taxpayers and married persons filing separately will receive a single payment, and married persons filing joint returns and heads of households (single persons with dependents) will receive a double payment.

The bill instructs the Secretary of the Treasury how to estimate the amount of these tax credits.

The credit will be limited to a taxpayer's tax liability, except for recipients of the earned income credit. The estimated amounts of these payments will be reflected in the withholding tax schedules for 1978.

Special payments.—Special payments will be made in 1979 to adults who are recipients of monthly benefits under social security, railroad retirement or supplemental security income. These payments will be made in the fall of 1979 and will equal the credits rebated to individual taxpayers. Special payments will be reduced by any tax credit received, in order to avoid double payments.

Special payments also will be made to adults who receive aid to families with dependent children. Other adults who do not receive a tax credit or special payment under one of the programs referred to above may file an appropriate form with the Secretary of the Treasury in order to receive a payment.

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[2] New new oil is defined in the Ways and Means Committee bill as crude oil produced from a property that did not have any commercial production at any time during the 90-day period ending on April 20, 1977.

The bill also authorizes payments to the governments of Puerto Rico and the possessions, if they submit acceptable plans to the Secretary of the Treasury for distribution of amounts similar to the tax credits and special payments.

Heating oil refund

An exception is provided from the crude oil equalization tax for heating oil used in residences, churches, schools, universities and hospitals. Distributors of heating oil will receive a refund of the equalization tax for each gallon sold to one of these users, so long as the refund is passed through completely to the customers in lower prices.

Part IV—Excise Tax on Business Use of Oil and Gas

Imposition of tax

A tax would be imposed on the use of oil or natural gas as fuel in a trade or business. Three levels of tax would be imposed: Tier 1, which would apply to an industrial use where *conservation* in fuel consumption is feasible; Tier 2, which would apply to uses of oil or natural gas in which *conversion* to another fuel is feasible; and Tier 3, which would apply to electric utilities and industrial producers of electricity using boilers with a total rating of at least 100 megawatts per plant and, under the Ad Hoc Committee amendment, to industrial cogenerators as well.

The bill only imposes the tax on the larger industrial and utility users of oil and gas. An exemption is provided which limits the tax only to firms using more than the Btu equivalent of 50,000 barrels of oil per year or the equivalent amount of gas (i.e., 300 billion Btu). In cases of a regional competitive disadvantage, the Secretary of the Treasury may provide aditional exempt amounts for individual plants, and he is required to publish the names of taxpayers and plants which receive additions to their exempt amounts.

Determination of tax amount

The tax on Tier 3 uses and on use of oil in Tiers 1 or 2 would be determined according to the following schedules:

	Tax on oil (per barrel)			Tax on natural gas (per million Btu)
Year of use	Conservation tier (Tier 1)	Conversion tier (Tier 2)	Electric utilities (Tier 3)	Electric utilities (Tier 3)
1979	$0.30	$0.30	None	None
1980	.60	.60	None	None
1981	1.00	1.00	None	None
1982	1.00	1.45	None	None
1983	1.00	2.00	$1.50	$0.55
1984	1.00	2.50	1.50	.65
1985 and thereafter	1.00	3.00	1.50	.75

The bill provides a variable tax on the industrial use of natural gas in Tier 1 and Tier 2 categories. The tax would be determined by subtracting the user acquisition price (per million Btu of gas) and a cost differential from the target price (per million Btu of gas) for the region in which the gas is used. The cost differential will change each year—declining annually from $1.35 in 1979 to $.30 in 1985 and later years for Tier 1 use, and from $1.05 in 1979 to zero for Tier 2 use in 1985 and later years. The natural gas target price is determined by the average regional price of all No. 2 grade distillate oil sold during the preceding calendar year in the region, adjusted for differences in energy (Btu) content between such oil and natural gas. In cases where natural gas is purchased under an interruptible contract, the users tax would be subject to a 10 percent reduction.

Beginning in 1981, the tax rates would be adjusted annually for inflation that occurs after 1979. The implicit price deflator for the gross national product is to be used as the index of inflation. The index for the calendar year preceding the current calendar year would be used in order to inform the taxpayer as early as possible in the current year what the tax rate would be.

The tax on the use of natural gas in Tier 3 would be limited so that it could not exceed the amount necessary to make the firm's cost of gas (including the tax) equal to the cost of the residual oil (including the tax) in the region where the gas is used.

Suspension of tax

The President could suspend the tax for a period up to 1 year, if he believes it would have an adverse economic effect. A suspension plan would have to be submitted to Congress and would be subject to a veto by either House within 15 days of its submission.

Exemptions from tax

(1) Industrial process use would be exempt from the tax when the use of fuels other than oil or natural gas would materially and adversely affect the manufacturing process or the quality of the manufactured goods, or when the use of such alternate fuels would not be economically and environmentally feasible.

(2) An exemption from the tax would be provided to nonindustrial uses of oil and natural gas in residential facilities, in transportation (including pipelines), on a farm for farming purposes, in nonmanufacturing commercial buildings, and in the exploration, development and production of crude oil and natural gas.

(3) Oil and natural gas would be exempt from taxation if used in a facility that was in existence or under construction on April 20, 1977, and which is precluded from using coal by State air pollution regulations in effect on that date or by Federal air pollution regulations. State regulations in effect after that date would also be grounds for exemption if such regulations were necessary to meet a requirement of Federal law. A regulation of a local agency having jurisdiction over a facility under an approved State Implementation Plan also would be the basis for an exemption.

The Ways and Means Committee bill provided that an industrial use would be granted an exemption from the tax for the duration of an exception provided under specified provisions of title I of the Na-

tional Energy Act, but the Ad Hoc Committee amendment deleted this provision.

Reclassification of uses

The Secretary of the Treasury is to establish a procedure for reclassifying uses to a category which is taxed at a lower rate or which is exempt from tax. Reclassification would depend on the extent to which reduction in oil and natural gas use could be achieved as a result of the tax. The ad hoc committee wishes to clarify this provision in the Ways and Means Committee bill providing for a reclassification procedure in cases where there is an economic hardship and no significant potential for the conversion from or conservation of oil or natural gas. It is the intention of the Ad Hoc Committee that the Secretary of the Treasury shall prescribe by regulations a procedure under which he will classify the use of oil or natural gas by a regulated public utility (the principal activity of which is the production of electricity for sale) to the exempt use category if the Secretary determines that the imposition of the tax would have the net effect of increasing consumer rates without facilitating conversion from the use of oil or natural gas as a fuel and would impair the utility's ability to accomplish such conversion.

Part V—Credit Against Tax on Business Use of Oil and Gas

A taxpayer may elect a credit against the use tax of $1 for each dollar of qualified investment, up to 100 percent of the taxpayer's oil and natural gas use taxes. If the amount of investment exceeds the amount of use taxes for the year, a carryforward of this investment is permitted against use taxes in future years. Any use tax liability for 1979 and 1980 may be carried forward to 1980 and 1981.

Utilities would be allowed to carry forward qualifying investment expenditures to offset use tax liabilities incurred beginning in 1983. Utilities would be allowed a credit only to the extent that old oil and gas boilers are replaced or phased down for peakload or standby use (1,500 hours or less per calendar year). Under an Ad Hoc Committee amendment, the extent to which the tax credit would be passed through to consumers in the form of lower rates is left to the discretion of State regulatory agencies.

If a phased-down old boiler is used between 1,500 and 2,000 hours in a calendar year, a penalty equal to the use tax would be imposed. Taxes paid in such cases would not be available for offset by qualified investment expenditures. If old boilers are used more than 2,000 hours in a calendar year, there would be a recapture of credits against tax.

The credit would not be available after 1990, except for qualified property on which construction had begun before 1991.

Qualified energy investment costs which could be allowed as a credit against the use tax includes the cost of alternative energy property placed in service during the year or, if the taxpayer elects, the progress expenditures made for that property during the year. It does not include a building or its structural components and does not include property to be used in the business of leasing. It includes costs of the following:

(1) a boiler whose primary fuel is an alternate substance;

(2) a burner and equipment necessary to supply fuel to a combustor other than a boiler for which the primary fuel is an alternate substance;

(3) equipment used in the production of energy by nuclear, hydroelectric, or geothermal power other than the fuel, steam, turbines or equipment beyond the turbine stage;

(4) equipment for converting an alternate substance into synthetic gas;

(5) pollution control equipment required to be installed in equipment described above (other than equipment required to be installed on a facility using coal as of April 20, 1977);

(6) equipment used for unloading, transferring, storing, reclaiming from storage and preparation of an alternate substance for use in the equipment described above or in a facility which uses coal as a feedstock for products other than coke; and

(7) the costs for plans and designs for equipment described above.

An alternate substance would be a fuel that is not oil, natural gas or their products.

The taxpayer could receive the regular investment tax credit on his qualified energy investment expenditures only to the extent that a credit against the use tax was not claimed for the same investment outlay.

Part VI—Changes in Business Investment Credit to Encourage Conservation of, or Conversion From, Oil and Gas or to New Energy Technology

Business energy credit

A 10-percent business energy tax credit is allowed in addition to the investment credit provided under present law for investments by business in qualified energy property intended to reduce the amounts of oil, natural gas or other energy consumed in heating or cooling a building or used in an industrial process.

The credit would be available for investments in qualifying property made after April 19, 1977, and before January 1, 1983. If credits are generated by investments in alternative energy property, they may be applied against 100 percent of the taxpayer's income tax liability, rather than the 50-percent limitation that is now generally available for the regular investment tax credit.

The business energy tax credit would be available for alternative energy property as an option to the use tax credit for taxpayers who would be liable for the oil and natural gas use taxes. The taxpayer could elect either the dollar-for-dollar credit against the use taxes or the business energy credit for investments in alternative energy property. A taxpayer who elected the credit against the use tax would receive the regular investment credit only on the amount of the investment that was not credited against the use tax.

Qualifying property.—For the business energy tax credit, qualifying property includes alternative energy property which is described above. Other types of property which would receive the 10-percent additional energy investment credit are:

(1) installation or expansion of cogeneration property which generates electricity and also creates steam or another form of usable heat;

(2) advanced technology property which would use solar, geothermal, or wind energy to provide heat, cooling or electricity;

(3) specified items of equipment (such as recuperators, heat wheels, and energy control systems) which would recover waste heat and gases or otherwise reduce energy consumption, and also equipment to modify existing facilities to allow the use of oil or natural gas and at least 25 percent of some other substance in a combustor or to produce an industrial feedstock; and

(4) equipment used exclusively to recycle solid waste and to sort and prepare solid wastes for recycling.

In order to qualify, property or equipment in these categories (except alternative energy property and recycling equipment) must be new property which would be used in connection with a building or facility in existence or substantially completed by April 20, 1977. Where the property would be added to an industrial process, this process must have been carried on as of April 20, 1977.

Business insulation

For purposes of the regular investment credit, insulation installed in connection with an existing building or industrial facility would be qualifying property through 1982. Insulation includes storm doors and windows, thermal glass and double glazing.

Denial of regular investment tax credit and accelerated depreciation

The regular investment credit would be denied for portable air conditioners and space heaters.

The regular investment credit also would be denied for new oil and gas boilers. In addition, straight-time depreciation would be required for these boilers, and the 20-percent variance from the guideline lives for depreciable property under ADR would not be available for these boilers. These limitations, however, would not apply where the use of coal as an alternative fuel is precluded by Federal or State regulations or where the use of oil or natural gas qualifies as an exempt process use.

These rules would be prospective, with exemptions only for binding contracts in existence on April 20, 1977.

Depreciation adjustment for planned retirement of boilers

If a taxpayer certifies that he plans to replace or retire a boiler or other combustor which uses oil or natural gas as a fuel before a specified date, the undepreciated value of the equipment would be deductible using the straight line method and a useful life equal to the period from certification to the specified date for retirement. Interest would be charged on the tax benefit that would accrue as a result of this provision, if the retirement takes place later than the specified date.

Part VII—Miscellaneous Provisions

Tax treatment of geothermal expenses

A current deduction would be allowed for intangible drilling costs related to the exploration and development of geothermal resources.

To the extent that these intangible drilling costs exceed the taxpayer's income from the production of geothermal resources, these costs would be subject to the minimum tax on preference items.

In addition, the bill provides percentage depletion at a 10-percent rate for all geothermal resources, subject to the limitation that the total amount of depletion allowed with respect to any property is not to exceed the taxpayer's adjusted cost basis in that property.

Minimum tax on intangible drilling costs for oil and gas wells

The bill extends beyond 1977 the provision in present law relating to the minimum tax on intangible drilling costs. As a result, the minimum tax on preference items applicable to intangible drilling costs for oil and gas wells would be modified to treat these intangible costs as preference items only to the extent they exceed the sum of the taxpayer's oil and gas production income straight line depreciation.

Rerefined lubricating oil

New lubricating oil would be exempt from the 6-cents-per-gallon excise tax, if it is combined with rerefined oil and the new oil makes up 55 percent or less of the mixture. If the new oil in the mixture exceeds 55 percent of the contents, the exemption would apply only to the new oil that would make up 55 percent of the mixture. In any case, the mixture must contain at least 25 percent waste or rerefined lubricating oil in order to qualify for the exemption.

Annual report on energy savings and revenue effects

Beginning August 1978, the President will be required to report each year to the Congress on the savings in energy use accomplished, the revenue received, and the revenue disbursed under each of the energy tax provisions.

The following sections of the report have been omitted:

IV—Explanation of Ad Hoc Committee Amendments

A. Amendments to Findings, Goals, Etc., of the Bill (page 37)

B. Amendments to Title I of the Bill—Pricing, Regulatory, and Other Nontax Provisions (pages 37-50)

C. Amendments to Title II of the Bill—Tax Provisions

1. Extension of Period for Residential Insulation and Solar and Wind Energy Equipment Credits

The Ways and Means Committee bill provides that both the residential insulation credit and the residential solar and wind credits are to apply from April 20, 1977, through December 31, 1982. The Ad Hoc Committee amendment makes these credits available for 2 additional years, through December 31, 1984.

Since the firms that produce insulating materials are presently operating near their optimal plant capacity, the Ad Hoc Committee is concerned that taxpayers, in their desire to use the credit before the expiration date, would increase demand above the industry's ability to produce insulation. The additional 2 years should moderate demand sufficiently to enable producers to fill each year's orders.

The extension of the solar and wind credit is designed to further encourage the installation of this newly commercialized technology for residential use.

Energy savings estimate

It is estimated that the 2-year extension of the credit period under the committee amendment would result in an additional decrease in fuel consumption in 1985 (over and above the 250,000 to 310,000 barrels-per-day decrease resulting under the Ways and Means Committee provision) of about 20,000 barrels of oil per day.

Revenue effect

It is estimated that this provision will result in a decrease in budget receipts of $748 million in fiscal year 1984 and $710 million in fiscal year 1985.

2. Increased Tax on Gasoline and Other Motor Fuels; Energy Conservation and Conversion Trust Fund

In order to encourage the conservation of energy, to promote conversion to alternate energy sources, and to provide revenue for States and energy-related projects, the committee amendment would impose additional taxes on gasoline, diesel fuel, and special motor fuels and would appropriate the revenue from these taxes to a new Energy Conservation and Conversion Trust Fund.

Increased tax on gasoline and other motor fuels

Imposition of tax

The new taxes on gasoline, diesel fuel, and special motor fuels would be in addition to the 4-cent Federal taxes provided on these fuels under present law. These new taxes would be imposed at the rate of 2 cents per gallon for fuel sold (or used) during 1978 and at a rate of 4 cents a gallon in 1979 and thereafter.

The additional tax on gasoline is a manufacturers excise tax imposed on gasoline sold by the producer or importer. It is generally imposed in the same manner as the current 4-cents-a-gallon Federal excise tax on gasoline. The additional tax on diesel fuel is a retailers excise tax which is imposed on fuel which is either sold for use, or used, as fuel in a diesel-powered highway vehicle. The additional tax on special motor fuels is a retailers excise tax imposed upon such fuels if they are sold for use, or used, in a motor vehicle or motorboat.[1] In general, these retailers excise taxes are patterned after the present law retailers excise taxes on diesel fuel and special motor fuels respectively.

Gasoline floor stocks taxes

When the additional tax is imposed at a 2-cent rate on January 1, 1978, and also when the additional tax is increased on January 1, 1979, there are also to be floor stocks taxes on the dates of such tax changes. This is the practice followed generally when a major manufacturers excise tax is increased, in order to provide the same tax on inventories held by dealers on the date of tax increase as on subsequent sales by manufacturers. The gasoline floor stocks tax is to be imposed at a rate equal to the difference between the new tax rate and the old tax rate, and is to apply to the dealer's stock on hand that has been subject to the manufacturers excise tax at the old rate. A "dealer" does not include a retailer, producer, or importer. Since the term "dealer" does not include a retailer, no floor stocks tax would be imposed on, for-example, gasoline which has been delivered to a service station for retail sales before the date of the tax increase.[2]

Present law exemptions or credits

Exemptions or credits, as under present law, are to be continued for the new gasoline and special motor fuels taxes in the case of motor fuels used: (1) by State and local governments, (2) by non-profit educational organizations, (3) as supplies on vessels or aircraft, (4) on farms for farming purposes, (5) by commercial aircraft, and (6) by certain aircraft museums. Also, use in intercity, local, and school buses will be exempt from these additional taxes to the same extent that such use is exempt from the present law 4-cents-a-gallon taxes under the bill (as provided by the Ways and Means Committee).

The exemption for export and the discretionary exemption for sales to the United States, which apply to the present 4-cent taxes, are not available in the case of the new conservation taxes.

Also, in the case of gasoline and special motor fuels, the partial exemption, or credit, for nonhighway use is not available. However, since the additional tax on diesel fuel, like the present tax on diesel fuel, is imposed only on fuel sold for use, or used, in a diesel-powered

[1] These special motor fuels are benzol, benzene, naptha, liquified petroleum gas, casing head and natural gasoline, and any other liquid fuel (other than kerosene, gas oil, fuel oil, gasoline, or diesel fuel). Also, in certain cases, the partial exemption of taxes for nonhighway use and local transit use are also applicable to diesel fuel and special motor fuels.

[2] The purpose of the floor stocks tax is to provide for an equality between the tax rate borne by fuel in dealers' inventories as of the date of the tax change and gasoline sold by the producer or importer after such date. Since the taxes on diesel fuel and special motor fuels are imposed at the retailer level, no similar floor stocks taxes are required with respect to these fuels.

highway vehicle, no additional tax would be imposed on diesel fuel used for off-highway operations.

Under this committee amendment, the additional taxes do not apply to noncommercial (general) aviation. However, another committee amendment would apply this tax to noncommercial aviation.

Amendments relating to highway and airport trust funds

The amendment makes technical changes in the Highway Trust Fund and the Airport and Airways Trust Fund. Under present law, all credits or refunds of taxes imposed on gasoline, diesel fuel, or other motor fuels are charged against either the Highway Trust Fund or the Airport and Airways Trust Fund. The effect of these changes is to charge these trust funds only with the amount of credits (or refunds) for overpayment of the 4-cent taxes imposed under present law. Credits or refunds of the new motor fuels taxes imposed under the committee amendment are to be charged against the Energy Conservation and Conversion Trust Fund.

Energy Conservation and Conversion Trust Fund

In general

The committee amendment creates an Energy Conservation and Conversion Trust Fund and establishes within the trust fund three separate accounts: (1) the Energy Program Account, (2) the Mass Transportation (Including Car Pooling, Etc.) Account, and (3) the States Account. The committee amendment appropriates to the trust fund the amounts received by the Treasury from the increased tax on gasoline and special motor fuels. The amounts appropriated to the trust fund are to be reduced by credits for repayments attributable to these taxes.

These amounts are to be transferred to the trust fund by the Secretary of the Treasury from the general fund at least quarterly. Of each amount transferred to the trust fund, the Secretary is required to place 50 percent in the Energy Program Account, 37½ percent in the Mass Transportation Account, and 12½ percent in the States Account.

In general, each separate account of the trust fund is to be treated as a separate trust fund, and is to be managed and accounted for separately. Each account in the trust fund is to be managed by the Secretary of the Treasury, who is to report annually to the Congress on each account's financial condition and the results of its operations during the preceding fiscal year, as well as each account's expected condition and operation during the next 5 fiscal years. The Secretary is directed to invest any portions of any account which in his judgment are not required to meet current withdrawals. Investments may be made only in interest-bearing obligations of the United States or obligations guaranteed both as to principal and interest by the United States. These obligations may be acquired either on original issue at the issue price, or by purchase of outstanding obligations at the market price. The Secretary is given authority to sell at the market price any obligations acquired by any account in the fund. The proceeds from any sale, plus any interest on these obligations, are to be credited to and added to the account.

Amounts in any account of the trust fund may be expended only for purposes specified for such account; however, appropriations acts are required for any expenditure from any account.

Energy Program Accounts

Under the committee amendment, amounts in the Energy Program Account may be used only for purposes of the Federal energy program. These purposes include, but are not limited to the following:

(1) the maintenance of the Strategic Petroleum Reserve (created by part V of Title I of the Energy Policy and Conservation Act);

(2) basic and applied research programs related to new energy technologies;

(3) development and demonstration of new energy technologies; and

(4) programs relating to the development of energy resources from properties (including off-shore properties) in which the United States has an interest.

Under the committee amendment, it is not intended that this provision be treated as specifying narrow areas for coverage, but rather merely broad general guidelines of the types of purposes for which expenditures may be made, when and as authorized by appropriations acts.

Mass Transportation Account

The committee amendment provides that amounts in the Mass Transportation (Including Car Pooling, Etc.) Account may be used only for projects involving: (1) mass transportation by bus, rail, etc., (2) exclusive or preferential lanes for buses, vans, and cars, and (3) car and van pooling. It is contemplated that the expenditures in all these categories will be directed toward more efficient transportation systems. The mass transportation account is not limited to encouraging mass transportation for local transit purposes, but is also intended to encourage mass transportation for intercity travel. No restrictions are intended to be placed on whether amounts may be spent for research and development, demonstration projects, capital expenditures or operating subsidies. To the extent that the expenditures are authorized by appropriations acts, any of these types of expenditures would be allowed.

The expenditures from this account are not limited to public transportation, but are also to recognize the importance of more efficient use of privately owned vehicles. Thus, the amounts in this account may be used for exclusive or preferential lanes for car pools and van pools, as well as buses. In addition, car pooling and van pooling projects may be funded from amounts in this account.

States Account

The States Account is established in recognition of the fact that a number of provisions in the bill will adversely affect revenues from State motor fuels taxes. In particular, the additional Federal gasoline taxes and the crude oil tax will cause the price of gasoline to increase, and the gas guzzler tax will increase auto mileage efficiency. Both of these types of changes will have an adverse impact on State motor

fuels tax revenues. The transfer of 12½ percent of the revenues collected from these new 4-cent motor fuels taxes is intended to compensate the States for this impact.

Under the Ad Hoc Committee amendment, the amounts in this account may be used only for payments to States (including the District of Columbia). The funds are to be distributed in accordance with the fuel consumption in the States, which is considered as a rough measure of the proportion in which State motor fuels tax revenues would be affected. There are two restrictions on the use by the States of these moneys. First, the payments are to be used by the States only in transportation programs, including the maintenance and rebuilding of highways. Second, the States may not use the moneys from this account either directly or indirectly for the purpose of obtaining Federal matching funds.

Energy saving estimate

It is estimated that the additional taxes on motor fuels will result in a decrease in motor fuel consumption equivalent to 17,000 barrels of oil per day in 1978, 40,000 barrels per day in 1979, and 80,000 barrels per day in 1985. While it cannot be estimated, considerable energy savings may result under the programs funded by the Energy Conservation and Conversion Trust Fund.

Revenue effect

It is estimated that this provision will result in an increase in budget receipts of $1.75 billion in fiscal 1978, $4.4 billion in fiscal 1979, and $6.0 billion in fiscal year 1985. As indicated above, all these sums will be transferred to the Energy Conservation and Conversion Trust Fund.

3. Increase in Tax on Fuels Used by Noncommercial Aviation

The committee amendment would increase the present 7-cent-a-gallon taxes on fuel used in noncommercial (general) aviation by 4 cents a gallon (for a total tax rate of 11 cents). In general, the same exemptions as apply to the present taxes on aviation fuel also would apply to this tax,[3] except that the exemption for exports does not apply to the new 4-cent taxes, and the Secretary of the Treasury is not authorized to exempt Federal agencies from them.

The committee believes that it is equitable to increase the burden on general aviation by the same 4 cents a gallon as is provided for other users of gasoline, diesel fuel, and special motor fuels to the extent that such users are currently subject to a fuels tax.

Although the net proceeds from the present taxes on aviation fuel are appropriated to the Airport and Airway Trust Fund, the revenues collected from these taxes are to be transferred to the Energy Conservation and Conversion Trust Fund to be used in the same manner as the other new fuels taxes transferred to that fund.

In general, this provision is to take effect on January 1, 1978.

[3] Under present law, exemptions from the 7-cent-a-gallon taxes are provided for farm use, military aircraft and aircraft used in foreign trade, State and local governments, exports, tax-exempt schools, and certain aircraft museums. Also, the Secretary of the Treasury is authorized to exempt Federal agencies from these taxes.

Energy savings estimate

The energy savings from this proposal is estimated to be negligible.

Revenue effect

It is estimated that this provision will result in an increase in budget receipts by $38 million in fiscal year 1978, $47 million in fiscal 1979, and $76 million in fiscal 1985.

4. Deletion of Special Rule for New New Oil for Purposes of Crude Oil Tax

Under present law (The Emergency Petroleum Allocation Act of 1973 as amended), price controls on oil are determined by the FEA, subject to certain legislative guidelines. The Ways and Means Committee bill is generally consistent with these price control regulations because the bill imposes the crude oil equalization tax on the difference between the controlled price of oil, under FEA regulations, and the uncontrolled (or world) price of oil. However, the Ways and Means Committee bill provided its own definition of new new oil for purposes of the crude oil tax, leaving open the possibility that the tax definition and the price control definition would not be consistent.

If some oil were considered as new new oil under the crude oil equalization tax but were treated as upper or lower tier oil under price controls, the producer could still not have received any higher price for that oil (because of price controls), but the crude oil equalization tax would not have applied. The net result would have been a windfall for the refiner who could have purchased oil at the low controlled price, without paying a full equalization tax, and could have sold that oil at the world price.

The ad hoc committee amendment eliminates this potential inconsistency by deleting the separate definition of "new new oil" for tax purposes.

Energy savings estimate

This amendment does not change the estimate of energy savings that will result from the crude oil equalization tax. The energy savings estimate remains at 430 to 650 thousand barrels per day.

Revenue estimate

The amendment will increase the estimate of budget receipts from the levels in the Ways and Means Committee bill by $49 million in fiscal year 1980, $137 million in 1981 and $49 million in 1982.

5. Deletion of Exemption from Tax on Business Use of Oil and Natural Gas for Facilities Exempt from Regulatory Program under Title I of Bill

The Ways and Means Committee bill provided an exemption from the users tax for the duration of certain exemptions prescribed under the regulatory program as set forth under title I of this bill. The ad hoc committee amendment deletes this exemption from the tax. The principal sanction available under the relevant sections of the regulatory program is an order prohibiting a plant from the use of oil or gas.

However, the users tax is a less drastic sanction and is designed to encourage conversion through a combination of taxes and rebates.

Under the Ways and Means Committee bill, the users tax applies only to the largest industrial users in the United States, covering about 1,400 firms. The purpose of this tax is to encourage the greatest amount of conversion and conservation that is possible among both the existing and the new facilities of each of these firms. If one facility in a firm cannot convert from the use of oil or gas, it would be appropriate to exempt it from the regulatory part of the energy program. But the user tax from this facility could be used to encourage conservation and to provide user tax credits that would be available to fund the conversion of another facility of that firm which can use an alternate fuel.

There may be individual cases where a firm has no conversion or conservation potential. But the bill carefully provides a procedure to cover special cases where the tax would impose an undue burden. Under this procedure, the Secretary of the Treasury may reclassify uses to a lower tax category, or exempt them entirely from the tax, where there are economic and technological problems which prevent that business from conserving or converting.

For these reasons, the ad hoc committee amendment deletes the exemption, provided under the Ways and Means Committee bill, for facilities which are exempt under the regulatory program.

Energy savings estimates

The amendment to delete this provision from the bill will increase energy savings from the level in the Ways and Means Committee bill by the equivalent of 250,000 to 400,000 barrels of oil per day by 1985.

Revenue estimate

This amendment will change the estimates of budget receipts in the Ways and Means Committee bill by a decrease of $3 million in fiscal year 1979 and then successive increases of $25 million in 1980, $3 million in 1981, $11 million in 1982 and $161 million in 1985.

6. Treatment of Cogeneration Facilities as a Utility for Purposes of Business Use Tax on Oil and Natural Gas

Under the Ways and Means Committee bill, cogeneration facilities of a utility are placed in Tier 3. No tax is imposed until 1983 and, at that time, the tax is imposed at a lower rate than that imposed on other boilers and turbines (Tier 2). The ad hoc committee amendment provides similar Tier 3 treatment for the use of oil or natural gas in the production of electricity or other useful energy in a qualifying industrial cogeneration facility (within the meaning of section 546(b)(2) of this bill). That section requires that in order to be "qualifying," the cogeneration facility must meet standards prescribed by the Federal Power Commission concerning minimum size and fuel efficiency. Only the fuel used in the industrial plant in the boilers engaged in cogeneration would be eligible for the Tier 3 tax treatment under the committee amendment.

The amendment adopted by the Ad Hoc Committee provides similar tax treatment of both industrial cogenerators and utility cogenerators. This is consistent with the policy determination of the Committee on Interstate and Foreign Commerce which, in providing for the removal of institutional barriers against cogeneration and the preven-

tion of discriminatory practices against cogenerators, provided for similar treatment for cogeneration, regardless of whether done by a utility or by an industrial cogenerator.

Energy savings estimates

The energy savings from this amendment are included in the revised estimate for the business use tax and credits, which is an additional 250,000 to 400,000 barrels of oil per day.

Revenue effect

It is estimated that this provision will result in a decrease in budget receipts from the levels in the Ways and Means Committee bill of $10 million in fiscal year 1980, $14 million in fiscal year 1981, and $10 million in fiscal year 1985.

7. Treatment of Use Tax Credit of Public Utilities for Regulatory Purposes

The Ways and Means Committee bill limits the extent to which the benefit of utility credits against the tax on business use of oil and natural gas may be passed through to consumers in the form of rate reductions. This limitation (presently provided for the investment tax credit) generally requires that the benefit be passed through in the form of lower utility rates over the useful life of the asset for which the credit is claimed through adjustments in the rate base. The Ad Hoc Committee believes that this question should be left to the discretion of State regulatory bodies. Therefore, the Ad Hoc Committee deleted this requirement.

Energy savings estimates and revenue effect

This amendment has no direct effect on the estimates of energy savings and budget receipts.

The following sections of the report have been omitted:

IV—Explanation of Ad Hoc Committee Amendments
  D. Budget and Energy Effects of Title II of the Bill (pages 59-69)
V—Economic and Energy Impacts of the Bill (pages 71-80)
VI—Cost of the Bill and Vote of the Committee (pages 81-93)
VII—Other Matters to be Discussed under House Rules (pages 95-97)
VIII—Changes in Existing Law Made by the Bill as Reported (pages 99-266)
IX-XIV—Supplemental, Minority, and Additional Views (pages 267-304)

95TH CONGRESS } HOUSE OF REPRESENTATIVES { REPT. NO. 95-543
1st Session } { VOL. II: APPENDIX

NATIONAL ENERGY ACT

REPORT

OF THE

AD HOC COMMITTEE ON ENERGY
U.S. HOUSE OF REPRESENTATIVES

ON

H.R. 8444

JULY 27, 1977.—Committed to the Committee of the Whole House on the State of the Union and ordered to be printed

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NATIONAL ENERGY ACT

JULY 27, 1977.—Committed to the Committee of the Whole House on the State of the Union and ordered to be printed

Mr. ASHLEY, from the Ad Hoc Committee on Energy, submitted the following

REPORT

[To accompany H.R. 8444]

The following sections of the report have been omitted:
A—Committee on Banking, Finance and Urban Affairs—Rept. 95-488 (pages 1-35)
B—Committee on Public Works and Transportation—Rept. 95-496, Part I (pages 37-54)
C—Committee on Government Operations—Rept. 95-496, Part III (pages 55-112)

95TH CONGRESS 1st Session } HOUSE OF REPRESENTATIVES { REPT. No. 95-496 PART III

ENERGY TAX ACT OF 1977

REPORT

OF THE

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

TOGETHER WITH SUPPLEMENTAL, ADDITIONAL, MINORITY, AND ADDITIONAL MINORITY VIEWS

ON

Title II of H.R. 6831

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95TH CONGRESS } HOUSE OF REPRESENTATIVES { REPORT
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Part III

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ENERGY TAX ACT OF 1977

JULY 13, 1977.—Ordered to be printed

Mr. ULLMAN, from the Committee on Ways and Means, submitted the following

REPORT

together with

SUPPLEMENTAL, ADDITIONAL, MINORITY, AND ADDITIONAL MINORITY VIEWS

[To accompany Title II of H.R. 6831, which on May 2, 1977, was divided and initially referred for a period ending not later than July 13, 1977, as follows: sections 101 through 109 and sections 201 through 603 to the Committee on Interstate and Foreign Commerce; sections 110 through 131, and, concurrently with the Committee on Interstate and Foreign Commerce, those portions of subpart 1 of part A of title I relating to financial assistance to residential customers defined in section 101, to the Committee on Banking, Finance and Urban Affairs; section 701 to the Committee on Government Operations; sections 721 through 746 to the Committee on Public Works and Transportation; title II to the Committee on Ways and Means; and sections 2 through 4 concurrently to all of the above committees]

The Committee on Ways and Means, to whom was referred the bill (title II of H.R. 6831) to provide for an energy tax policy to encourage energy conservation and conversion to alternate energy sources, having considered the same, report favorably thereon with an amendment and recommend that title II of the bill, as amended, do pass. The amendment strikes out title II of the bill and inserts a new text which appears in italic type in the reported bill.

I. OVERVIEW OF ENERGY TAX PROVISIONS

Need for an energy program

Domestic demand for oil and natural gas exceeds present domestic levels of production, including the oil and natural gas available in Alaska. Demand for oil and natural gas, moreover, has been expanding while domestic production has been declining, requiring increasing levels of imports. Presently, the United States is importing nearly half the oil it consumes, an increase from 30 percent in 1972.

Too great reliance on oil imports poses potential dangers for the U.S. economy foreign policy. One illustration is the embargo on sales to the United States by Arab countries in the Fall of 1973 and the subsequent fourfold increase in worldwide crude oil prices. The higher prices and the excessive oil imports have already had a serious adverse effect on the U.S. economy, and further increases in oil imports will only aggravate these undesirable patterns.

The Energy Tax Act of 1977 is an effort to curtail the rate of growth of domestic energy consumption and to encourage conversion from use of oil and natural gas to coal and other, more abundant sources of fuel and energy. Toward these ends, the bill employs the taxing power to raise the prices of energy consumption, especially where conservation and conversion are feasible objectives, to stimulate shifts to alternative fuels or to install energy conserving methods and to encourage installation of new technologies, such as synthetic gas, solar heat systems and nuclear or hydroelectric systems to generate electricity.

Consequently, the committee has approved a series of tax changes to conserve and convert domestic use of energy.

Summary of major tax provisions

Insulation credit.—To encourage residential energy conservation, the committee approved a tax credit of 20 percent of the first $2,000 of expenditures on insulation and other energy conserving components for a taxpayer's principal residence in existence on April 20, 1977. The credit is allowed on the cumulative spending total of $2,000 made from April 20, 1977, through December 31, 1982.

Solar and wind credit.—Homeowners also would be eligible for a credit up to $2,150 for solar water heating, space heating and air conditioning systems and for wind energy systems. The credit would be 30 percent of the first $1,500 and 20 percent of the next $8,500, which makes the credits applicable to a cumulative total of $10,000 of expenditures from April 20, 1977, through December 31, 1982. This credit would be available for both new and existing residences.

Gas guzzler tax.—A graduated excise tax would be applied to the sale of each passenger car that falls 3 to 5.5 miles per gallon below the efficiency standards set for each model year. The gas guzzler tax increases as a car's mileage rating moves further downward from the standard, i.e., the more inefficient the car is, the greater is the tax. The

tax applies first to model year 1979 vehicles, and the tax increases in severity each model year through 1985. Revenue from this tax will go into a trust fund to be used to retire portions of the public debt.

Crude oil equalization tax.—The committee also approved a tax on the first purchase of crude petroleum. The tax increases in three stages until 1980 when the tax would be fully effective and would bring the price (including tax) of domestic oil up to the world price of crude oil. The tax goes into effect in 1978 and would terminate after September 30, 1981. There is to be a rebate of the tax to users of oil for heating residences, educational institutions, hospitals and churches. There also would be rebates of the remaining tax revenues in 1978 to every adult. An equalization tax also applies to price-controlled natural gas liquids. Further, the bill provides authority for the President to suspend scheduled increases in the equalization taxes in the event an increase would be harmful to the economy.

Tax on business use of oil and gas.—A tax would be levied on the use of oil and natural gas by industry and electric utilities. The tax is to be applied in three tiers: Tier 1 is to encourage conservation where conversion to alternate fuels is not feasible; Tier 2 would apply to uses where conversion to alternate fuels is feasible, and Tier 3 would apply to electric utilities and to industrial plants where there is electrical generating capacity of 100 or more megawatts. Investment in alternative energy property could be credited against the use tax liability. The tax would begin in 1979 for industrial firms and 1983 for utilities.

Business energy investment credit.—An additional 10-percent energy investment credit would be available through December 31, 1982, for investment in alternative energy property (where the taxpayer elects this credit instead of the offset against the business use tax), advanced technology property, specially defined energy property, cogeneration property and certain recycling equipment. In addition, business insulation, which has been ineligible for the investment credit because it has been considered as a structural component, would be made eligible for the regular investment tax credit through 1982.

Other tax provisions

The other tax provisions include the following changes:

- Repeal of the personal deduction for State and local gasoline taxes for non-business use after December 31, 1977.
- Continuation of the existing 4-cents-a-gallon Federal excise tax on gasoline and other motor fuels through September 30, 1985.
- Removal of the 2-cents-a-gallon refund or credit for gasoline and other fuels used by motorboats.
- Repeal of the 10-percent excise tax on buses and the 8-percent excise tax on bus parts.
- Exemption of privately-owned intercity, local and school buses from excise taxes on fuels, tires, tubes and tread rubber, and lubricating oil.

- $300 tax credit on the purchase of electric powered automobiles.
- Denial of investment credit and accelerated depreciation for new oil or natural gas boilers where conversion to alternative fuels is possible and denial of investment credit for air conditioning and space heating units.
- 10-percent depletion rate for geothermal resources, up to the taxpayer's adjusted basis.
- Current deduction of intangible drilling expenses associated with exploration and development of geothermal resources.
- Limitation of the minimum tax on intangible drilling costs for geothermal resources and oil and gas production to the amount that exceeds the taxpayer's income from production of such resources.
- Exemption of rerefined lubricating oil from the excise tax on new lubricating oil.
- Annual report by the President on energy savings and revenues received and disbursed under this bill.

II. REASONS FOR THE ENERGY TAX PROVISIONS

The nation has delayed too long the bold actions needed to solve our energy problem. The United States is rapidly depleting its oil and gas resources, and the U.S. Geological Survey estimates that at current rates of production we have only enough oil and gas to last about 45 years. Worldwide demand for oil is also growing much more rapidly than the worldwide capacity to produce oil, and many experts are predicting either further large price increases or outright oil shortages in the early 1980's. U.S. reliance on oil imports now exceeds what it was prior to the Arab oil embargo which began in the Fall of 1973, and unless there is decisive action, this dangerous dependence is likely to increase significantly during the next ten years. Furthermore, the high price we pay for oil imports, together with the large volume of these imports, has had a serious adverse effect on the U.S. economy, and further increases in oil imports will worsen these undesirable economic trends. Finally, the increasingly severe shortages of natural gas can be expected to grow progressively worse unless present policies are changed to discourage natural gas consumption and to encourage additional gas supplies.

The "Energy Tax Act of 1977" (Title II of H.R. 6831) responds to these extremely serious problems by providing incentives to cut down energy consumption in the United States and to convert from the use of oil and gas to coal, nuclear power, and other more abundant energy sources. The bill raises taxes on many users of energy, particularly in cases where conservation or conversion from oil and gas is relatively easy. The bill also provides tax incentives to both individuals and businesses for investments to conserve energy or to convert from oil and gas to other energy sources.

The committee is greatly concerned that the nation's program for energy conservation and conversion be equitable and, in designing the tax changes in this bill, has taken into account the ability of various energy users to pay additional taxes. The committee believes that its program meets this essential criterion of fairness.

The need for decisive action to reduce energy consumption and to convert from oil and gas to more abundant energy sources can be seen by examining statistics on U.S. energy use.

Energy consumption trends

Table 1 shows energy consumption in the United States from 1947 to 1976, measured in quadrillions of Btu's, or quads.[1] Since 1947, U.S.

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[1] A Btu, or British thermal unit, is the amount of energy needed to raise the temperature of one pound of water by one degree Farenheit. A barrel of crude oil, containing 42 gallons, contains 5.8 million Btu's. Natural gas contains about one million Btu's per thousand cubic feet (mcf). One million barrels of oil per day equals approximately two quads per year, and one trillion cubic feet of natural gas equals about one quad.

energy consumption has more than doubled—from 33.0 quads in 1947 to 74.2 quads in 1976. The data for 1976 indicate that the drop in energy consumption after 1973 resulted from the recession, not from a major change in the fuel consuming habits of the American people. A continuation of this rapid growth in energy consumption is not possible for very much longer, because the United States relies too heavily on rapidly depleting sources of energy, and this bill is designed to effect a significant reduction in energy demands.

Table 1.—Energy consumption in the United States, 1947-76

Year	*Energy consumption (quadrillion Btu's)*
1947	33.0
1950	34.0
1955	39.7
1960	44.6
1965	53.3
1966	56.4
1967	58.3
1968	61.7
1969	65.0
1970	67.1
1971	68.7
1972	71.9
1973	74.6
1974	72.6
1975	70.6
1976	74.2

SOURCES: *Statistical Abstract of the United States 1976* (1947-72) and *Monthly Energy Review* (1973-76).

Table 2 compares U.S. energy consumption in 1974 with that of other industrial countries. (The measure of energy in table 2 is coal-equivalents; that is, other sources of energy are converted to the amount of coal that would produce the same amount of energy.) The United States consumes at least twice as much energy per capita as any other country listed in the table. Although Sweden and Switzerland each have a higher gross national product per capita than the United States, U.S. energy consumption per capita is 1.97 times that of Sweden and 3.18 times that of Switzerland. Germany has a per capita GNP approximately equal to that of the United States, but it uses only half as much energy per capita.

Half of the difference in consumption levels can be attributed to the transportation sector, about evenly divided between the higher efficiency of the European automobile fleets and the generally more extensive use—partly because of greater distances—of automobiles and trucks in the United States. About a quarter of the difference in overall energy consumption is related to differences in the energy consumption in residences, even after making adjustment for differences in climate. Residences in Sweden, Germany and Switzerland are built

with greater insulation. In the United States, there is a far greater proportion of single family residences; the rooms are larger; there are more rooms in a residence; the average room temperature is higher; and the whole house is heated. Air conditioning is not used extensively in Europe. European industry is also more energy-efficient than American industry.

Those statistics show that it is possible to maintain a high standard of living, such as exists in such countries as France, Germany, Sweden and Switzerland, while consuming considerably less energy per capita than does the United States. They indicate that the energy goals embodied in this bill can be achieved—if tax and other policies are adjusted to give people the appropriate incentives to conserve energy.

Table 2.—Energy consumption per capita in various countries, 1974

Country	Consumption of energy—coal equivalent (million metric tons)	Consumption of energy per capita (kilograms of coal—equivalent)
United States	2, 433. 5	11, 485
Germany	353. 0	5, 689
United Kingdom	306. 5	5, 464
France	227. 6	4, 330
Italy	178. 6	3, 227
Japan	421. 0	3, 839
Sweden	47. 4	5, 804
Switzerland	23. 3	3, 608
World total	7, 953. 0	2, 100

Source: *Statistical Abstract of the United States 1976.*

Demand for petroleum and oil imports

Table 3 shows the U.S. supply and demand for petroleum, along with the level of imports, between 1955 and 1976. Since 1955, demand has approximately doubled—from 8.5 million barrels per day to 17.4 million barrels per day. U.S. production of crude oil and natural gas liquids did rise between 1955 and 1970, but at a slower rate than demand; therefore, there was a gradual rise in imports. After 1965, U.S. oil imports began to exceed spare capacity within the United States, so that we were no longer self-sufficient in oil. Since the 1972 peak in U.S. oil production, imports have grown at an especially rapid rate. In 1976 imports were 7.3 million barrels per day, or 42 percent of U.S. oil demand. Thus, except for the years 1974–75, when energy consumption was sharply reduced by the severe recession, there has been a steady growth in oil demand. Moreover, the trend is now towards lower production as U.S. oil fields become depleted.

Table 3.—U.S. oil demand, supply and imports, 1955–76

[In millions of barrels per day]

Year	U.S. demand for petroleum	U.S. production of crude oil	U.S. production of natural gas liquids	U.S. spare capacity for crude oil	U.S. oil imports
1955	8.49	6.81	.77	1.78	1.25
1956	8.82	7.15	.80	2.08	1.44
1957	8.86	7.17	.81	2.78	1.57
1958	9.15	6.71	.81	2.60	1.70
1959	9.49	7.05	.88	2.67	1.78
1960	9.81	7.04	.93	2.71	1.82
1961	9.99	7.18	.99	2.75	1.92
1962	10.41	7.33	1.02	2.63	2.08
1963	10.75	7.54	1.10	2.67	2.12
1964	11.03	7.61	1.16	2.73	2.26
1965	11.52	7.80	1.21	2.45	2.47
1966	12.10	8.30	1.28	2.24	2.57
1967	12.57	8.81	1.41	2.12	2.54
1968	13.40	9.10	1.50	1.90	2.84
1969	14.15	9.24	1.59	1.38	3.17
1970	14.71	9.64	1.66	1.33	3.42
1971	15.23	9.46	1.69	.69	3.93
1972	16.37	9.44	1.74	.20	4.74
1973	17.30	9.21	1.74		6.26
1974	16.65	8.77	1.69		6.11
1975	16.32	8.38	1.63		6.06
1976	17.44	8.12	1.69		7.29

Source: Independent Petroleum Association of America (1955–71) and *Monthly Energy Review* (1972–76).

The United States cannot continue to behave as if it had plenty of spare capacity for oil production and could expect further growth in domestic oil supplies. The best we can reasonably hope for is a slowdown in the rate of decline in U.S. oil production. (Even the production from the large Alaskan oil fields will only serve to raise U.S. production back to the 1970 level.) We have to adapt ourselves to the reality that oil consumption cannot be permitted to continue to grow rapidly.

Our reliance on imported oil is expected to increase dramatically if present policies are continued. The Federal Energy Administration predicts that, under current policy, oil demand will rise from 17.4 million barrels per day (mbd) in 1976 to 21.1 mbd in 1980, 22.8 mbd in 1985 and 24.9 mbd in 1990. These levels of demand will imply imports of 10.2 mbd in 1980 (48 percent of consumption), 11.5 mbd in 1985 (50 percent of consumption), and 14.5 mbd in 1990 (58 percent of consumption). These alarming FEA estimates are consistent with most private forecasts.

Such an increase in our reliance on oil imports is clearly unacceptable. It would greatly constrain our foreign policy and do considerable damage to our economy. Attempting to achieve historical growth rates in demand for oil through additional domestic production is probably impossible and, even if it were possible, would serve only to deplete our limited reserves of oil and gas and postpone for a brief period of time the inevitable day of reckoning. A major goal of this bill, therefore, is to achieve a sharp reduction in oil imports by encouraging a sharp drop in the growth rate of oil consumption.

The natural gas problem is equally serious. Gas shortages have grown progressively worse in each of the past several winters and reached crisis proportions last winter. It is essential to convert industrial users of gas to coal, where this is feasible, and to encourage residential users to conserve. Otherwise, the economic damage from natural gas shortages and high prices will continue to grow. The bill contains substantial incentives to conserve gas and to convert energy use from gas to coal.

Clearly, the United States needs to reduce its demand for oil and gas. The Energy Tax Act of 1977 is intended to achieve much of the necessary reduction in a manner which is as equitable as possible and which minimizes any adverse economic effects resulting from the energy conservation and conversion program. The committee believes that its bill achieves these ambitious goals.

III. SUMMARY OF THE ENERGY TAX PROVISIONS

A. Residential Credits

Residential energy conservation credit

The bill provides a credit of 20 percent on the first $2,000 of cumulative expenditures on home insulation and other energy conserving components for a maximum credit of $400. The credit would be available for installations made from April 20, 1977, through December 31, 1982.

Insulation means materials that will reduce the heat loss or heat gain of a residence. Attic, floor and wall insulation made of fiberglass, rock wool, cellulose or styrofoam are examples of insulating materials. Energy conserving components include a replacement burner for a furnace that provides increased combustion efficiency, devices to modify flue openings, automatic ignition systems that replace a standing gas pilot light, exterior storm or thermal doors or windows, a clock thermostat and exterior caulking or weatherstripping of doors or windows.

The expenditures must be made for a principal residence that was in existence on April 20, 1977. Vacation homes and other residences do not qualify for the credit, nor do residences that were constructed after April 20, 1977, or were substantially completed after that date. If a taxpayer moves to another principal residence after taking the maximum credit on a previous principal residence, he would be eligible for another $400 credit for his new residence before January 1, 1983.

Owners and renters will be eligible for the credit. Cooperative and condominium housing owners are eligible for the credit up to the $400 maximum on their proportionate shares of qualifying expenditures made in common. Joint occupants of a principal residence must allocate the credit.

An increase in the cost or other basis of the residence by the amount of qualifying expenditures must be reduced by the amount of the credit.

Residential solar and wind energy equipment credit

A credit up to $2,150 would be available on the first $10,000 of expenditures on solar and wind energy equipment credits. The credit is 30 percent of the first $1,500 spent and 20 percent of the next $8,500 spent for installations of this equipment from April 20, 1977, through December 31, 1982.

Eligible equipment covers equipment that uses solar energy to heat or cool, or to provide hot water for a principal residence, and equipment that uses wind to generate electricity and other forms of energy. Solar and wind energy equipment only need to be installed in connection with a residence rather than in or on it, but they do not include backup systems of conventional heating or cooling equipment.

For solar and wind energy equipment, the principal residence may be either an existing structure or a new structure that was completed after April 20, 1977. Owners and renters are eligible for the credit. Members of cooperative and condominium associations are eligible for the credit to the maximum amount for their proportionate shares of the common qualifying expenditures.

The taxpayer's cost or other basis in his residence may be increased by the amount of the expenditures for this equipment less the amount of tax credits taken.

B. Transportation

Gas guzzler tax

The tax would apply to manufacturers sales of each automobile that falls below efficiency standards established for each model year. The efficiency standard increases for each model year 1979 through 1985. The standards start from 3 to 5.5 miles per gallon below the fleetwide average standards imposed under the Energy Policy and Conservation Act (EPCA). The tax applies to automobiles weighing less than 6,000 pounds, but does not apply to trucks with a cargo carrying capacity less than 1,000 pounds.

A separate tax table applies to each model year 1979 through 1985; the table for 1985 applies to later model years as well. The lowest tax increases from $339 for an auto efficiency rating of 15 miles per gallon in 1979 to $397 for an efficiency rating of 23.5 miles per gallon in 1985 and later years. The highest tax each model year applies to vehicles with efficiency ratings at or below 12.5 or 13 miles per gallon and increases from $553 in 1979 to $3,856 in 1985 and later model years.

The tax will apply to new and used imported cars, according to their model years, and the tax is to be imposed on the importer. For automobiles leased by a manufacturer, the first lease is to be treated as a sale that gives rise to the tax.

The basis of the automobile is to be reduced by the amount of the gas guzzler tax. In other words, the amount of this tax is not eligible for depreciation, the investment tax credit or gain or loss on resale.

The bill also establishes a Public Debt Retirement Trust Fund into which the proceeds of the gas guzzler tax will be deposited. The proceeds are to be used to retire obligations of the United States that are included in the public debt.

Repeal of personal deduction for State gasoline tax

The bill repeals the personal deduction for State and local government taxes paid on the purchase of gasoline and diesel and other motor fuels for nonbusiness use after December 31, 1977.

Extension of excise tax on gasoline and other motor fuels

The current Federal excise tax of 4 cents a gallon on gasoline and other motor fuels will be continued at that rate through September 30, 1985. This tax is currently scheduled to be reduced to one and one-half cents a gallon after September 30, 1979. The committee took no action at this time on the Highway Trust Fund which will continue to receive these funds under present law through September 30, 1979.

Repeal of refund of motor boat fuel tax

The bill repeals the 2-cent-a-gallon refund (or credit) of the excise tax on gasoline and special motor fuels used in a motorboat. The refunds are presently made because this is a nonhighway use of gasoline. The committee decided to conform the tax on motorboat use of fuel to the tax on highway use. The increased tax on motorboat fuel will go into the Land and Water Conservation Fund as a user tax on motorboat operators (as does the present 2-cents-a-gallon tax).

Repeal of excise tax on buses and bus parts

The 10-percent excise tax on all buses and the 8-percent excise tax on bus parts and accessories will be repealed under the bill. Parts and accessories that may be interchangeable between trucks and buses will be taxed on sale unless the purchaser provides an exemption certificate which indicates that the part or accessory is purchased for use on a bus.

Removal of excise taxes on items used with certain buses

The committee removed the excise taxes on tires, inner tubes and tread rubber, gasoline and other motor fuels, and lubricating oil sold for use with intercity, local, and school buses. Removal of these excise taxes on private transit and private school bus operators puts them on a par—with respect to these excise taxes—with governmental and nonprofit school bus operators.

Tax credit for electric motor vehicles

New electric cars purchased for personal use will be eligible for a tax credit of 100 percent of the first $300 of the purchase price. A qualified electric motor vehicle is a 4-wheeled vehicle manufactured for use on public roads that is powered by an electric motor which receives electric current from rechargeable storage batteries or other portable sources.

C. Crude Oil and Natural Gas Liquid Equalization Taxes and Rebates

Crude oil equalization tax

Under the bill, an excise tax is imposed on the first purchase (generally by the refiner) of price controlled, domestically produced crude oil. The tax increases the cost of all crude oil to the world price by 1980. The termination date of the tax is September 30, 1981.

The tax is imposed in three stages. In 1978, a tax of $3.50 per barrel is imposed on lower tier oil (old oil under current regulations). In 1979, the tax will be raised so that the national average refiner acquisition cost will be identical for lower tier and upper tier oil. In 1980 and for the duration of the tax, the tax will equal the difference between the wellhead prices of uncontrolled and controlled crude oil of the same classification. As a result, the price of controlled oil plus the tax will be raised to the world price of oil in 1980.

New new oil will be subject to a special tax rate which may not exceed the difference between the uncontrolled price and highest

controlled price for crude oil of the same classification. New new oil is defined in the bill as crude oil produced from a property that did not have any commercial production at any time during the 90-day period ending on April 20, 1977.

There are exemptions for oil used to extract oil and natural gas and for oil used to produce natural gas liquids.

Natural gas liquids equalization tax

The tax is imposed on sales to end users in three stages based upon the difference (the price gap) between the controlled price of the liquid and the wholesale price for No. 2 distillate in the region, adjusted for differences in Btu content. The tax will be equal to one-third of the price gap in 1978, two-thirds of the gap in 1979, and equal to the entire gap in 1980 and later years.

There are exemptions for natural gas liquids used in residences, on farms and in churches, schools and hospitals.

Presidential authority to suspend the tax

The President is granted authority to suspend any or all of the equalization tax increase, if there is a significant increase in the world price of oil that will result in a higher equalization tax and will have a substantial adverse economic effect.

Crude oil credits; special payments and refunds

Taxpayer credits.—The net receipts from the equalization taxes will be apportioned equally and returned to each taxpayer in 1978 through a new tax credit. Single taxpayers and married persons filing separately will receive a single payment, and married persons filing joint returns and heads of households (single persons with dependents) will receive a double payment.

The bill instructs the Secretary of the Treasury how to estimate these tax credits.

The credit will be limited to a taxpayer's tax liability, except for recipients of the earned income credit. The estimated amounts of these payments will be reflected in the withholding tax schedules for 1978.

Special payments.—Special payments will be made in 1979 to adults who are recipients of monthly benefits under social security, railroad retirement or supplemental security income. These payments will be made in the fall of 1979 and will equal the credits rebated to individual taxpayers. Special payments will be reduced by any tax credit received in order to avoid double payments.

Special payments also will be made to adults who receive aid to families with dependent children. Other adults who do not receive a tax credit or special payment under one of the programs referred to above may file an appropriate form with the Secretary of the Treasury in order to receive a roundup payment.

The bill also authorizes payments to the governments of Puerto Rico and the possessions, if they submit acceptable plans to the Secretary of the Treasury, for distribution of amounts similar to the tax credits and special payments.

Heating oil refund.—An exemption is provided from the crude oil equalization tax for heating oil used in residences, churches, schools,

universities and hospitals. Distributors of heating oil will receive a refund of the equalization tax for each gallon sold to one of these users, so long as the refund is passed through completely to the customers as lower prices.

D. Tax on Business Use of Oil and Gas and Credit

Excise tax on business use of oil and gas

A tax would be imposed on the use of oil or natural gas as fuel in a trade or business. Three levels of tax would be imposed: Tier 1 which would apply to an industrial use where *conservation* in fuel consumption is feasible; Tier 2 which would apply to uses of oil or natural gas in which *conversion* to another fuel is feasible; and Tier 3 would apply to electric utilities and industrial producers of electricity using boilers with a total rating of at least 100 megawatts per plant.

The tax on Tier 3 uses and on use of oil in Tiers 1 or 2 would be determined according to the following schedules:

Year of use	Tax on oil (per barrel)			Tax on natural gas (per million Btu)
	Conservation tier (Tier 1)	Conversion tier (Tier 2)	Electric utilities (Tier 3)	Electric utilities (Tier 3)
1979	$0. 30	$0. 30	None	None
1980	. 60	. 60	None	None
1981	1. 00	1. 00	None	None
1982	1. 00	1. 45	None	None
1983	1. 00	2. 00	$1. 50	$. 55
1984	1. 00	2. 50	1. 50	. 65
1985 and thereafter	1. 00	3. 00	1. 50	. 75

With respect to the industrial use of natural gas in Tier 1 and Tier 2 categories, the tax would be determined on a variable tax basis by subtracting a cost differential, which would be reduced annually from $1.35 to $.30 for Tier 1 and from $1.05 to zero for Tier 2 by 1985, and the user acquisition price per million Btu of gas from the natural gas target price per million Btu for the region in which the gas is used. The basis for determining the natural gas target price is the average regional price of all No. 2 grade distillate oil sold during the preceding calendar year in the region, adjusted for differences in energy (Btu) content between such oil and natural gas.

Beginning in 1981, the tax rates would be adjusted annually for inflation that occurs after 1979. The implicit price deflator for the gross national product would be used as the index of inflation. The index for the calendar year preceding the current calendar year would be used in order to inform the taxpayer as early as possible in the current year what the tax rate would be.

In the case of the tax on natural gas for use in the production of electricity for sale, the tax would not exceed the amount necessary to make the firm's cost of gas (including the tax) equal to the cost of the residual oil (including the tax) in the region where the gas is used. The inflation adjustment also would apply in this case.

The President could suspend the tax for a period up to one year, if he believes it would have an adverse economic effect. A suspension plan would have to be submitted to Congress, and it would be subject to a veto by either House before the end of 15 days.

Industrial process use would be exempt from the tax when the use of fuels other than oil or natural gas would materially and adversely affect the manufacturing process or the quality of the manufactured goods, and the use would not be economically and environmentally feasible.

An exemption from the tax would be provided to nonindustrial uses of oil and natural gas in residential facilities, in transportation (including pipelines), on a farm for farming purposes, in nonmanufacturing commercial buildings, and in the exploration, development and production of crude oil and natural gas.

Oil or natural gas would be exempt from taxation if used in a facility that was in existence or under construction on April 20, 1977, and which was precluded from using coal by State air pollution regulations in effect on that date or by Federal air pollution regulations. State regulations in effect on that date would also be grounds for exemption if such regulations were necessary to meet a requirement of Federal law. A regulation of an agency having jurisdiction over a facility under an approved State Implementation Plan also would be the basis for an exemption.

An industrial use would be granted an exemption from tax for the duration of an exception provided under specified provisions of Title I of the National Energy Act.

In addition to oil or natural gas employed in exempt uses, firms would also be able to exempt from taxation the Btu content of 50,000 barrels of oil per year (i.e., 300 billion Btu). In cases of a regional competitive disadvantage, the Secretary of the Treasury may provide additional exempt amounts for individual plants, and he is required to publish the identification of taxpayers and plants which receive additions to their exempt amounts.

The Secretary of the Treasury would establish a procedure for reclassifying uses to a category which is taxed at a lower rate or which is exempt from tax. Reclassification would depend on the extent to which reduction in oil and natural gas use could be achieved as a result of the tax.

Credit against tax on business use of oil and gas

A taxpayer may elect a credit against the use tax of $1 for each dollar of qualified investment, up to 100 percent of the taxpayer's oil and natural gas use taxes, made after April 20, 1977. If the amount of investment is in excess of the amount of use taxes for the year, a carry-

forward is permitted against use taxes in future years and a carry-forward to 1981 is provided for use taxes incurred in 1979 and 1980.

Utilities would be allowed to carry forward qualifying investment expenditures for offset against use tax liabilities that would be incurred beginning in 1983. Utilities would be allowed a credit to the extent that old oil and gas boilers are replaced or phased down for peakload or standby use (1500 hours or less a calendar year).

Where a phased-down old boiler is used between 1500 and 2000 hours in a calendar year, a penalty equal to the use tax would be imposed. Taxes paid in such cases would not be available for offset by qualified investment expenditures. Where old boilers would be used more than 2000 hours in a calendar year, there would be a recapture of credits against tax.

The taxpayer who elected this alternative would receive the regular investment tax credit on his qualified energy investment expenditures only to the extent that a credit against the use tax was not claimed for the same investment outlay.

The credit would not be available after 1990, except for qualified property on which construction had begun.

Qualified energy investment which could be a credit against the use tax includes the cost of alternative energy property placed in service during the year or, if the taxpayer elects, the progress expenditures made for that property during the year.

Alternative energy property includes new, depreciable, tangible property which is used by a taxpayer in his trade or business, which has a useful life of at least 3 years and which is not used predominantly outside the United States. It does not include a building or its structural components and does not include property to be used in the business of leasing. It includes—

(1) a boiler whose primary fuel is an alternate substance,

(2) a burner and equipment necessary to supply fuel to a combustor other than a boiler for which the primary fuel is an alternate substance,

(3) equipment used in the production of energy by nuclear, hydroelectric, or geothermal power other than the fuel, steam, turbines or equipment beyond the turbine stage,

(4) equipment for converting an alternate substance into synthetic gas,

(5) pollution control equipment required to be installed in equipment described above (other than equipment required on April 20, 1977, to be installed on a facility using coal),

(6) equipment used for unloading, transferring, storing, reclaiming from storage and preparation of an alternate substance for use in the equipment described above or in a facility which uses coal as a feedstock for products other than coke, and

(7) the costs for plans and design for equipment described above.

An alternate substance would be a fuel that is not oil, natural gas or a product of oil or natural gas.

E. Business Energy Property Tax Credit; Investment and Depreciation Changes

Business energy credit

There would generally be a 10-percent business energy tax credit (in addition to the investment credit provided under present law) for investments by business in qualified property intended to reduce the amounts of oil, natural gas or other energy consumed in heating or cooling a building or used in an industrial process.

The credit would be available for investments in qualifying property made after April 19, 1977, and before January 1, 1983. Where credits are generated by investments in alternative energy property, they may be applied against 100 percent of the taxpayer's income tax liability, rather than the 50-percent limitation that is now generally available.

The business energy tax credit would be available for alternative energy property as an option for taxpayers who would be liable for the oil and natural gas use taxes. The taxpayer could elect either the dollar-for-dollar credit of the use taxes or the business energy credit for investments in alternative energy property. A taxpayer who elected the credit against the use tax would receive the regular investment credit only on the amount of the investment that was not credited against the user tax.

Qualifying property.—For the business energy tax credit, qualifying property includes alternative energy property which is described above. Other types of property which would receive the 10-percent additional energy investment credit are:

(1) expansion of cogeneration property installed in an existing facility;

(2) advanced technology property which would use solar, geothermal, or wind energy to provide heat, cooling or electricity;

(3) specified items of equipment (such as recuperators, heat wheels, and energy control systems) which would recover waste heat and gases or otherwise reduce energy consumption, and also equipment to modify existing facilities to allow the use of oil or natural gas and at least 25 percent of some other substance in a combustor or to produce an industrial feedstock; and

(4) equipment to recycle solid waste and to sort and prepare solid wastes for recycling.

In order to qualify, property or equipment under these categories generally must be new property which would be used in connection with a building or facility in existence or substantially completed by April 20, 1977. Where the property would be added to an industrial process, this process must have been carried on as of April 20, 1977.

Business insulation

For purposes of the regular investment credit, insulation installed in connection with an existing building or industrial facility would be qualifying property through 1982. Insulation includes storm doors and windows, thermal glass and double glazing.

Denial of regular investment tax credit and accelerated depreciation

The regular investment credit would be denied for air conditioners and space heaters.

The regular investment credit also would be denied for new oil and gas boilers. Straight-line depreciation would be required for these boilers, and the 20-percent variance from the guideline lives for depreciable property under ADR would not be available for these boilers. These limitations, however, would not apply where the use of alternative fuel (coal) is precluded by Federal or State regulations or where the use of oil or gas qualified as an exempt process use.

These rules would be prospective with exemptions only for binding contracts in existence on April 20, 1977.

Depreciation adjustment for planned retirement of boilers

If a taxpayer certifies that he plans to replace or retire a boiler or other combustor which uses oil or natural gas as a fuel before a specified date, the undepreciated value of the equipment would be deductible using the straight line method and a useful life equal to the period from certification to the specified date for retirement. Interest would be charged on the tax benefit that would accrue as a result of this provision, if the retirement takes place later than the specified date.

F. Miscellaneous Provisions

Tax treatment of geothermal expenses

A current deduction would be allowed for intangible drilling costs related to the exploration and development of geothermal resources. To the extent that these intangible drilling costs exceed the taxpayer's income from the production of geothermal resources, these costs would be subject to the minimum tax on preference income.

In addition, the committee provided percentage depletion at a 10-percent rate for all geothermal resources, subject to the limitation that the total amount of depletion allowed with respect to any property is not to exceed the taxpayer's adjusted cost basis in that property.

Minimum tax on intangible drilling costs for oil and gas wells

The committee extended beyond 1977 the provision in present law relating to the minimum tax on intangible drilling costs. As a result, the minimum tax on preference income applicable to intangible drilling costs for oil and gas wells would be modified to treat these intangible costs as a preference income only to the extent they exceed the taxpayer's oil and gas production income.

Rerefined lubricating oil

New lubricating oil would be exempt from the 6-cents-per-gallon excise tax, if it is combined with rerefined oil and the new oil makes up 55 percent or less of the mixture. If the new oil in the mixture exceeds 55 percent of the contents, the exemption would apply only to the new oil that would make up 55 percent of the mixture. In any case, the mixture must contain at least 25 percent waste or rerefined lubricating oil in order to qualify for the exemption.

Annual report on energy savings and revenue effects

Beginning in August 1978, the President will report each year to the Congress on the savings in energy use accomplished, the revenue received, and the revenue disbursed under each specific program contained in Title II of H.R. 6831, The Energy Tax Act of 1977.

The following section of the report has been omitted:
D—Committee on Ways and Means—Rept. 95-496, Part III
IV—Energy Savings Estimates and Budget Effects of Energy Tax Provisions (pages 139-150)

V. EXPLANATION OF ENERGY TAX PROVISIONS

A. RESIDENTIAL ENERGY CREDITS

1. Residential Insulation and Other Energy-Conserving Component Credit (sec. 2011 of the bill and new sec. 44C of the Code)

Present law

Under present law, no special tax credit or deduction is allowed for the installation of insulation or other energy-conserving components in or on a taxpayer's residence. However, if these installations constitute capital improvements to a residence, the amount of the expenditures involved can be added to the taxpayer's basis in the residence for purposes of determining gain or loss on a subsequent sale of that residence.

Reasons for change

A substantial portion of our domestic energy consumption is used to heat or cool residences. Currently, about 23.7 percent of our domestic consumption, or about 7 percent of total world demand, is used in the United States for residential purposes. Surveys have indicated that many residences in the United States are not adequately insulated.

Because of the substantial energy savings that may be effected by proper insulation of homes and other energy-conserving measures, and to reduce the potential problems in the event of any future energy shortages (such as the 1973–74 shortage which resulted from the oil embargo), the committee's bill includes a nonrefundable income tax credit to provide homeowners and tenants with an incentive to conserve energy by immediate installations of insulation and other energy-conserving components.

The credit is provided for a limited number of years (through 1982) in order to accelerate the purchase and installation of insulation and other energy-conserving components in order to achieve the energy savings as soon as possible.

The committee hopes that the States and localities will recognize the need for enacting laws in the immediate future to exempt from property taxation increases in value resulting from insulation and other energy-conserving component improvements.

Explanation of provision

Nature, amount, and period of credit

The committee's bill provides a nonrefundable income tax credit for insulation and other energy-conserving component expenditures for installations in or on the principal residence of the taxpayer. The credit is 20 percent of the first $2,000 of qualifying expenditures. Thus, the maximum credit would be $400.

In determining the credit, the $2,000 maximum allowable expenditures amount is to be reduced by previous expenditures by the taxpayer which were taken into account in computing the energy conservation expenditures credit (all or any part of which was allowed) for prior taxable years. An individual will be eligible for the maximum credit each time he changes his principal residence. Thus, an individual would be eligible for the maximum credit for qualifying expenditures on his new principal residence, notwithstanding the allowance of the credit for qualifying expenditures on his previous principal residence and notwithstanding the allowance of the credit to a prior owner of the individual's new principal residence.

The entire cost of insulation or other energy-conserving components property is allowed toward the credit only if at least 80 percent of the use of the property is for personal residential purposes. If less than 80 percent of its use is for personal residential purposes, the amount is reduced proportionately. For example, if an expenditure of $3,000 is made, but only 50 percent of the use of the property is for personal residential purposes (the other 50 percent of use being for business purposes), the allowed credit will be $300 (the allowable credit on $1,500, which is 50 percent of $3,000). For purposes of this provision, use for a swimming pool is not to be treated as personal residential use.

In order to avoid administrative burdens which could result from credit for only a small amount of qualified expenditures in a year, a minimum credit amount of $10 for any taxable year is required with respect to any tax return (joint or separate) if any credit is to be allowed. This minimum credit requirement applies to the aggregate of the credits claimed for a taxable year for solar and wind energy expenditures and for insulation and other energy-conserving component expenditures.

The credit is to be nonrefundable, that is, it may not exceed an individual's tax liability for any year.[1]

The credit is to be available for expenditures made on or after April 20, 1977, and before January 1, 1983.

When qualified expenditures are treated as made

Expenditures for insulation and other energy-conserving components (including expenditures for installation) are to be treated as made when the original installation of the property is completed. Con-

[1] In determining the amount of tax liability against which the credit may be applied, the bill provides that the tax liability is first reduced by the sum of the credits which are allowable under a section (other than 31, 39 and 43) in Part IV, Subchapter A, of Chapter 1 of the Code (relating to credits against tax) having a lower number or letter designation than this newly added section, 44C. This means that before applying this credit to a taxpayer's liability, the amount of the liability would first be reduced by the sum of the credits provided under the following sections: (1) section 33 (relating to foreign tax credit), (2) section 37 (relating to credit for the elderly), (3) section 38 (relating to investment in certain depreciable property), (4) section 40 (relating to expenses of work incentive programs), (5) section 41 (relating to contributions to candidates for public office), (6) section 42 (relating to general tax credit), (7) section 44 (relating to purchase of new principal residence), (8) section 44A (relating to expenses for household and dependent care services), and (9) section 44B (relating to employment of certain new employees).

sequently, for purposes of this section, the time of payment or accrual of amounts for insulation or other energy-conserving components would not be determinative of when the expenditures for such property have been made.

Qualifying residences

In order to qualify for the credit, installations of insulation or other energy-conserving components must be in or on an individual's principal residence, and that residence must be located in the United States. The credit is available, however, only with respect to residences the construction of which was substantially completed before April 20, 1977. Owners and renters will be eligible for the credit; moreover, an individual who owns stock in a cooperative housing association or who is a member of a condominium management association [2] will be treated as having expended an allocable share of amounts expended by the association for insulation and other energy-conserving components and will be eligible for the maximum $400 credit.

The cooperative stockholder's allocable share of the qualifying expenditures is to be the same as his proportionate share of the cooperative's total outstanding stock. The condominium management association's member's allocable share is to be the amount he is assessed by the association as a result of the energy conservation expenditures.[3]

The determination of whether a dwelling unit is used by a taxpayer as his principal residence will be made under principles similar to those applicable to section 1034 of the Code (relating to a sale or exchange of a principal residence) except that ownership of the dwelling unit will not be required for renters. Moreover, in making this determination, the period for which a dwelling will be treated as a taxpayer's principal residence will include the 30-day period immediately preceding the date the dwelling unit would, under principles similar to those applicable to section 1034, be treated as being used as the taxpayer's principal residence. Thus, installations which are completed within the 30-day period immediately preceding the date the residence would (but for this section) be treated as being used as the taxpayer's principal residence will be eligible for the credit.[4]

Qualifying property

The credit applies to qualifying insulation and other energy-conserving components. The credit is to be allowed also for the original installation of qualifying insulation (or of a qualifying energy-conserving component) in a residence. Therefore, expenditures for such purposes as the reinstallation in the fall of storm windows which had

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[2] For these purposes, the term "condominium management association" means an association meeting the requirements of section 528(c) (1) of the Code, other than subparagraph (E) of that subsection (which requires an election to be taxed under section 528), with respect to a condominium project substantially all of the units of which are used as residences.

[3] In most cases, an individual renting a residence from a member of a condominium management association could not obtain the credit because he would not be assessed for any of the association's expenditures.

[4] It is contemplated that the date when habitation of the dwelling unit by the taxpayer begins will constitute in most cases the date the dwelling would be treated (but for this provision of the bill) as being used as the taxpayer's principal residence.

been taken down in the spring are not to qualify for the credit. Expenditures for installing insulation or other energy-conserving components removed from one structure and placed on the taxpayer's principal residence will also not qualify because of this requirement.

Insulation is defined as any item specifically and primarily designed to reduce, when installed in or on a dwelling (or water heater), the heat loss or gain of the dwelling (or water heater).

Qualifying insulation must be specifically and primarily designed for insulation use. Except for items which qualify as "other energy-conserving components" (such as storm or thermal windows or doors), items which qualify for this credit are to be primarily and specifically designed for use as insulating materials. Materials which are primarily structural or decorative in purpose would not qualify. For example, carpeting, drapes, wood paneling, and exterior siding would not qualify although they may have been designed in part to have an insulating effect. Moreover, the replacement of an existing wall or the addition of a new wall (except for the qualifying insulation installed in the wall) would not qualify for the credit. Attic, floor, and wall insulation made of fiberglass, rock wool, cellulose, or styrofoam are examples of insulating materials qualifying for the credit.

The term "other energy-conserving component" means any item (other than insulation) which is:

(1) a furnace replacement burner designed to achieve a reduction in the amount of fuel consumed as a result of increased combustion efficiency;

(2) a device for modifying flue openings designed to increase the efficiency of operation of the heating system;

(3) an electrical or mechanical furnace ignition system which replaces a gas pilot light;

(4) a storm or thermal window or door for the exterior of the dwelling;

(5) a clock thermostat;

(6) caulking or weatherstripping of an exterior door or window; or

(7) an item of a kind which the Secretary of the Treasury specifies by regulations as increasing the energy efficiency of the dwelling.[5]

Qualifying storm or thermal windows are to include any multi-glazing arrangement whereby a pane of glass is so affixed that it is separated from another pane of glass (or thermal-type window) by air in a space which tends to be enclosed, such as by window sills or other structures containing the glasses.

The Secretary is also authorized to specify items by regulations which would qualify as insulation or as other energy-conserving components. In addition to meeting the definitional requirements set forth in the bill, the determination of whether items qualify should take into account the extent of energy savings and the extent of their use of conventional energy sources.

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[5] In promulgating regulations, the Secretary is to consider, among other things, whether thermostats which employ photoelectric cells, thermostats which are designed to automatically reduce temperatures, and attic fans constitute items of a kind which increase the energy efficiency of a dwelling.

In the case of both insulation and other energy-conserving components, the original use of the property must commence with the taxpayer. Both must also be reasonably expected to remain in operation for at least three years and meet performance and quality standards prescribed by the Secretary (after consultation with the Secretary of Energy, Secretary of Housing and Urban Development and other agencies, such as the National Bureau of Standards). However, these performance and quality standards will not apply to insulation and other energy-conserving components purchased prior to the promulgation of such standards. The committee is concerned with the potential for consumer fraud in the absence of definitive performance and quality standards which are to apply to the insulation and energy-conserving components qualifying for the credit. Thus, it is the committee's desire that the regulations establishing such performance and quality standards be promulgated by the Secretary without unnecessary delay.

Expenditures by joint occupants

If two or more individuals install qualifying property in or on a dwelling jointly occupied by them as their principal residence, the amount of the credit for any calendar year is to be determined by treating all of the joint occupants as one taxpayer. Thus, a total of $2,000 of qualifying expenditures may be made for that residence, rather than $2,000 for each of the occupants. The amount of the credit allowed to each occupant is to be apportioned according to the same ratio as the amount of qualifying expenditures made by that occupant bears to the total amount of qualifying expenditures made by all the occupants.

The fact that a joint occupant may be unable to claim all or a part of his credit because he has insufficient tax liability or because his allowable credit does not equal the $10 minimum credit amount is to have no effect upon the computation of the amount of the allowable credits for the other joint occupants. For example, if each of three joint occupants would otherwise be entitled to a credit for $10 for a particular year, but one of the joint occupants cannot claim his credit because he has no tax liability, the proportion of the expenditures allowable to the other joint occupants would not be affected, and the amounts of their credits would remain the same.

The maximum expenditure amount ($2,000) is to be reduced by the aggregate of prior years' expenditures on the residence by any of the joint occupants, which expenditures were taken into account in computing the credits (all or parts of which were allowed) for such years. This aggregate amount of prior years' expenditures is not broken down and is not applied in the current year to take account in any way of the specific expenditures of the individual occupants in prior years. For example, assume A and B have together made prior years' qualifying expenditures of $1,600 (A has made qualifying expenditures of $1,200 and B has made qualifying expenditures of $400) on their principal and jointly occupied residence. In the current year, each makes qualifying expenditures of $300, for a total of $600 of current expenditures. Of the $400 of expenditures allowable for the credits ($2,000–$1,600), $200 will be allocated to A ($300/$600 x $400)

and $200 will be allocated to B ($300/$600 x $400). The fact that A had previously computed his credit in prior years with respect to $1,200 out of the total $1,600 of expenditures is irrelevant to the apportionment of expenditures made in the current year.

Effect on tax basis of residence

In order to avoid a double tax benefit (allowance of a credit and also a reduced gain on a subsequent sale of the residence), the bill requires that any increase in basis of the residence on account of qualified expenditures for insulation or other energy-conserving components be reduced by the amount of the credit which is allowed with respect to the expenditures. For example, assume a taxpayer made $2,000 of qualified expenditures which would normally increase the tax basis of his home by that amount. Assuming the taxpayer was allowed the maximum credit allowable in this case, $400 (20 percent of the $2,000), the taxpayer's basis in his residence would be increased by only $1,600 (the $2,000 of expenditures minus the $400 allowed credit).

Of course, an owner of a residence would not be entitled to an increase in tax basis with respect to qualifying expenditures of a lessee who uses the residence as his principal residence.

Effective date

The amendments made by this section are to apply to taxable years ending on or after April 20, 1977, for expenditures made on or after that date and before 1983.

Revenue effect

This provision is estimated to reduce receipts by $361 million for fiscal year 1978, $466 million for fiscal year 1979, $546 million for fiscal year 1982, and $486 million for fiscal year 1983.

Energy savings estimate for residential credits

It is estimated that as a result of the committee provisions for residential insulation and solar and wind tax credits, the consumption of natural gas and oil will be reduced by the equivalent of from 250,000 to 310,000 barrels per day in 1985.

2. Residential Solar and Wind Energy Equipment Credit (sec. 2011 of the bill and new sec. 44C of the Code)

Present law

Under present law, no special tax credit or deduction is allowed for solar or wind energy equipment installed in connection with a residence. However, if installations constitute capital improvements to a residence, the amount of the expenditures involved can be added to the taxpayer's basis in the residence for purposes of determining gain or loss on a subsequent sale of that residence.

Reasons for change

Residential use of oil and natural gas energy represents a major portion of the country's total consumption of these fossil fuels. In view of the substantial potential oil and natural gas savings that could result from the use of alternate-energy-source measures for residential purposes, the committee believes that it is appropriate to encourage residential use of solar and wind energy equipment.

At the same time, the committee recognizes that solar and wind energy equipment technology is presently at an early stage of commercialization. In view of this, the committee feels that there is a need to encourage the purchase and installation of this equipment. Thus, the committee decided to provide a credit for a limited numbers of years in order to accelerate the purchase and installation of this equipment and the development of solar and wind energy technology.

The committee recognizes that presently the most practical and least costly method of use of solar energy is with respect to hot water heating. In order to encourage the use of solar energy in this manner, the committee decided to provide a two-tiered credit structure, with the first $1,500 of expenditures (the approximate cost of many solar hot water heating systems) subject to a higher level of credit (30 percent) than the next $8,500 of expenditures (subject to a 20-percent credit).

Presently, as many as twenty-three States provide tax incentives (principally, property tax exemptions) with respect to residential use of solar energy equipment. The committee hopes that the other States and localities will recognize the need to enact laws in the immediate future to exempt from property taxation increases in value resulting from solar and wind energy improvements.

Explanation of provision

Nature, amount, and period of credit

The committee's bill provides a nonrefundable income tax credit for solar and wind energy expenditures for installations in connection with the principal residence of the taxpayer. The credit is 30 percent of the first $1,500 of qualifying expenditures and 20 percent of the next $8,500 of qualifying expenditures. Thus, the maximum credit on the

total qualifying expenditures of $10,000 ($1,500 plus $8,500) is to be $2,150.

In determining the credit, the maximum allowable expenditures (the first $1,500 subject to a 30-percent credit and the next $8,500 subject to a 20-percent credit) are to be reduced by previous expenditures by the taxpayer which were taken into account in computing the solar and wind energy credit (all or any part of which was allowed) for prior taxable years. Thus, if a taxpayer expended $2,000 for solar and wind energy equipment in 1978 and obtained a credit of $550 ($450 of the credit representing 30 percent of $1,500 plus $100 of the credit representing 20 percent of $500), and he expended another $2,000 for solar and wind energy equipment in 1979, his credit for 1979 would be $400, or 20 percent of $2,000.

An individual will be eligible for the maximum credit each time he changes his principal residence. Thus, an individual would be eligible for the maximum credit for qualifying expenditures on his new principal residence, notwithstanding the allowance of the credit for qualifying expenditures on his previous principal residence and notwithstanding the allowance of the credit to a prior owner of the individual's new principal residence.

The entire cost of a solar or wind energy property is allowed toward the credit only if at least 80 percent of the use of the property is for personal residential purposes. If less than 80 percent of its use is for personal residential purposes, the amount is reduced proportionately. For example, if a full expenditure of $10,000 is made, but only 50 percent of the use of the property is for personal residential purposes (the other 50 percent of use being for business purposes), the allowed credit will be only $1,150 (the allowable credit on $5,000, which is 50 percent of $10,000). For purposes of this provision, use for a swimming pool is not to be treated as personal residential use.

In order to avoid undue administrative burdens due to de minimis claims, a minimum credit amount of $10 for any taxable year is required with respect to any tax return (joint or separate) if any credit is to be allowed. This minimum credit requirement applies to the aggregate of the credits claimed for a taxable year for solar and wind energy expenditures and for insulation and other energy-conserving component expenditures.

The credit is to be available for expenditures made on or after April 20, 1977, and before January 1, 1983.

When qualified expenditures are treated as made

Generally, solar and wind energy property expenditures are to be treated as made when the original installation of the property is completed. Consequently, for purposes of this section, the time of payment or accrual of amounts for solar and wind energy property would not be determinative of when the expenditures for such property have been made.

However, in the case of solar and wind energy expenditures in connection with the construction or reconstruction [1] of a dwelling, the expenditures are to be treated as made when the taxpayer commences

[1] The term "reconstruction" contemplates the destruction and replacement of most of a dwelling's major structures (i.e., floors, walls, ceilings).

original use of the dwelling as his principal residence. Reoccupation by a taxpayer of a reconstructed dwelling, which he occupied as his principal residence prior to reconstruction, would not constitute the commencing of the original use of the dwelling as his principal residence. In this situation, the general rule stated above, i.e., time when original installation is completed, is to apply in determining when the solar or wind energy property expenditure was made.[2]

Qualifying residences

In order to qualify for the credit, installations of solar and wind energy equipment must be in connection with an individual's principal residence, and that residence must be located in the United States. The credit is available for existing and newly constructed and reconstructed dwellings. Owners and renters will be eligible for the credit; moreover, an individual who owns stock in a cooperative housing association or who is a member of a condominium management association [3] will be treated as having expended an allocable share of amounts expended by the association for solar and wind energy property and will be eligible for the maximum $2,150 credit.

The cooperative stockholder's allocable share of the qualifying expenditures is to be the same as his proportionate share of the cooperative's total outstanding stock. The condominium management association's member's allocable share is to be the amount he is assessed by the association as a result of the solar or wind energy expenditures.[4]

The determination of whether a dwelling unit is used by a taxpayer as his principal residence will be made under principles similar to those applicable to section 1034 of the Code (relating to sale or exchange of a principal residence) except that, in relation to renters, ownership of the dwelling unit will not be required. Moreover, in making this determination, the period for which a dwelling will be treated as a taxpayer's principal residence will include the 30-day period preceding the date the dwelling unit would, under principles similar to those applicable to section 1034, be treated as being used as the taxpayer's principal residence. Thus, installations which are completed within the 30-day period preceding the date the residence would (but for this section) be treated as being used as the taxpayer's principal residence will be eligible for the credit.[5]

Qualifying property

The credit for solar energy property applies to solar equipment (and parts solely related to the functioning of such equipment) which,

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[2] It is contemplated that during the period of reconstruction, when the taxpayer must temporarily reside in another dwelling, the reconstructed dwelling would continue to be treated as (assuming it originally was) the taxpayer's principal residence.

[3] For these purposes, the term "condominium management association" means an association meeting the requirements of section 528(c)(1) of the Code, other than subparagraph (E) of that subsection (which requires an election to be taxed under section 528), with respect to a condominium project substantially all of the units of which are used as residences.

[4] In most cases, an individual renting a residence from a member of a condominium management association could not obtain the credit because he would not be assessed for any of the association's expenditures.

[5] It is contemplated that the date habitation of the dwelling unit by the taxpayer begins would constitute in most cases the date such unit would be treated as being used as the taxpayer's principal residence.

when installed in connection with a dwelling, uses solar energy to heat or cool the dwelling or to provide hot water for use within the dwelling. Generally, a solar energy equipment system involves the transformation of sunlight into heat or electricity through the use of such components as collectors (to absorb sunlight and create hot air), rockbeds (to store hot air), thermostats (to activate fans which circulate the hot air) and heat exchangers (to utilize the hot air to create hot water). The credit for wind energy property applies to wind energy equipment (and parts solely related to the functioning of such equipment) which, when installed in connection with a dwelling, uses wind energy to produce energy (in any form) for personal residential purposes. Generally, wind energy equipment involves a windmill which uses wind to generate electricity and other mechanical forms of energy.

Solar and wind energy property need only be installed in connection with a dwelling, rather than in or on it. Thus, a "collector" (which absorbs sunlight) forming part of a solar energy system need not be installed on the roof or any structure of a house in order to qualify for the credit. Furthermore, qualifying property could include a windmill or solar collector jointly owned by a number of families living in separate residential structures.

Solar and wind energy property does not include conventional heating or cooling systems which serve to supplement ("back up") the solar or wind energy equipment in heating or cooling the residence. Solar and wind energy property also does not include expenditures for a swimming pool used as an energy storage medium or any other energy storage medium which serves a dual purpose.

In the case of both solar and wind energy property, the original use of the property must commence with the taxpayer. Both solar and wind energy property must also be reasonably expected to remain in operation for at least five years and meet performance and quality standards prescribed by the Secretary of the Treasury (after consultation with the Secretary of Energy, Secretary of Housing and Urban Development and other agencies, such as the National Bureau of Standards). However, these performance and quality standards will not apply to equipment purchased prior to the promulgation of such standards. The committee is concerned with the potential for consumer fraud in the absence of definitive performance and quality standards which are to apply to the equipment qualifying for the credit. Thus, it is the committee's desire that the regulations establishing such performance and quality standards be promulgated by the Secretary without unnecessary delay.

The Secretary is also authorized to specify equipment qualifying as solar and wind energy property (in addition to those relating to performance and quality standards).

Purchasers of newly constructed or reconstructed homes in connection with which solar or wind energy equipment has been installed are eligible for the credit with respect to expenditures for both the equipment itself and for the labor costs attributable to the onsite preparation, assembly, and installation of such equipment. These costs are to include direct labor costs and indirect labor costs (such as the cost of construction supervisory personnel properly allocable to the onsite preparation, assembly; and installation of the equipment. The

Secretary may require the taxpaper to supply a certification by the builder or contractor as to cost of the equipment and the labor costs attributable to the onsite preparation, assembly, and installation of such equipment.

Expenditures by joint occupants

If two or more individuals install qualifying solar or wind energy property in connection with a dwelling used jointly by them as their principal residence, the amount of the credit for any calendar year is to be determined by treating all of the joint occupants as one taxpayer. Thus, a total of $10,000 of qualifying expenditures may be made for that residence, rather than $10,000 by each of the residents. The amount of the credit allowed to each occupant is to be apportioned according to the same ratio as the amount of qualifying expenditures made by that occupant bears to the total amount of qualifying expenditures made by all the occupants.

The fact that a joint occupant may be unable to claim all or a part of his credit because he has insufficient tax liability or because his allowable credit does not equal the $10 minimum credit amount is to have no effect upon the computation of the amount of the allowable credit for the other joint occupants. For example, if each of three joint occupants would otherwise be entitled to a credit of $10 for a particular year, but one of the joint occupants cannot claim his credit because he has no tax liability, the proportion of the expenditures allowable to the other joint occupants would not be affected, and the amounts of their credits would remain the same.

The maximum expenditure amount ($10,000) is to be reduced by the aggregate of prior years' expenditures on the residence by any of the joint occupants, which expenditures were taken into account in computing the credits (all or parts of which were allowed) for such years. This aggregate amount of prior years' expenditures is not broken down and is not applied in the current year to take account in any way of the specific expenditures of the individual occupants in prior years. For example, assume A and B have together made prior year qualifying expenditures of $8,000 (A, $6,000 and B, $2,000) on their principal and jointly occupied residence. In the current year, each makes qualifying expenditures of $1,500, for a total of $3,000. Of the $2,000 of expenditures subject to credits ($10,000 − $8,000), $1,000 will be allocated to A ($1,500/$3,000 × $2,000) and $1,000 will be allocated to B ($1,500/$3,000 × $2,000). The fact that A had previously computed his credit in prior years with respect to $6,000 out of the total $8,000 of expenditures would be irrelevant to the apportionment of expenditures for the current year.

Effect on tax basis of residence

In order to avoid a double tax benefit (allowance of a credit and also a reduced gain on a subsequent sale of the residence), the bill requires that any increase in basis on account of a qualified solar or wind energy expenditure be reduced by the amount of the credit which is allowed with respect to the expenditure. For example, assume a taxpayer made $1,500 of qualified expenditures which would normally increase the tax basis in his home by that amount. Assuming that the

taxpayer was allowed the maximum credit allowable in this case, $450 (30 percent of the $1,500), the taxpayer's basis in his residence would be increased by only $1,050 (the $1,500 of expenditures minus the $450 allowed credit).

Of course, the owner of a residence would not be entitled to an increase in tax basis with respect to qualifying expenditures of a lessee who uses the residence as his principal residence.

Effective date

The amendments made by this section are to apply to taxable years ending on or after April 20, 1977, for expenditures made on or after that date and before 1983.

Revenue effect

These provisions are estimated to reduce receipts by $26 million for fiscal year 1978, $54 million for fiscal year 1979, $87 million for fiscal year 1982, and $111 million for fiscal year 1983.

Energy savings estimate for residential credits

It is estimated that as a result of the committee provisions for residential insulation and solar and wind tax credits, the consumption of natural gas and oil will be reduced by the equivalent of from 250,000 to 310,000 barrels per day in 1985.

B. TRANSPORTATION TAX PROVISIONS

1. Gas Guzzler Tax and Use of Proceeds (secs. 2021 and 2022 of the bill and new sec. 4064 and sec. 4217 of the Code)

Present law

Under the Internal Revenue Code, an excise tax has never been imposed on automobiles or other vehicles for the purpose of encouraging the manufacture of fuel-efficient vehicles.[1]

The Energy Policy and Conservation Act (Public Law 94–163, "EPCA") provides average fuel economy standards and civil penalties for automobile manufacturers who do not meet these standards. The standards are 18 miles per gallon for 1978 model year passenger automobiles, 19 miles per gallon for 1979 model year passenger automobiles, 20 miles per gallon for 1980 model year passenger automobiles, and 27.5 miles per gallon for 1985 model year passenger automobiles.

Pursuant to EPCA, the Secretary of Transportation is to prescribe regulations setting forth average fuel economy standards for passenger automobiles for model years 1981 through 1984.[2] Essentially, passenger automobiles are defined under EPCA as 4-wheeled, fuel-propelled vehicles, manufactured primarily for public street or highway use and designed for the transportation of not more than 10 individuals.

EPCA provides that the fuel economy standards are to apply to passenger automobiles weighing 6,000 pounds or less and requires the Secretary of Transportation to set fuel economy standards for nonpassenger automobiles. Furthermore, the Secretary of Transportation is given the authority to promulgate regulations setting forth those vehicles weighing between 6,000 and 10,000 pounds which also will be subject to prescribed average fuel economy standards (either as passenger automobiles or nonpassenger automobiles). Those vehicles selected by the Secretary of Transportation are to be of the type for which (1) average fuel economy standards would be feasible and (2) either such standards would result in significant energy conservation or such vehicles are determined by the Secretary of Transportation to

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[1] However, until 1971, an ad valorem excise tax was imposed on the manufacturers' sales of automobiles. A 10-percent excise tax is presently imposed on the sale by manufacturers of buses and trucks with gross vehicle weight of over 10,000 lbs., and an 8-percent tax is imposed on the sale by manufacturers of parts and accessories for buses and trucks. In addition, the Code imposes excise taxes based on weight upon tires, inner tubes, and tread rubber (sec. 4071). These excise taxes also apply to imported articles.

[2] The Secretary of Transportation has recently published final regulations in the Federal Register prescribing the following standards: 22 miles per gallon for 1981 model year passenger automobiles, 24 miles per gallon for 1982 model year passenger automobiles, 26 miles per gallon for 1983 model year passenger automobiles, and 27 miles per gallon for 1984 model year passenger automobiles. (42 F.R. 33533, 33552 (June 30, 1977).)

be substantially used for the same purposes as vehicles weighing 6,000 pounds or less.

The penalty for failure to meet the fleetwide standard in any year is $5 per one-tenth of a mile per gallon by which the manufacturer falls short of the standard for that year, multiplied by all the automobiles produced by the manufacturer in that year. The penalty is not deductible for income tax purposes (sec. 162(f)).

Generally, in determining whether a company has met the standard for any year, separate computations are made with respect to passenger automobiles which are domestically manufactured (i.e., 75 percent of the cost being attributable to value added in the U.S. or Canada) and those which are not domestically manufactured. However, for each of the model years 1978 and 1979, one overall computation is made for a manufacturer's domestic and foreign automobiles (instead of the separate computations referred to in the preceding sentence).

Reasons for change

The committee is concerned about the energy consumption in our country's transportation sector. Gasoline consumption comprises a very significant part of the petroleum consumption in the United States, both in absolute terms and as a percentage of total consumption. Approximately 40 percent of the petroleum consumed annually in the United States is in the form of gasoline. The average daily consumption of gasoline in 1976 was 7 million barrels, an increase of 1.2 million barrels per day, or 21 percent, over the level of consumption in 1970. Since automobile usage accounts for about 74 percent of total gasoline consumption, the committee believes that it is imperative to decrease the number of fuel inefficient automobiles.

Although the EPCA system of fleetwide standards and penalties will in all likelihood significantly increase the efficiency of new automobiles, the committee believes that it is necessary to further reduce the production and sale of inefficient automobiles by reducing the demand for such automobiles. While the fleetwide standard discourages the production of inefficient automobiles, many of these automobiles are still being manufactured. As long as a manufacturer meets the average fleetwide standards, he may continue to produce inefficient automobiles without penalty.[3] Also, the consumer demand for less efficient cars (that is, generally, cars with larger engines, substantial weight, and energy consuming options) remains strong.[4] This demand would undoubtedly encourage the future production of inefficient auto-

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[3] Thus, for example, for model year 1977, the Environmental Protection Agency ("EPA") projected in October 1976 that the average fuel economy would be approximately 18.6 miles per gallon ("mpg") on total automobile sales of 11,-500,000. However, for that year it was estimated that 580,000 new cars sold would get less than 14 mpg, 1,420,000 would get more than 14 mpg but less than 16 mpg, and 3,975,000 would get more than 16 but less than 18 mpg.

[4] The strength of the demand for less efficient cars may be illustrated by the changes in estimates of average mileage for all 1977 model cars. The EPA had originally estimated that the average mileage of all 1977 model year cars would be 18.6 mpg. However, it appears that, because more inefficient cars are being purchased than EPA had estimated, the average mileage for all 1977 model cars will be approximately 18 mpg.

mobiles (at least to the extent the manufacturers could still meet the average fleetwide standards).

The committee believes that a strong argument for the gas guzzler tax is that it would dampen demand for inefficient cars, thereby providing the auto manufacturers with a further incentive to produce fewer inefficient cars. It may have a particularly strong impact in the next few years, when manufacturers will still have the latitude to produce a substantial number of inefficient cars because of the relative ease of meeting the fleetwide standards in these years.

While the EPCA penalties, if imposed, would increase the cost of cars, they would do so on a fleetwide basis and there is no requirement that all of the increased cost be passed through to consumers who purchase the inefficient cars. In fact, in order to remain competitive with other manufacturers meeting the fleet average standard, a manufacturer subject to the penalty would probably have to absorb part or all of the penalty and refrain from passing it on to the consumer.[5]

The committee believes that it is important for the tax to be highly visible to indicate to consumers that there is a serious energy problem and that the Congress has taken action to deal with it. When the consumer sees the amount of the gas guzzler tax shown on the car invoice, he will realize he is paying a premium (which, in many cases, is substantial) to purchase an inefficient car. Thus, consumers would be provided with a financial and, perhaps, psychological incentive to purchase more fuel-efficient automobiles.

The committee also feels that if individuals are to be permitted to purchase inefficient cars and detract from the conservation effort made by most others, they should as a matter of equity pay a considerable premium (in the form of a gas guzzler tax) for this privilege.

However, these new rules should not apply to 1978 model year passenger automobiles since the imposition of these taxes represents a substantial change in the tax rules affecting the automobile industry which has already set the design and tooling of 1978 model year automobiles. Also, the committee believes that it is inappropriate to place a tax on (1) vehicles which come close to achieving the EPCA standard for the model year involved, or (2) certain light-duty trucks (since these trucks are frequently used for business purposes and are required to have substantial cargo capacity and pulling power).

Consequently, the bill imposes a gas guzzler tax on the sale by the manufacturer of inefficient 1979 and later model year automobiles, except trucks of certain cargo capacity, in amounts which are generally related to the degree of inefficiency involved.

Revenue from this tax is to be placed in a special "Public Debt Retirement Trust Fund" to emphasize the committee's commitment to fiscal responsibility and determination to reduce the national debt. For this reason, amounts in the trust fund may be used only for the redemption or purchase of public debt instruments of the United States.

[5] To the extent a manufacturer cannot accurately estimate the amount by which he will fail to meet the standard for a year (which is based on actual sales), he will not be able to adjust the prices of cars sold during that year for the precise amount of the penalty attributable to those cars.

Explanation of provisions

Summary

Under the bill, a gas guzzler (or auto inefficiency) tax would apply to the sales by the manufacturer of automobiles having a gross vehicle weight of no more than 6,000 pounds which fall below certain fuel efficiency standards established by the committee.[6] The tax would apply to 1979 and later model year automobiles but would not apply to trucks with a cargo capacity of 1,000 pounds or more. The amount of the tax applicable to an inefficient automobile is provided in separate rate tables (shown below). The amount of the tax would not be included in the basis of the automobile for any purpose (including the computation of depreciation or the investment credit).

The proceeds of the gas guzzler tax would be appropriated to a trust fund to be used for the purpose of reducing the national debt.

Rates of tax

For the 1979 model year automobiles, the gas guzzler tax would range from $339 for an automobile rated between 14 and 15 miles per gallon ("mpg") to $553 for an automobile rated at less than 13 mpg. As the miles-per-gallon efficiency standards increase each year, so will the tax for those cars failing to meet the standards. The mileage standards and applicable taxes for automobiles failing to meet such standards are set forth below.

Schedule of Gas Guzzler Tax, by Model Year

In the case of a 1979 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	$339
At least 13 but less than 14	438
Less than 13	553

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 17	0
At least 16 but less than 17	$249
At least 15 but less than 16	333
At least 14 but less than 15	428
At least 13 but less than 14	538
Less than 13	666

[6] Generally, these standards start from 3 to 5.5 miles below (depending on the year involved) the fleetwide average standards of EPCA. Thus, for model year 1980 automobiles, the lowest miles per gallon efficiency at which no tax would be imposed is 17, whereas the lowest fleetwide miles per gallon average at which no EPCA penalty would be imposed is 20; for 1985 and later model year automobiles, the lowest miles per gallon efficiency at which no tax would be imposed is 23.5, whereas the lowest fleetwide miles per gallon average at which no penalty would be imposed is 27.5.

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 18.5	0
At least 17.5 but less than 18.5	$245
At least 16.5 but less than 17.5	341
At least 15.5 but less than 16.5	458
At least 14.5 but less than 15.5	597
At least 13.5 but less than 14.5	764
At least 12.5 but less than 13.5	968
Less than 12.5	1,216

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 20	0
At least 19 but less than 20	$266
At least 18 but less than 19	369
At least 17 but less than 18	491
At least 16 but less than 17	636
At least 15 but less than 16	809
At least 14 but less than 15	1,015
At least 13 but less than 14	1,264
Less than 13	1,565

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 20.5	0
At least 19.5 but less than 20.5	$345
At least 18.5 but less than 19.5	459
At least 17.5 but less than 18.5	593
At least 16.5 but less than 17.5	751
At least 15.5 but less than 16.5	938
At least 14.5 but less than 15.5	1,161
At least 13.5 but less than 14.5	1,427
At least 12.5 but less than 13.5	1,747
Less than 12.5	2,134

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 22	0
At least 21 but less than 22	$371
At least 20 but less than 21	490
At least 19 but less than 20	631
At least 18 but less than 19	797
At least 17 but less than 18	990
At least 16 but less than 17	1,218
At least 15 but less than 16	1,486
At least 14 but less than 15	1,804
At least 13 but less than 14	2,183
Less than 13	2,638

In the case of a 1985 or later model year automobile:

If the fuel economy of the model type in which the automobile falls is:	*The tax is:*
At least 23.5	0
At least 22.5 but less than 23.5	$397
At least 21.5 but less than 22.5	524
At least 20.5 but less than 21.5	671
At least 19.5 but less than 20.5	843
At least 18.5 but less than 19.5	1,043
At least 17.5 but less than 18.5	1,276
At least 16.5 but less than 17.5	1,550
At least 15.5 but less than 16.5	1,868
At least 14.5 but less than 15.5	2,244
At least 13.5 but less than 14.5	2,688
At least 12.5 but less than 13.5	3,219
Less than 12.5	3,856

Vehicles to which applicable

The gas guzzler tax applies to "automobiles", as that term is defined in the bill. Under the bill, the term automobile means any 4-wheeled vehicle propelled by fuel[7] (1) which is manufactured primarily for use on public streets, roads and highways (except any vehicle operated exclusively on a rail or rails), and (2) which is rated at no more than 6,000 pounds gross vehicle weight.

However, the bill specifically excludes from the definition of automobile (and thus from the tax) any truck designed primarily to carry property if the cargo capacity of the truck is at least 1,000 pounds. For purposes of this exception, the cargo capacity of a truck refers to its capacity to carry property (as distinguished from passengers) when the truck is carrying the number of adult passengers it is normally designed to accommodate. The term truck is not intended to be limited to vehicles with open-bed cargo areas. Thus, if a van or other special purpose vehicle is designed primarily to carry property and its cargo capacity is at least 1,000 pounds, it would not be subject to the gas guzzler tax.

A vehicle which is equipped with 4-wheel drive and other significant features (such as specially designed wheels and suspension for increased road clearance) designed to equip it for off-highway operation will not be considered a vehicle which is manufactured primarily for use on public streets, roads and highways.

Application to imported automobiles

In the case of imported automobiles, the importer is treated as the manufacturer and the tax is imposed upon his sale of the automobile. Also, as in the case of a manufacturer, if the importer uses the vehicle himself rather than selling it, such use is treated as a sale (sec. 4218), and the gas guzzler tax would be imposed upon the commencement

[7] Generally, "fuel" includes gasoline and diesel fuel. However, the Secretary of the Treasury, after consultation with the Secretary of Transportation, may prescribe regulations including any other petroleum or natural gas fuel within the meaning of the term if he determines that the inclusion is consistent with the need of the nation to conserve energy.

of such use. The key to measuring the amount of the gas guzzler tax imposable on an imported automobile (as with any other automobile) is the model year in which it is produced.[8] Also, the fact that an automobile is not new when it is first imported does not prevent the imposition of tax. For example, if during 1982 an individual imports for his personal use a 1979 model year automobile (produced by a foreign manufacturer) which is rated at less than 13 mpg, the individual would be liable for a tax of $553 (the tax on a 1979 model year automobile rated at less than 13 mpg).[9]

Application to leased automobiles.

If a manufacturer leases an automobile, the first lease is treated as a sale, and the gas guzzler tax (if any) is payable by the manufacturer out of each lease payment in the ratio that such lease payment bears to the total amount to be paid under the lease. A second or subsequent lease is not treated as a sale. If such a first lease is canceled, or the automobile is sold or otherwise disposed of before the total gas guzzler tax is payable, the remaining portion of the gas guzzler tax becomes payable when such cancellation, sale, or disposition occurs. On the other hand, if the leased automobile is sold or otherwise disposed of after the total gas guzzler tax is payable, no further gas guzzler tax would be imposed by reason of the sale or disposition.

Determination of fuel efficiency

The gas guzzler tax provided by the committee bill makes specific provision for its own mileage standards and does not tie these standards to any changes which might be made in the fleet standards of EPCA, either by legislation or by changes in the applicable regulations by the Department of Transportation. The testing is to be done by the Environmental Protection Agency ("EPA"), which is to report the results to the Secretary of the Treasury.

Also, in order to insure that testing procedures cannot be varied without consultation of the committee, the bill prescribes specific testing procedures, which are the same procedures that have been employed by the EPA Administrator for the 1975 model year and subsequent model years (weighted 55 percent urban cycle and 45 percent highway cycle), or procedures which yield comparable results. Any change in testing procedure cannot result in any significant loosening or tightening of the stringency of the fuel economy measurements as they relate on an overall basis to a manufacturer's fleet of automobiles. Thus, for any model year in which new test procedures become applica-

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[8] The term "model year" (which is defined in the same manner as it is in EPCA) means, with reference to any specific calendar year, a manufacturer's annual production period (as determined by the Administrator of the Environmental Protection Agency) which includes January 1 of such calendar year. If a manufacturer has no annual production period, the term "model year" means the calendar year.

[9] There is no exception for a manufacturer of a small number of automobiles or for a model type of which only a limited number are imported.

In the case of an imported or domestic automobile for which there are no EPA miles-per-gallon ratings, the EPA shall, at the request of the Secretary of the Treasury, provide a miles-per-gallon determination (by measurements or by estimation based on the ratings for similar vehicles) for such automobile or the class of automobiles which contains such automobile.

ble, either the results of the new test procedures must be comparable to the results using the 1975 test procedures on that model year's cars, or the Secretary must adjust the results from the new test procedures so that they are comparable to the results used in the 1975 test procedures.

Like EPCA, the bill requires that the fuel economy test be conducted in conjunction with the emissions test conducted under section 206 of the Clean Air Act. This coordination of testing is intended to allow the manufacturers to be able to supply the same vehicles for both sets of tests, rather than having to supply separate vehicles for each test. Also, testing and calculation procedures applicable to a model year (except for technical or clerical changes) are required to be promulgated not less than 12 months before the model year to which the procedures apply.

Certain exemptions and refund provisions not available

Under present law, the manufacturer's excise taxes generally do not apply to direct sales or leases to State and local governments or tax-exempt schools if the items purchased or leased are for their exclusive use (sec. 4221(a)(4) and (5)). Also, if a State or local government or tax-exempt school purchases an item subject to the tax from someone other than the manufacturer, the manufacturer may obtain a credit or refund of the tax paid (sec. 6416(b)(2)) if he has repaid or agreed to repay the amount of the tax to the ultimate vendor or obtained the consent of said vendor to the allowance of the credit or refund. In addition, the Secretary of the Treasury has the authority to exempt sales to the United States (sec. 4293) from manufacturers excise taxes, although the Secretary has not exercised this authority extensively.

Under the bill, these exceptions for sales and leases to State and local governments and tax-exempt schools (and the provisions for obtaining a refund if the tax is paid by the manufacturer but not passed on to the government or school) are not to be available in the case of the gas guzzler tax. Also, the Secretary of the Treasury will not have the authority to waive application of the tax in the case of a sale or lease of a vehicle to the United States. These exemptions are not available for the gas guzzler tax because it is felt that governments and tax-exempt schools, like private citizens, should utilize efficient vehicles. Since the gas guzzler tax does not apply to either vehicles designed for offhighway operation, trucks with a cargo capacity of at least 1,000 pounds, or vehicles the gross vehicle weight of which exceeds 6,000 pounds, the cost of providing essential work-related vehicles for agencies such as the Department of Defense would not be increased in most cases by the imposition of the gas guzzler tax.

Reduction in basis of automobiles on which gas guzzler tax was imposed

In general, under present law, a taxpayer's unadjusted basis in property he purchases either for use in his trade or business or for personal use is the cost of the property. This basis is utilized not only in computing depreciation and the investment credit but also, after taking into account any appropriate adjustments, in computing gain or loss on the sale of the property. Since an excise tax imposed upon the sale of a vehicle by a manufacturer reflects an additional cost of the item sold, it would be included in the purchaser's basis for the vehicle.

The committee believes that it is inconsistent with the basic purposes of the gas guzzler tax to allow it to be included in basis for computing depreciation and the investment credit for persons who use automobiles subject to the tax in their trades or businesses. The effect of such allowances would be to reduce the amount of the tax by 10 percent (for the investment credit) plus a precentage equal to the taxpayer's marginal tax rate (for the depreciation deduction). Thus, under the general tax rules, if a taxpayer were in a 50-percent marginal tax bracket, he could reduce his income taxes by 60 percent of the amount of the gas guzzler tax imposable upon a gas guzzling automobile used in a trade or business. Also, it seems inappropriate to allow this tax to increase a taxpayer's basis in an automobile for purpose of computing gain or loss (but not depreciation or the investment credit), since this would result not only in a diminution of the effect of the tax, but also in some additional complexity because two separate bases would have to be computed for any automobile used in a trade or business.

Consequently, the committee's bill provides that, if a taxpayer acquires any automobile with respect to which a gas guzzler tax was imposed and (except in situations where the vehicle is sold for ultimate use prior to importation) the use of the automobile by the taxpayer begins not more than 1 year after the date of the original sale for consumption, then the basis of the automobile shall be reduced by the amount of the gas guzzler tax imposed on the automobile. If an automobile is sold for ultimate use prior to importation, the 1-year period referred to in the preceding sentence begins on the date it is considered to have entered this country for customs purposes. This reduction in the basis is automatic; it does not depend upon the extent to which the manufacturer may or may not have passed the tax on to the purchaser. Rather, the basis is computed simply by reducing the taxpayer's cost basis in the vehicle by the amount of the tax imposed.

The reduction is an across-the-board reduction for all purposes, including depreciation, computation of the investment credit, and computation of gain or loss on sale, and it applies whether the vehicle is used in a taxpayer's trade or business or for personal purposes.

The rule applies not only to the original purchaser of the automobile (or user, in the case where a use is considered a sale), but also to any other person whose use of the automobile begins not more than 1 year after the date of the original sale of the automobile for ultimate use (or, if sale for ultimate use precedes importation, the date the vehicle is considered to have entered this country for customs purposes). This 1-year rule is designed to prevent persons from indirectly obtaining the benefit of an increase in basis for the gas guzzler tax by purchasing (or having someone purchase for them) a relatively new automobile.

Use of proceeds of gas guzzler tax

The bill establishes a trust fund known as the "Public Debt Retirement Trust Fund," and appropriates to this trust fund, out of any money in the Treasury not otherwise appropriated, amounts equivalent to the amount of the gas guzzler tax collected by the Treasury. In general, the amounts appropriated are to be transferred at least monthly from the general fund of the Treasury to this trust fund.

Use of amounts in the trust fund is limited to the payment at maturity, or the redemption or purchase before maturity, of any obligation of the United States included in the public debt. All such obligations paid, redeemed, or purchased with money out of the trust fund are directed to be canceled and retired and shall not be reissued.

Effective date

These provisions shall apply with respect to 1979 and later model year automobiles.

Revenue estimate

It is estimated that the gas guzzler tax will result in an increase in budget receipts of $100 million per year during fiscal years 1979 and 1980, and $170 million in fiscal year 1985.

Energy savings estimates

It is estimated that this provision will save about 10,000 barrels of gasoline per day in 1981, about 40,000 barrels per day in 1982, and about 175,000 barrels per day in 1985.[11]

[11] The estimates are based on an Administration model which assumes that not all manufacturers of automobiles will comply with the standards of EPCA. If it were assumed that, without the application of this bill, all such manufacturers would comply with EPCA, the energy savings in 1985 would be between 40,000 barrels per day and 70,000 barrels per day.

2. Repeal of Personal Deduction for State and Local Taxes on Gasoline (sec. 2023 of the bill and sec. 164 of the Code)

Present law

Under present law, an individual who itemizes his deductions may deduct State and local taxes imposed with respect to gasoline, diesel fuel, and other motor fuels purchased by him. In practice, the amount of this deduction may be computed either from a record of taxes actually imposed with respect to gasoline (or other motor fuels) purchased by the individual or the amount shown in the gasoline tax tables provided by the Internal Revenue Service. These tables are based on a taxpayer's calculation of the mileage driven during the year, the number of cylinders in the car, and the gasoline tax rates in each State.

Reasons for change

The committee believes that, in view of the need to conserve gasoline, the Federal Government should not subsidize nonbusiness use of gasoline (or other motor fuels) through a deduction for State and local motor fuels taxes. Repeal of this deduction is a further signal to consumers that the energy shortage is serious and that the Congress is taking steps to deal with it.

In addition, State and local gasoline taxes, like the nondeductible Federal gasoline tax, are essentially charges for the use of highways. Therefore, the taxes seem more like a personal expense for automobile travel (such as tolls) than a tax. Their deductibility is inconsistent with the user charge character of the tax because deductibility shifts part of the cost from the highway user to the general taxpayer.

The committee also believes that the gasoline tax deduction involves complications out of proportion to any benefit that may be derived. Not only is there much guessing in the gasoline tax calculation, but the amount of tax savings to the average taxpayer is generally small.

Explanation of provision

The bill repeals the deduction for State and local taxes paid by a taxpayer for the purchase of gasoline, diesel fuel, and other motor fuels for nonbusiness use. (The business expense deduction for gasoline, etc., including the tax, still remains available.)

The repeal of this deduction is estimated to result in a tax increase of about $636 million (at 1976 levels) for 18.6 million returns (21 percent of all returns), or an average of about $34 per return. As shown below, less than 34 percent of the tax increase is derived from returns with incomes under $20,000, and only 12 percent of those with incomes below that level will experience a tax increase (because of the extensive use of the standard deduction at these income levels).

RETURNS WITH TAX INCREASE AND AMOUNT OF TAX INCREASE FROM REPEAL OF THE STATE AND LOCAL GASOLINE TAX DEDUCTION, 1976 INCOME LEVELS

Adjusted gross income class	Total returns (thousands)	Returns with tax increase [1] (thousands)	Cumulative percent of returns with tax [2] increase	Returns with increase as percent of total returns within each AGI class	Tax increases: Amount (millions)	Tax increases: Percentage distribution
Under $5,000	25,480	77	0.3	0.3	$1	0.2
$5,000 to $10,000	20,130	1,172	2.7	5.8	18	2.8
$10,000 to $15,000	16,171	3,142	7.1	19.4	70	11.0
$15,000 to $20,000	11,810	4,418	12.0	37.4	125	19.7
$20,000 to $30,000	9,938	6,198	18.0	62.4	234	36.8
$30,000 to $50,000	3,305	2,623	20.3	79.4	130	20.4
$50,000 to $100,000	949	789	21.0	83.1	46	7.2
$100,000 and over	216	179	21.1	82.9	12	1.9
Total	88,000	18,598	21.1	21.1	[3] 636	100.0

[1] It is estimated that 957,000 returns would use the standard deduction (rather than itemize deductions).

[2] This column indicates the percentage of total returns at or below each AGI class with tax increases.

[3] 1976 calendar year liability estimate. However, the estimate takes into account the tax law changes made by the Tax Reduction and Simplification Act of 1977.

Note: Details may not add to totals because of rounding.

Effective date

The repeal of the deduction for State and local motor fuels taxes applies to purchases made after December 31, 1977.

Revenue effect

This provision is estimated to result in an increase in budget receipts of $115 million in fiscal year 1978, $780 million in fiscal year 1979, and $1,383 million in fiscal year 1985.

Energy savings estimate

This provision is not expected to have any significant energy savings impact because it is unlikely that consumers will regard the elimination of the deduction as an increase in the price of gasoline.

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3. Extension of Existing Rate of Tax on Gasoline and Other Motor Fuels (sec. 2024 of the bill and secs. 4041, 4081, 6412 and 6421 of the Code)

Present law

Under present law, a retailers excise tax of 4 cents a gallon is imposed on diesel and other special motor fuels sold for use (or used) in a highway vehicle (sec. 4041).[1] Also, a manufacturers excise tax of 4 cents a gallon is imposed on gasoline sold by the producer or importer (sec. 4081).[2] These taxes are scheduled to be reduced to 1½ cents a gallon on October 1, 1979 (as the Highway Trust Fund—to which the revenues now go—is scheduled to expire as of September 30, 1979).

Reasons for change

The committee believes that, because of the need to conserve energy and reduce gasoline consumption, it would be inappropriate to reduce the price of gasoline on October 1, 1979, by allowing the Federal excise tax on gasoline and other motor fuels to be reduced from 4 cents a gallon to 1½ cents a gallon. Thus, the committee decided to extend the present 4-cents-a-gallon tax rate for 6 years (until October 1, 1985) as a further signal to motorists of the extent of the congressional concern for energy conservation.

Explanation of provision

The bill extends the current 4-cents-a-gallon excise tax on gasoline and other motor fuels for six years, or from September 30, 1979 to September 30, 1985 (after which time, the rate will be 1½ cents a gallon). The bill, however, does not extend the Highway Trust Fund, which is currently scheduled to expire as of September 30, 1979. The committee's bill does not address the question of the specific use of such motor fuel tax revenues after September 30, 1979, except that, until the use is otherwise specified in subsequent legislation, the revenues will go into the general fund of the Treasury.

The committee is aware that the House Committee on Public Works and Transportation will be considering surface transportation authorization legislation during this Congress, and that recommendations will be made regarding the Highway Trust Fund and the present

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[1] The other special motor fuels are benzol, benzene, naphtha, liquified petroleum gas, casinghead and natural gasoline, or any other liquid (other than kerosene, gas oil, fuel oil, gasoline or diesel fuel). (See also discussion below, in section 4, of application of the tax on other special motor fuels in the case of nonhighway use, such as motorboat use.)

[2] Gasoline used for nonhighway purposes or by local transit systems is currently eligible for a refund or credit equal to 2 cents a gallon (sec. 6421). (See also changes made by this bill in the gasoline tax paid by motorboat users and by local transit systems, as well as the tax on other motor fuels used by school buses and local or intercity buses.)

trust fund taxes. The committee also will be giving consideration to these matters later in this Congress, and will decide at that time on the future use of the gasoline and other motor fuels tax revenues.

Effective date

The bill extends the present 4-cents-a-gallon excise taxes on gasoline and other motor fuels from September 30, 1979 through September 30, 1985.

Revenue effect

It is estimated that this provision will increase budget receipts by $3.3 billion in fiscal 1980, $3.4 billion in 1981, and $3.8 billion in fiscal 1985.

Energy savings estimate

This provision will result in a savings of oil consumption of about 28,000 barrels per day in 1980 and about 26,000 barrels per day in 1985.

4. Removal of Refund or Credit for Certain Motorboat Fuel Use (sec. 2025 of the bill, secs. 4041(b) and 6421(a) of the Code and sec. 201(b) of the Land and Water Conservation Fund Act of 1965)

Present law

Under present law, a 4-cents-a-gallon tax is levied on the sale of gasoline by the producer or importer (sec. 4081). However, when the fuel is used in other than a highway vehicle which is registered, or is required to be registered, for highway use, the ultimate purchaser may obtain a refund of 2 cents a gallon on his purchase (sec. 6421) or credit against his income tax (sec. 39). Use of gasoline in a motorboat thus qualifies for the payment of the 2 cents a gallon.

The 4-cents-a-gallon retail tax on special motor fuels (sec. 4041(b))[1] also contains a provision for sale of these fuels at the 2-cent tax rate if the purchaser is to use them in other than a highway vehicle which is registered, or required to be registered, for highway use. If special motor fuels are sold at the 4-cent rate, and used in a manner qualifying for the 2-cent rate, the purchaser is entitled to a 2-cent-a-gallon payment on such use(sec. 6427); the payment is by a refund, or income tax credit, in the same manner as the gasoline tax payment.

Diesel fuel also is taxed at 4 cents a gallon, but the tax does not affect motorboats as the fuel is taxed only when sold for use, or used, in a diesel-powered highway vehicle (sec. 4041(a)).

The net proceeds from the fuel taxes collected from fuel used in motorboats are transferred to the Land and Water Conservation Fuel (after first having been appropriated to the Highway Trust Fund).

Reasons for change

The committee considers it to be in the interest of the national energy conservation policy to treat motorboat fuel use the same as highway fuel use. Thus, the committee believes it appropriate at this time to remove the present 2-cents-a-gallon refund or credit for motorboat use of gasoline and other special motor fuels.

Moreover, since the user tax contribution from motorboats is increased by this provision, the committee concluded that the revenues from the 2-cents-a-gallon increase in the fuels tax should also be transferred to the Land and Water Conservation Fund (as are the revenues rom the present 2-cent-a-gallon tax) to be available for, among other things, the provision of increased funding of water recreational facilities used by motorboats.

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[1] The fuels are benzol, benzene, naphtha, liquefied petroleum gas, casinghead and natural gasoline, and any other liquid fuel (other than kerosene, gas, oil, fuel oil, gasoline, or diesel fuel).

Explanation of provision

The bill removes the current 2-cents-a-gallon reduction in the fuels tax (gasoline and special motor fuels other than diesel fuel) for fuel used in a motorboat. Therefore, the tax on motor fuels used in a motorboat (other than diesel fuel, which remains exempt from tax) will be 4 cents a gallon, the same as for motor fuels used in a highway vehicle.

The additional 2-cents-a-gallon fuels tax on motorboat use will be transferred into the Land and Water Conservation Fund, to be available for expenditure for purposes under that fund.

Effective date

These provisions are effective on and after October 1, 1977.

Revenue effect

It is estimated that the revision in the tax treatment of motorboat fuel will increase budget receipts by $1 million for fiscal year 1978 and by $4 million per year thereafter. These amounts would be transferred to the Land and Water Conservation Fund.

Energy savings estimate

This provision is estimated to result in negligible energy savings.

5. Repeal of Excise Tax on Buses and Bus Parts (secs. 2026 and 2027 of the bill and secs. 4061, 4063, 4221 and 6416(b)(2) of the Code)

Present law

Under present law, a 10-percent manufacturers excise tax is imposed on the sale of buses having a gross vehicle weight of more than 10,000 pounds (sec. 4061(a)).[1] However, present law provides for an exemption from this tax for "local transit buses"; that is, those "which are to be used predominantly by the purchaser in mass transportation service in urban areas" (sec. 4063(a)(6)).[2] The tax also does not apply to school buses sold to any person for "exclusive" use in transporting students and employees of schools operated by State or local governments or by tax-exempt educational organizations (sec. 4221(e)(5)).[3]

Present law also contains an 8-percent manufacturers excise tax on parts and accessories (other than tires and inner tubes, which are taxed separately under sec. 4071) of the type used on buses and trucks (sec. 4061(b)).[4] There are no exemptions from this tax for parts and accessories sold for use on local transit buses or privately-owned school buses.

The revenues from the excise taxes on buses and bus parts go into the Highway Trust Fund (through September 30, 1979).

Reasons for change

The committee considers it desirable to encourage the use of bus transportation because it is a more energy-efficient mode of transportation than use of private automobiles. In addition, the committee believes that the tax distinction between local transit buses and intercity buses (scheduled and charter) should be removed, as both types of bus transportation conserve energy as compared with private auto transportation (upon which there is no manufacturers excise tax for the purchase of either the passenger automobile or the related parts and accessories). Consequently, the committee decided that the excise taxes on buses and bus parts and accessories should be repealed.

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[1] This tax is scheduled to be reduced to 5 percent for sales on or after October 1, 1979.

[2] This exemption applies to privately-owned local transit buses, since "public" transit buses are exempted under the provision exempting State and local governments from manufacturers excise taxes (sec. 4221(a)(4)).

[3] This exemption applies to persons purchasing school buses for contract operation to transport school students or employees; school buses sold directly to State and local governments and to tax-exempt educational organizations for their exclusive use are already exempted under the general manufacturers excise tax exemption provisions for State and local governments (sec. 4221(a)(4)) and for tax-exempt educational organizations (sec. 4221(a)(5)).

[4] This tax is also scheduled to be reduced to 5 percent on October 1, 1979.

Explanation of provision

The committee's bill repeals the 10-percent excise tax on all buses as well as the 8-percent tax on bus parts and accessories.

Tax on buses

With respect to the 10-percent excise tax on buses, floor stocks refunds are provided in the case of tax-paid buses in dealers' inventories as of the day after the date of enactment. Also, consumer refunds are provided in the case of sales made on or after April 20, 1977, and on or before the date of enactment. The floor stocks refunds and consumer refunds are essentially similar to those generally provided on past occasions for repealed excise taxes, such as in the Revenue Act of 1971 (when the manufacturers excise tax was repealed for automobiles and light-duty trucks).

Floor stock refunds.—Floor stocks refunds of the 10-percent tax paid by a manufacturer, producer, or importer are provided for buses held in dealers' inventories as of the day after the date of enactment of this Act if the bus has not been used and is intended for sale. The amount of tax is to be credited or refunded (without interest) to the manufacturer, producer, or importer, if certain conditions are met.

The claim for the credit or refund must be filed with the Secretary of the Treasury before the first day of the 10th calendar month beginning after the day after the date of enactment based upon a request from a dealer submitted to the manufacturer, producer, or importer before the first day of the 7th calendar month beginning after the day after the date of enactment. Further, reimbursement of the tax amount must be made to the dealer by the manufacturer, producer, or importer on or before the first day of the 10th month, or written consent must be obtained from the dealer regarding allowance of the credit or refund. No credit or refund is to be allowed to a manufacturer, producer, or importer without such evidence of the dealer's inventory for which the credit or refund is claimed as may be required under Treasury regulations.

Consumer refunds.—The bill also provides for consumer refunds of the 10-percent tax for bus purchases made on or after April 20, 1977, and on or before the date of enactment. The amount of the tax is to be credited or refunded (without interest) to the manufacturer, producer, or importer: (1) if the taxpayer has evidence of the sale to the ultimate purchaser and of the reimbursement of the tax to the purchaser (as may be required by Treasury regulations); (2) if the claim for the credit or refund is filed before the first day of the 10th calendar month beginning after the day after the date of enactment based upon information supplied from the person who sold the bus before the first day of the 7th calendar month beginning after the day after enactment; and (3) if reimbursement of the tax has been made to the ultimate purchaser on or before the first day of such 10th calendar month.

Other provisions.—Any tax paid by reason of section 4218(a) (relating to use by the manufacturer or importer considered a sale) is to be treated as an overpayment of the tax if the tax

is imposed on or after April 20, 1977. The term "dealer" includes a wholesaler, jobber, distributor, or retailer. A bus is considered as "held by a dealer" if the title has passed to the dealer (whether or not delivery has been made), and if, for purposes of consumption, the title (or possession) has not at any time been transferred to any person other than a dealer.

Tax on bus parts

The bill also repeals the 8-percent manufacturers excise tax on bus parts and accessories. Under regulations prescribed by the Secretary of the Treasury, the parts and accessories tax imposed by section 4061(b) is not to apply to any part or accessory which is "sold for use" by the purchaser on or in connection with a bus. It is contemplated that such parts and accessories would be sold tax-free by the manufacturer, producer, or importer for use on or in connection with a bus only if an appropriate exemption certificate is furnished by the purchaser. If the sale of the parts and accessories is made other than by the manufacturer, producer, or importer, the bill provides for a refund of the 8-percent tax where the part or accessory is "sold for use" by the purchaser on or in connection with a bus. Thus, parts and accessories that may be interchangeable between trucks and buses will continue to be subject to the parts tax if they are not "sold for use" with respect to buses.

There is no provision for floor stocks refunds or consumer refunds with respect to the repeal of the excise tax on bus parts and accessories, because the relatively small amount of tax per unit would not appear to cause a delay in consumer purchases, and because there would be considerable administrative burden in providing and processing such refunds.

Effective date

Tax on buses

The repeal of the 10-percent excise tax on buses is effective for sales by the manufacturer, producer, or importer on or after April 20, 1977. An article is to be considered as sold before April 20, 1977, if possession or right to possession passes to the purchaser before that time.

In the case of partial payments of tax in connection with leases, certain types of installment sales, conditional sales, or certain types of chattel mortgage arrangements, present law (sec. 4216(c)) provides that the manufacturers excise tax is to be paid upon each partial payment and is to be based on the tax rate in effect on the date each partial payment is due. To avoid windfall benefits to a manufacturer where the lease, installment sale, etc., took into account the 10-percent tax, the bill provides that no tax is due on partial payments made on or after April 20, 1977, if the lessor or vendor establishes that the amount of the payments payable on or after that date has been reduced by the amount of tax that would otherwise have been due with each partial payment on or after that date. If the lessor or seller does not establish that the payments have been so reduced, the tax reduction provided by the bill is not to apply to the article on which those partial payments are being made. In other words, for the tax reduction to be available in partial payment cases, the benefit of the repeal must be passed on to the lessee or purchaser.

Tax on bus parts

The repeal of the 8-percent excise tax on bus parts and accessories is effective for sales by the manufacturer, producer, or importer on or after the first day of the first calendar month beginning more than 10 days after the date of enactment.

Revenue effect

Tax on buses

It is estimated that the repeal of the 10-percent excise tax on buses will reduce budget receipts by $13 million for fiscal 1978 (which includes the floor stocks and consumer refunds) and $9 million per year thereafter.

These amounts would otherwise go into the Highway Trust Fund (through September 30, 1979).

Tax on bus parts

The repeal of the 8-percent excise tax on bus parts and accessories is estimated to reduce budget receipts by $3 million for fiscal year 1978 and each year thereafter.

These amounts would otherwise go into the Highway Trust Fund (through September 30, 1979).

Energy savings estimate

These provisions are estimated to result in negligible energy savings.

6. Removal of Excise Tax on Certain Items Used on or in Connection with Intercity, Local, or School Buses (sec. 2028 of the bill and secs. 4071, 4092, 4221(e), 6416(b), 6421(b)(1), 6424 and 6427 of the Code)

Present law

Presently, privately-owned and operated buses are subject to the manufacturers excise taxes on tires, tubes and tread rubber,[1] gasoline,[2] and lubricating oil,[3] as well as the retailers excise tax on diesel fuel and other special motor fuels.[4] Complete exemption is provided from these excise taxes for State and local governments (secs. 4041(g)(2) and 4221(a)(4) and for tax-exempt educational organizations (secs. 4041(g)(4) and 4221(a)(5)). A partial exemption (2-cents-a-gallon refund or credit) is available from the tax on gasoline and other motor fuels for use by a privately-owned local tansit system for the portion of its total fare revenue represented by "commuter fare revenue" (secs. 6421(b) and (d)(2) and 6427(b)).[5]

The revenues from these taxes paid with respect to highway use now go into the Highway Trust Fund (through September 30, 1979).

Reasons for change

Since bus transportation is more energy-efficient than private automobile transportation, the committee believes it desirable to encourage greater use of bus transportation. In addition, the committee considers it appropriate to make the excise tax treatment of private transit and school bus operations consistent with governmental and tax-exempt educational bus operations. Therefore, the committee decided to extend the present exemptions from the taxes on tires, tubes and tread rubber, gasoline and other motor fuels, and lubricating oil to privately-owned intercity and local bus operations and private school bus operations not presently exempt from these taxes.

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[1] A tax of 10 cents a pound on highway tires and inner tubes and of 5 cents a pound on tread rubber for highway use (sec. 4071). (The taxes on highway tires and inner tubes are scheduled to be reduced to 5 cents a pound and 9 cents a pound, respectively, on October 1, 1979, while the tax on tread rubber expires on that date.)

[2] A tax of 4 cents a gallon (sec. 4081).

[3] A tax of 6 cents a gallon (sec. 4091).

[4] A tax of 4 cents a gallon (sec. 4041).

[5] The partial exemption is available only if at least 60 percent of the total passenger fare revenue derived during a calendar quarter from "scheduled common carrier public passenger land transportation service along regular routes" is from "commuter fare revenue." Commuter fare revenue is defined (sec. 6421(d)(2)) as fares derived from transportation of persons and attributable to (1) amounts paid which do not exceed 60 cents, (2) amounts paid for commuting or season tickets for single trips of less than 30 miles, or (3) amounts paid for commuting tickets for one month or less.

Explanation of provisions

The bill removes the excise taxes on highway tires, inner tubes and tread rubber, gasoline and other motor fuels, and lubricating oil for private intercity, local and school bus operations.

In the case of the excise taxes on highway tires, inner tubes and tread rubber, the bill provides an exemption for sales by a manufacturer, producer, or importer of such items "sold for use" by the purchaser on or in connection with an intercity, local, or school bus. It is contemplated that such tires, tubes and tread rubber would be sold tax-free only if an appropriate exemption certificate is furnished by the purchaser. Where the sale of such items is made other than by the manufacturer, producer, or importer, the bill provides for a refund (or credit) of the tax when the item is "sold for use" by the purchaser on or in connection with an intercity, local, or school bus.

An "intercity or local bus" means any bus which is used predominantly in furnishing (for compensation) passenger land transportation available to the general public if either (1) the transportation is scheduled and along regular routes, or (2) the passenger seating capacity of the bus is at least 20 adults (not including the driver).[6] Thus, under the first alternative portion of this definition, a bus which is used predominantly (that is, more than 50 percent) in providing (for compensation) scheduled transportation along regular routes (such as is provided by local transit systems or an intercity bus operation providing regularly scheduled service along regular routes) will qualify for the exemption from the taxes on tires, tubes, and tread rubber, regardless of the size of the bus involved. For nonscheduled (i.e., charter) operations (covered by the second alternative portion of the definition), the exemption is available only if the bus has a passenger seating capacity of at least 20 adults (not including the driver) and the transportation is available to the general public. The purpose of the "at least 20 passenger" requirement is to insure that, in situations where regularly scheduled service is not being furnished, vans and similar vehicles used for vanpooling or taxi service are not eligible for the exemption from these taxes (and the fuels taxes).

Charter service is to be considered "available to the general public" if the taxpayer offers such service to more than a limited number of persons or organizations. For example, if a bus operator normally provides charter operations through travel agencies, but his buses are available for chartering by the general public, the buses predominantly used in providing such service would be considered "intercity or local buses." However, if the bus operator is engaged in providing charter services to only one person, group, or organization, or a limited number of persons, with respect to a particular bus, such a bus would not qualify as an "intercity or local bus." The purpose of this limitation is to provide these exemptions only for buses which are used in a passenger transportation business available to the general public (for compensa-

[6] The type of use which would qualify as "use in passenger land transportation available to the general public" includes not only mileage travelled with passengers (which otherwise meets the use qualification), but also use which is incident to such passenger transportation (such as "deadheading").

tion) and not to buses used primarily as part of a nontransportation business or for the personal use of the operator, one family, one group, or organization, or contract use with a limited number of persons.

A "school bus" means any bus with respect to which "substantially all" (that is, at least 85 percent) of the use involves transporting students and employees of schools. If, in connection with the transportation of students or employees of schools, a bus is driven without passengers to or from a point to or from which students or employees of schools are transported (that is, so-called "deadheading"), this use shall be considered as a use which involves transporting students or employees of schools. A school is any educational organization which normally maintains a regular faculty and curriculum and normally has a regularly enrolled body of students in attendance at the place where the educational activities are regularly conducted. Thus, the exemption from these taxes applies to use by both tax-exempt and taxable schools. Also, it applies to a private contractor who operates a bus for tax-exempt or taxable schools.

The bill provides for the refund or credit of the taxes paid with respect to lubricating oil used in an intercity, local, or school bus. If the bus meets the "predominant use" or "substantially all the use" test, the tax on all the lubricating oil used in the bus is to be credited or refunded.

In addition, the bill provides for the refund or credit of the taxes paid on gasoline and other motor fuels but only to the extent these fuels are used in a bus engaged in furnishing (for compensation) passenger land transportation available to the general public or in school bus transportation operations. The allocation of fuel to these nontaxable uses may be determined on a mileage basis (for the same or comparable vehicles) or on an actual fuel use basis. Use in "passenger land transportation available to the general public" means the same type of use that would qualify in meeting the predominant use test for intercity or local buses, and use in schoool bus transportation operations means the same type of use that would qualify in meeting the "substantially all the use" test for school buses.

Effective date

These provisions are effective on the first day of the first calendar month which begins more than 10 days after the date of enactment of this Act.

Revenue effect

These provisions are estimated to reduce budget receipts by $13 million for fiscal year 1978 and each year thereafter. These revenues would otherwise go into the Highway Trust Fund (through September 30, 1979).

Energy savings estimate

It is estimated that the energy savings as a result of these provisions will be negligible.

7. Tax Credit for Electric Motor Vehicles (sec. 2029 of the bill and new sec. 44D of the Code)

Present law

Under present law, there is no special income tax credit available with respect to the purchase of an electric motor vehicle,[1] and there also is no other special tax incentive to aid in the development of electric motor vehicles.

Reasons for change

The committee believes that the development of electric motor vehicles should be encouraged as part of the overall program to reduce the use of petroleum. Presently, electric motor vehicles are characterized by very limited range and speed, in large part, because of the weight and storage capacity of their batteries. To assist in developing a larger market which would contribute to an improvement in the present level of performance of electric motor vehicles, the committee concluded that a tax credit for the purchase of these vehicles would be appropriate. Greater use of electric motor vehicles (principally as a second car for local trips) should reduce petroleum consumption as well as noise and air pollution. Since the batteries of these vehicles will generally be recharged during nonpeak load periods for local utilities companies, there may be some energy savings compared to the use of petroleum, without requiring any additional capital investment. In addition, since most electricity is now generated by the use of coal, there will be a substitution of the use of coal for petroleum to the extent that this part of the automobile sector is increased.

Explanation of provision

The bill provides a nonrefundable tax credit for individuals for 100 percent of the cost of a qualified electric motor vehicle, up to a maximum credit of $300.[2] This credit is available only if the individual acquires the qualified electric motor vehicle exclusively for his personal use or the personal use of a member of his family.[3] A qualified

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[1] A purchaser of an electric motor vehicle who uses the vehicle in his trade or business would, of course, be able to claim the investment credit and depreciation in the same manner as for other tangible personal property.

[2] In the case of joint acquisition by 2 or more individuals, the total credit available is not to exceed $300, and is to be allocated among the purchasers in proportion to their respective shares of the cost.

[3] Since the investment credit and accelerated depreciation are available for electric motor vehicles purchased for business purposes, the committee believes that no additional incentive is appropriate for vehicles purchased for business purposes.

If an individual is eligible to claim the investment credit with respect to any portion of the cost of an electric motor vehicle (because the vehicle is used in part for business purposes), the individual cannot claim any portion of the new credit for qualified electric motor vehicles.

electric motor vehicle is a 4-wheeled vehicle manufactured primarily for use on public roads and powered by an electric motor which obtains current from rechargeable storage batteries or other portable sources of electric current. The original use of the vehicle must begin with the taxpayer or his family, i.e., the credit is not available for used electric cars or cars converted to electricity.

Effective date

The credit applies to qualified electric motor vehicles acquired on or after April 20, 1977, and before January 1, 1983.

Revenue effect

This provision is estimated to reduce budget receipts by less than $500,000 in each of the fiscal years 1978 and 1979, by $1 million in fiscal years 1980 and 1981, by $2 million in fiscal year 1982 and by $4 million in fiscal year 1983.

Energy savings estimate

The energy savings under this provision are estimated to be negligible.

Energy savings estimates for transportation provisions

It is estimated, that as a result of the tax on inefficient automobiles and other transportation tax provisions, the reduction in the consumption of gasoline will be in the range of 160,000 to 240,000 barrels per day in 1985.

C. CRUDE OIL AND NATURAL GAS LIQUIDS EQUALIZATION TAXES AND REBATE

(secs. 2031–2040 of the bill and secs. 4986–8, 44E and 6429 of the Code)

Present law

Under present law, the price of domestically produced crude oil is regulated by the FEA in accordance with the "Emergency Petroleum Allocation Act of 1973," as amended. Under these rules, all domestic oil production other than stripper oil (oil produced from properties where the average daily production per well is 10 barrels or less) is subject to first sale price controls. The exact nature of the price controls is determined administratively, but there is a legislatively mandated limit on the average price of the nonstripper oil. Currently, the average price limit is $8.71 per barrel. This is subject to an inflation adjustment which may not exceed 10 percent a year. Price increases in excess of this authority may be recommended by the FEA, but these increases are subject to a veto by either House of Congress within 15 legislative days. Under present law, these controls are mandatory through May 31, 1979, and the President has discretionary authority to continue controls until September 30, 1981.

Under the existing regulations, "old oil" (also known as "first tier oil" or "lower tier oil") is the amount of oil produced on a property up to either 1972 production of all oil or 1975 production of old oil, whichever is less, adjusted for part of the natural decline in production that occurs in any oil field. "New oil" (also known as "second tier oil" or "upper tier oil") is oil produced on a property in excess of this amount. Old oil presently is controlled at a first sale price which averaged $5.16 per barrel in April 1977, and new oil presently is controlled at a price which averaged $10.97 a barrel in April 1977. (The price of any particular barrel of oil may vary by several dollars from these averages depending on the quality of the oil and its location.) The price of stripper oil averaged $13.29 per barrel in April 1977.

Under the present law, there is an entitlements program which is designed generally to equalize the cost of crude oil to refineries in the United States, regardless of their actual mix of price-controlled and uncontrolled oil. Those U.S. refineries using more than the national average percentages of price-controlled crude oil must buy entitlements from refineries using less than the national average. This purchase and sale of entitlements among refiners offsets the advantages which would otherwise result for the refiners who have access to a disproportionate amount of price-controlled crude oil. The FEA sets the price of entitlements each month based on price differences between old, new and imported oil. Small refiners receive advantages under the entitlements program.

Price controls are also imposed on certain natural gas liquids, including propane, butane and natural gasoline. The price of these liquids is currently controlled at each level of sale (wholesale and retail). The controlled price of the liquids is different for every seller because it depends on several variables, the most important of which is permissible cost passthroughs for the seller.

Reasons for change

The present system of price controls on the sale of domestically produced crude oil has given rise to a number of problems. First, the lower prices of petroleum products that are produced from the controlled crude oil have fostered higher consumption of these products than would occur if U.S. crude oil prices to consumers were the same as world prices. As a result, the United States has had to import more crude oil than it otherwise would, thereby increasing our dependence on foreign suppliers. Moreover, the existence of crude oil controlled at prices lower than the market price has required the creation of a complex system of regulations, including the entitlements program. These regulations are the source of considerable complexity, inequity and inefficiency.

For these reasons, the committee believes that the price to consumers of U.S. crude oil should be increased to the world price.

However, the committee believes that it would be unfair for producers to obtain a windfall profit by being able to charge the full world price for crude oil produced from known reserves. In addition, the committee believes that the increase in the price of crude oil to U.S. consumers to the world price should be phased in over a three-year period to prevent serious economic disruptions.

Under the committee bill, an excise tax is imposed on the first purchase of domestically produced crude oil. In order to permit a gradual increase in the price to consumers of this oil to the world price, the excise tax is imposed in three stages. In 1978, the tax is imposed on lower tier oil and equals $3.50 per barrel. In 1979, the tax is also imposed only on lower tier oil and increases the price to consumers of lower tier oil to the price of upper tier oil. In 1980 and thereafter, the tax increases the price to consumers of all domestically produced oil to world prices. A similar equalization tax is imposed on natural gas liquids except those which are sold for farm and residential purposes or for use in a hospital, church or school.

In addition, the committee's bill provides a rebate of the equalization tax to consumers. The equalization taxes will raise substantial revenues, beginning in 1978. Most economic forecasts, including both those of the Administration and the Congressional Budget Office, are that the economy will be operating well below its potential levels of production and employment in 1978, in which case a large tax increase would create additional unemployment. To prevent this damage to the economy, the committee's bill returns to individuals and to certain institutions the full amount of the net revenues raised by the equalization taxes in 1978.

In deciding how to provide for this return of the equalization taxes, the committee was concerned about two problems. First, people with relatively low incomes tend to spend a larger fraction of their income on oil and products produced using oil than do higher income people;

therefore, by themselves, the crude oil equalization taxes would be regressive. Second, some individuals and institutions are dependent on fuel oil or natural gas liquids for heating, and the committee felt that these persons should not be faced with a price increase as a result of the equalization taxes.

In response to these two problems, the committee's bill provides two rebates of the equalization taxes. First, there is a heating oil rebate which returns the full amount of the tax on heating oil to residences, churches, schools and hospitals. Second, the remaining net revenues from the tax are to be returned to individuals through a system of per-adult tax credits and special payments.

The heating oil rebate is to apply for the life of the tax. However, the tax credits and special payments will apply only to 1978. The committee intends that the revenues raised by the equalization taxes in subsequent years be returned to the economy as well, but it seemed desirable to preserve flexibility on the precise way in which this return is to be accomplished, pending the committee's consideration of tax reform later in this Congress.

Explanation of provisions

A. Crude Oil Equalization Tax

1. Imposition of tax

The bill imposes an excise tax on the first purchaser of domestically produced crude oil. The tax is imposed in three stages and is designed to increase the price to consumers of this crude oil to the world price by 1980. The tax expires on September 30, 1981, (the "termination date"), when the existing price controls on crude oil are scheduled to expire, if the President exercises his full authority to extend those controls.

2. Oil subject to tax

The crude oil equalization tax is imposed on all domestically produced crude oil subject to price controls. "Crude oil" is defined to mean a mixture of hydrocarbons which existed in liquid phase in underground reservoirs and remains liquid at atmospheric pressure after passing through surface separating facilities. The term also includes condensate recovered in associated or nonassociated production by mechanical separators located at any point at or before the inlet side of a gas processing plant. This definition is substantially the same as the definition of "crude oil" provided by present price control regulations.

The crude oil equalization tax only applies to crude oil produced in the United States. For this purpose, the United States includes Puerto Rico, all U.S. possessions and the continental shelf.

In order not to tax oil used to increase production of other crude oil or natural gas, the bill provides an exemption from the tax for crude oil which is used by the producer to extract other crude oil or natural gas. In addition, this exemption to the tax applies to crude oil that is transferred to a refiner to the extent the producer receives in return refined products (including residual oil) which are then used on the lease for the extraction of crude oil or natural gas. In order to qualify for the exemption, the producer must keep accurate records of the amount of refined products that are used to produce

the crude oil and natural gas from each refiner to which crude oil is transferred. The committee intends that the Secretary issue regulations under which crude oil or refined products used in the extraction of oil and gas are to be allocated *pro rata* between the producer's old, new, new new and stripper oil.

3. Rate of tax

The crude oil equalization tax is imposed in three stages. In 1978, the tax is imposed only on lower tier oil [1] and is equal to $3.50 per barrel. In 1979, the tax is also imposed only on lower tier oil and is equal to the difference, computed monthly, between the national average refiner acquisition cost of upper tier oil for the month and the national average refiner acquisition cost for that month of lower tier oil. The effect of this second stage of tax will be to increase the national average cost of lower tier oil to the national average cost of upper tier oil. Prior to the start of 1979, the Secretary of the Treasury is to publish estimates of the tax rates to be applicable during each of the 12 months of 1979.

In 1980 and until the termination date, the tax is levied upon all controlled oil and is equal to the excess of the uncontrolled price of crude oil of a particular classification over the controlled price of that same classification of crude oil. The uncontrolled and controlled prices of crude oil are the prices at the wellhead and, thus, do not include the cost of transporting the oil from the field to the refinery.

The effect of this rate of tax will be to increase the price of controlled oil to consumers up to the world price for that oil; consequently, it should be possible to terminate the entitlements program after 1979. (However, if the President exercises his authority to suspend increases in the tax, as discussed below, it may be necessary to reinstate the entitlements program.)

The present entitlements program provides special subsidies for small refiners (i.e., those who refine fewer than 175,000 barrels per day). The effect of increasing the price of all domestic crude oil to the world price and removing the entitlements program would be to eliminate this subsidy. The bill provides that the Secretary of Energy is to make a study of the effect of the crude oil equalization tax on small and independent refiners and to submit it to Congress, with his conclusions and recommendations for legislation, within 90 days after the enactment of this bill. The entitlements program is not within the jurisdiction of the committee; nevertheless, the committee hopes that the Administration and the committees with jurisdiction over the program will evaluate possible hardships on small refiners during this 90-day period and consider whatever action may be necessary.

The Secretary of the Treasury is authorized to establish various classifications of crude oil by type, grade, and location. The approach of setting a separate rate of tax for various classifications of oil is

[1] The bill contemplates that something close to the present system of price controls will remain in effect until the termination date, i.e., there will be at least two tiers of price controlled crude oil, one called "lower tier" and the other called "upper tier."

designed to prevent the crude oil equalization tax from forcing a decrease in the price that the producer can charge for a particular classification of oil and to prevent windfall gains by refiners.

For example, assume that U.S. oil production consists equally of two grades of oil. Grade A oil is controlled at $4 per barrel, and Grade B is controlled at $6 per barrel. Also, assume that the uncontrolled prices of Grade A and Grade B oil are $11 and $15 per barrel, respectively. Under these circumstances, the third stage crude oil tax would be equal to $8 per barrel (i.e., an average uncontrolled price of $13 minus the average controlled price of $5). In such a case, the maximum amount refiners would be willing to pay for Grade A oil would be $3, i.e., the $11 uncontrolled price minus the tax of $8. Producers of Grade A oil, therefore, would experience a hardship from the tax. Also, refiners who purchased price-controlled Grade B oil at $6 would receive a windfall profit of $1 because their total cost for the oil (the $6 controlled price plus the $8 tax) would be less than its market value of $15.

In order to prevent such situations, the bill provides for different rates of tax for each separate classification of crude oil. Thus, in the example above, the tax on Grade A oil would be equal to $7 (the uncontrolled price of $11 minus the controlled price of $4). The tax on Grade B oil would be equal to $9 (the uncontrolled price of $15 minus the controlled price of $6).

Under the bill, the Secretary of the Treasury is required to establish as many different classifications of crude oil by grade, type and location as are necessary to prevent undue hardships or benefits. The committee intends that the Secretary have considerable latitude in setting up these classifications and that he take into account not only the hardships and benefits referred to above but also the desirability of making the tax as easy to administer as possible.

In addition, the Secretary of the Treasury, after consultation with the Secretary of Energy, is to determine, for purposes of the tax, the uncontrolled price of each classification of crude oil. That price is to be determined on the basis of the best available information. Generally, the best available information will be the price of oil from stripper wells in the same field. However, if the Secretary determines that the price of stripper oil is not representative of what the uncontrolled price of oil of a particular classification would be in a competitive market, if there is insufficient stripper production or if the stripper price is deemed unrepresentative of what the price of nonstripper oil would be without price controls, he is to determine the uncontrolled price from other available information. For example, it may be that only one oil refiner generally buys oil from a particular field and, because of its market power, is able to force down the price of stripper oil. In such a case, the Secretary would not use the stripper oil price as the uncontrolled price but instead would impute an uncontrolled price based on prices of oil of similar type in other, more competitive markets.

Determinations of the uncontrolled price of each classification of oil are to be made not less often than quarterly. However, where there have been relatively large changes in the uncontrolled price of a particular classification of oil during a quarter, it is expected that the

Secretary will make more frequent determinations of the uncontrolled price.

Rules applicable to "new new oil."—Under the committee bill, there is a special rate of tax for "new new oil." The tax on new new oil of a particular classification, as defined in the bill, cannot exceed the difference between the uncontrolled price for that classification of oil and the highest price permitted under price control regulations for that classification of oil, regardless of whether the price of that oil is, in fact, controlled at a lower price. In other words, the committee intends that new new oil, as defined in the committee bill, be taxed at the lowest applicable rate even if that oil is controlled at a price which would otherwise qualify it for a higher tax rate. (In cases in which the price ceiling for the most favorably treated price controlled oil is high enough that this oil is selling below its ceiling price, the tax rate on new new oil, as defined in the bill, will be zero.)

The bill contemplates the creation of a new tier of price controlled oil in addition to the present two tiers for lower and upper tier oil. The Administration has indicated that it intends to create such a third tier of controlled crude oil for "new new oil," which would be controlled at the current world price, adjusted for inflation. Under the Administration proposal, "new new oil" is oil from a well that is more than two and one-half miles from an onshore well in existence on April 20, 1977, or more than a thousand feet deeper than any well within the two and one-half mile radius, as well as oil from an offshore lease entered into after April 20, 1977.

Under the committee bill, "new new oil" is defined to mean oil produced from a property which did not have any commercial production at any time during the 90-day period ending on April 20, 1977. The term "property" means the right, arising from a lease or from a fee interest, to produce crude oil. For this purpose, a producer may treat as a separate property each separate and distinct producing reservoir subject to the same right to produce crude oil, if such reservoir is recognized by the appropriate governmental regulatory authority as a producing formation which is separate and distinct from, and not in communication with, any other producing formation. This is the identical definition of "property" that is presently contained in the price control regulations of the Federal Energy Administration.

4. The taxable event

Under the bill, the tax is imposed on the first purchaser of crude oil. In general, the first purchase occurs upon the first transfer for value of that crude oil. Where the crude oil is refined, exported or otherwise used prior to sale, the first purchase is deemed to occur at the time the crude oil is removed from the lease.[2] These are the points at which first sale price controls are applied.

[2] If the first purchase or use occurs after removal from the lease, it will be necessary to measure the amount of evaporation and other loss which has occurred subsequent to removal from the lease, for the tax applies to the crude oil which has evaporated or has otherwise been lost after removal from the lease and before its first purchase or use. It is contemplated that the Secretary will develop uniform rates of evaporation similar to the procedure under section 5008(c)(3) of the Code as a means of determining the amount of tax attributable to evaporation.

The crude oil tax is never imposed twice with respect to the same oil. Once the tax has been imposed, the taxed oil is not later subject to tax as crude oil when purchased, used, or exported. For example, if crude oil is exported and then subsequently purchased for the first time, the tax is imposed upon the export but not again at its subsequent purchase.

5. Liability for and collection of the tax

Under the bill, the first purchaser generally is liable for the crude oil equalization tax. However, where the tax is imposed upon the export of crude oil, the exporter is liable for the tax. Where the crude oil is used prior to purchase, the user is liable for the tax.

Generally, the first purchaser is required to pay the crude oil equalization tax on or before the first day of the fourth calendar month following the month of the first purchase. The purpose of this delay is to prevent hardship on the first purchaser by giving him a chance to pass the tax along to his customers before he is required to pay the Government.

However, the committee was concerned that attempts may be made to avoid the crude oil equalization tax through the purchase of the crude oil by a nonresident alien not doing business within the United States or by some other person who does not have sufficient assets within the United States with which to pay the tax. In these cases (or other situations prescribed in regulations where there is a substantial likelihood that the tax will not be paid by the first purchaser), the bill permits the Secretary to issue regulations providing that subsequent purchasers would be liable for the collection of the tax. It is contemplated that, in such cases, subsequent purchasers will make arrangements ensuring that the tax is paid by the first purchaser prior to payment for the crude oil.

6. Impact on domestic refiners

The committee understands that the crude oil equalization tax and other taxes in this bill may adversely affect the U.S. oil refining industry, whose existence is essential to national security. The Committee requests that the Administration, using existing authority, take appropriate administrative action if these taxes, together with import license fees and tariffs on crude oil and petroleum products and other costs of U.S. laws and regulations (including the tax treatment of foreign refineries) result in the domestic refining industry's being at a competitive disadvantage in relation to foreign refiners.

7. Effect of tax on natural gas contracts

There are cases in which natural gas prices are set in contracts based on the price of crude oil. The bill provides that the increase in crude oil prices resulting from this tax not be taken into account in the determination or redetermination of natural gas prices under such contracts entered into prior to the date of enactment.

B. Natural Gas Liquids Equalization Tax

1. Imposition of tax

The bill imposes an excise tax on the sale for end use of natural gas liquids and natural gas liquid products. The tax is imposed in three

stages and is designed to increase the price to consumers of these liquids to the price of distillate fuel oil by 1980. The tax on these liquids expires on September 30, 1981.

2. Liquids subject to tax

The tax is imposed only on natural gas liquids and products of natural gas liquids subject to price controls on sales to end users. "Natural gas liquids" are mixed hydrocarbon streams containing, in whole or in substantial part, mixtures of ethane, butane (iso-butane and normal butane), propane, or natural gasoline. This is the same definition presently used in the price control regulations. Where the natural gas liquid is separated into butane, propane, natural gasoline, etc., the tax applies to the sale or use of these products or blends of these products and not to the mixed stream.

3. Rate of tax

The natural gas liquids tax is imposed in three stages based upon the difference between (1) the controlled price of the liquid or product and (2) the wholesale price of No. 2 distillate oil in the region in which the sale or use occurred in the most recent month for which data are available, adjusted for the difference in Btu content between the liquid or product and No. 2 distillate oil and for seasonal price differences between the month for which data are available and the month in which the sale or use occurred. (For this purpose, the price of No. 2 distillate oil is not to be reduced by the amount of the home heating oil rebate added by this bill in connection with the crude oil equalization tax.) This difference is called the "price gap." The Btu adjustment is to be determined separately for different types of natural gas liquids and natural gas liquid products based on their Btu content. For purposes of these rules the "controlled price" is the controlled price of a particular vendor for the sale of a particular liquid at a particular time.

In 1978, the tax is equal to one-third of the price gap. In 1979, the tax is equal to two-thirds of the price gap. In 1980 and thereafter until the termination date, the tax is equal to the entire amount of the price gap.

The Secretary of the Treasury is authorized to determine the uncontrolled price of No. 2 distillate oil adjusted for seasonal price differences and for Btu differences between No. 2 oil and particular types of natural gas liquids. The Secretary is required to publish these figures in the Federal Register on a monthly basis before the month for which these figures are to be used to determine the rate of tax, using data for the latest month for which reliable data are available.

Because there is a lag of several months between the time when the sales of No. 2 oil are made and the earliest time when the price data for those sales are available to the Secretary, the price of No. 2 oil used for determining the rate of the natural gas liquids tax will be the price that occurred several months earlier than the month during which the taxable sale of natural gas liquids occurs. The committee understands that the price of No. 2 oil varies from season to season during the year but that the seasonal variations follow a fairly predictable pattern. In order to adjust for the use of noncurrent price data for determining the amount of the natural gas liquids

tax, the Secretary is to adjust (upwards or downwards, as the case may be) his calculation of the price of No. 2 oil to compensate for seasonal differences in the price of No. 2 oil between the prices at the time for which the latest data are available and the current month for which the tax is imposed.

For example, assume that in computing the price of distillate oil for the month of December, the most recent data available are for the month of September. If the price of No. 2 oil in a particular region for the month of September were $15 per barrel, and a particular natural gas liquid product had two-thirds of the energy content of a barrel of No. 2 oil, the uncontrolled price of the natural gas liquid (before the seasonal adjustment) would be $10 per barrel. Assume further that it was determined that the price of No. 2 oil in December is usually 10 percent higher than in September. After making this 10 percent adjustment, the imputed uncontrolled price of the liquid would be determined to be $11.00. If the controlled price of the liquid for a particular sale were $9.50, then the price gap would be $1.50 ($11.00 minus the $9.50 controlled price).

The committee understands that the price of No. 2 oil varies somewhat by region. Since the purpose of the tax on natural gas liquids is to increase the cost of natural gas liquids to the cost of No. 2 oil (adjusted for differences in Btu content), the Secretary is to determine the adjusted price of the No. 2 oil by region. The size and number of regions will be determined by the Secretary.

If natural gas liquids are used before the first sale for use and the tax is imposed, the controlled price to be used in computing the tax rate is to be the ceiling price which would have been applicable had the user sold the liquid instead of using it.

4. The taxable event

Under the committee bill, the tax generally is imposed on the last purchase prior to consumption of the natural gas liquid or natural gas liquid product. However, if the liquid is exported or used without a sale at retail, the tax is imposed at the time the liquid is exported or used. For example, the blending of butane into gasoline will be considered use of the butane and subject to tax at that time.

The imposition of the natural gas liquids tax on the sale to the ultimate consumer would cause substantial administrative problems where small amounts of liquids are sold in small containers, such as cigarette lighters and fuel cylinders for small stoves, lights, and torches. In order to avoid these administrative problems, the bill treats the placing of the liquid in a container having a capacity of 2 gallons or less as a use of the liquid. Consequently, the purchase of the liquid by such a manufacturer will be the taxable sale (i.e., the sale to him will be a "sale for use" within the meaning of the statute).

The equalization tax on natural gas liquids or its products applies only to natural gas liquids or their products which are sold or used within the United States. For this purpose, the United States includes its possessions, Puerto Rico and the continental shelf. The tax applies to products produced from imported natural gas liquids.

The committee bill contains three exceptions to the tax. First, in order not to tax both the natural gas liquids and their products, the

bill provides an exemption for natural gas liquids which are used as a feedstock in the production of natural gas liquid products.

Second, the tax does not apply to a retail sale of the liquid or its products if the liquid or product is to be used in an exempt structure. For this purpose, an exempt structure means a building or other structure 80 percent or more of the internal usable space of which is used as a residence or as a hospital, school or church.

Third, the tax does not apply to a retail sale of the liquid or its products if the liquid or product is to be used by the purchaser on a farm for farming purposes. The term "use on a farm for farming purposes" has the same meaning here as in the exemption under section 6420, relating to gasoline that is used on a farm for farming purposes.

5. Liability for and collection of the tax

Under the bill, the consumer of natural gas liquids or their products is liable for the tax. However, if the liquid is exported or used prior to retail sale, the tax is imposed upon the exporter or user.

Generally, the retailer is liable for the collection of the tax. The tax is to be paid on or before the 15th day of the second month after the month in which the retail sale occurred.

6. Credit or refund of crude oil tax where crude oil is used to produce natural gas liquids

A substantial amount of the natural gas liquids produced in this country is a product of the refining of crude oil. In order that there not be both a tax on the crude oil and on the natural gas liquids produced from such crude oil, the bill provides for a credit or refund of the crude oil equalization tax for the portion of domestically refined crude oil that is used to produce natural gas liquids. The credit or refund is available only to a refiner who furnishes such evidence as the Secretary may require to indicate that the price for the natural gas liquids produced from crude oil at his refinery does not include any of the tax on the crude oil for which the credit or refund is claimed.

The amount of the credit or refund on a per barrel basis is a fraction of the average net tax imposed on all refined products. (The net tax is the gross tax minus the reduction in Federal income taxes resulting from absorption of part of the tax by businesses, which is to be determined annually by the Secretary.) The fraction is equal to the Btu content of natural gas liquids produced from crude oil by a refiner divided by the Btu content of all the refined products produced from crude oil by that refiner during that period. The same amount of refund or credit is available for all crude oil that is refined into natural gas liquids regardless of the amount of tax that was actually paid on that crude oil and regardless of whether the crude oil was exempt from the crude oil equalization tax because it was stripper oil or foreign oil.

C. Presidential Authority To Suspend Increases in Equalization Taxes

The bill grants the President the authority to suspend any increase, or part of any increase, in either the crude oil equalization tax or the

natural gas liquids tax, or both, if there is a significant increase in the world price of oil which will result in an increase in the equalization taxes and the President determines that the increase will have a substantial adverse economic effect. The suspension would be accomplished by limiting the increase in the uncontrolled price of crude oil or the price of distillate fuel oil (for the natural gas liquids tax) which would otherwise be taken into account. This limit would have the effect of reducing the amount of the increase in the tax. Any suspension plan must be uniform among all classifications of crude oil and natural gas liquids and natural gas liquid products.

The bill provides that the President may suspend any increase in the equalization taxes by submitting a suspension plan to Congress. The bill requires that the suspension plan contain an explanation of the adverse economic effects on the basis of which the President has decided to suspend the tax. However, the committee does not believe that there will generally be an adverse economic effect as long as the increase is not more than the overall rate of inflation.

The bill limits in two ways the President's authority to suspend increases in the equalization taxes. First, the bill limits the length of any suspension of increased taxes to one year. If the President wants to extend the suspension beyond one year, he is required to submit a new suspension plan.

Second, the bill provides that the suspension plan can be vetoed by either House of Congress within 15 days of its submission to Congress by the President. In connection with the consideration of any suspension plan by Congress, the bill contains a number of rules that are designed to expedite the consideration of the suspension plan within the 15 day limit.

The bill provides that the suspension plan be delivered to the Clerk of the House of Representatives and to the Secretary of the Senate on the same day. The suspension plan is then to be referred to the Ways and Means Committee in the House and the Finance Committee in the Senate. Those committees then have 7 calendar days to consider the suspension plan. If one of the committees does not act within the 7-day limit, the suspension plan can be brought up in that House without committee action.

Debate on the suspension on the floor of either House is limited to 10 hours. In addition, the bill contains a number of procedural rules designed to expedite consideration of the suspension plan and to prevent procedural delays in the consideration of the suspension plan.

D. Equalization Tax Rebates

The bill provides two basic rebates of the equalization taxes (in addition to the exemptions from these taxes described above in the explanation of the taxes themselves.) These are a system of per-adult tax credits and special payments and a heating oil refund to residences and to certain institutions.

1. Crude oil equalization tax receipts credit

The bill provides a new tax credit for individuals called the "crude oil equalization tax receipts credit." Generally, the credit will be a

flat amount for each taxpayer. (In a joint return, each spouse is considered a separate taxpayer for this purpose.) This amount, referred to as the crude oil payment, will be based on the net revenue from the equalization taxes and will be determined by the Secretary of the Treasury in a manner described below. The amount of the credit will equal the crude oil payment for single persons and for married persons who file separate returns. For married couples who file joint returns and for heads of households (that is, single persons with dependents), the amount of the credit will equal twice the crude oil payment. Estates, trusts and nonresident aliens will not be eligible for this tax credit.

Generally, the tax credit will be limited to tax liability; however, it may exceed tax liability for persons entitled to the earned income credit.[3]

The crude oil equalization tax receipts credit will be reflected in lower withheld taxes for wages paid during 1978. The bill gives the Secretary of the Treasury the authority to issue new withholding tables for 1978 which reflect his estimate (as of October 1, 1977) of the amount of the crude oil payment for 1978. The committee intends that the credit appear as a separate line item on tax forms 1040 and 1040A.

The precise amount of the crude oil payment, on which the tax credit will be based, is to be determined by the Secretary of the Treasury in consultation with the Secretary of Energy and is to be published in the Federal Register no later than October 1, 1978. The Secretary is to set the amount of the crude oil payment so that the estimated revenue loss from the crude oil equalization tax receipts credit plus the outlays for the special payments (including the payments to Puerto Rico and the possessions) will approximate, as closely as possible, the net revenues from the equalization taxes, reduced by the estimated administrative costs of the special payments and the home heating oil refund. The net revenues from the equalization taxes are defined as the gross revenues from those taxes attributable to first purchases of crude oil and sales to end users of natural gas liquids during calendar year 1978, reduced by (1) the amount of the home heating oil rebate, (2) the estimated reduction in corporate and individual income taxes which will result from businesses' being unable to pass on to consumers the full amount of the equalization taxes, and (3) the refund of the crude oil equalization tax on crude oil processed into natural gas liquids.

The committee believes that the full amount of the equalization taxes will not be passed through to consumers and that part of the taxes will be absorbed by businesses and will reduce business profits. The reduction in business income taxes resulting from this absorp-

[3] For this purpose, tax liability will be determined after subtracting the following tax credits: the foreign tax credit (sec. 33 of the Code), the credit for the elderly (sec. 37), the investment credit (sec. 38), the work incentive credit (sec. 40), the political contributions credit (sec. 41), the general tax credit (sec. 42), the child care credit (sec. 44A), the new jobs credit (sec. 44B), the home insulation credit (new sec. 44C) and the electric car credit (new sec. 44D).

tion of part of the tax by businesses will offset some of the additional gross revenue raised by the equalization taxes themselves and, therefore, will not be available to be returned to consumers. (To the extent that businesses absorb part of the taxes, the combination of taxes and rebates will actually increase consumers' disposable income because their credits and special payments will include the amount of the tax absorbed by businesses and will be reduced only by the estimated reduction in business income taxes that is expected to occur.)

Businesses should be unable to pass through to consumers the full equalization taxes for several reasons. First, U.S. oil refiners (especially small refiners) receive certain benefits as a result of the existing "old oil entitlements program," which is intended to equalize the cost of crude oil among various U.S. refiners regardless of their mix of price-controlled or uncontrolled crude oil. As the crude oil equalization tax is phased in, the entitlements program will be phased out, and refiners will lose these benefits. Second, the existing controls on oil refiners and distributors reduce competition in those industries, which leads to higher prices which partly offset the lower prices resulting from the price controls on crude oil. Phasing out the controls on oil refiners and distributors in connection with the crude oil equalization taxes, then, should also mean that prices to consumers will rise by less than the full amount of those taxes. Finally, many businesses sell their products in world markets at prices based on the world price of oil. These companies are now receiving windfall profits from being able to buy oil at controlled U.S. prices and sell their products in markets in which their competitors must pay world oil prices. When the price of crude oil in the United States is raised to the world price, these businesses will not be able to raise their product prices above the world price, and the price to U.S. consumers of these products will not increase.

It is not clear at this time just how strong will be these economic forces which can be expected to prevent a full passthrough of the equalization taxes to consumers. To some extent, the amount of the passthrough will depend on the precise nature of regulations on the industry and on the tariffs or license fees imposed on imports of petroleum products, neither of which is known with certainty at this time. Therefore, the bill empowers the Secretary of the Treasury to estimate the extent to which income tax revenues will be reduced as a result of absorption of part of the equalization taxes by businesses. The committee expects that the Secretary will undertake a careful study of this issue prior to making his estimate.

Under current market conditions and regulations, the committee believes that at least two-thirds of the equalization taxes would be passed through as higher prices to consumers.

2. Special payment to recipients of social security, SSI and railroad retirement benefits

The committee was concerned that many adults who have little or no tax liability would receive no benefit from the crude oil equalization tax receipts credit, even though their energy costs would rise as

a result of the equalization taxes. In order to provide comparable benefits to these people, the bill provides for a series of special payments, which will be made in 1979.

The bill provides a special payment, equal to the crude oil payment (defined above), to recipients of monthly social security benefits (under title II of the Social Security Act),[4] monthly railroad retirement pensions or annuities (under the Railroad Retirement Acts of 1935, 1937 or 1974), or supplemental security income (SSI) benefits as eligible individuals or spouses (under Title XVI of the Social Security Act). Child beneficiaries of social security (except disabled adult children) are excluded from this special payment; therefore, this special payment will largely be limited to adults, except for certain disabled children who receive SSI benefits. The SSI payment excludes persons who receive only State supplements and no Federal SSI benefit.

For social security and railroad retirement beneficiaries, the payment will be made to persons who are entitled to benefits for the month of May 1979. For SSI beneficiaries, the month of eligibility will be June 1979. In all cases, the payment will be made only to persons who receive their benefits for the appropriate month in a check issued no later than June 30, 1979, and whose names are submitted by the Social Security Administration to the Treasury Department before August 1, 1979. (Others may claim the "roundup payment" described below.)

A payment is to be made only to an individual who is a resident of the United States, defined to include the fifty States and the District of Columbia. (This limitation applies to the special payment to AFDC recipients and the roundup payment as well.) Residents of Puerto Rico and the possessions will receive a payment administered by the governments of these places.

The amount of this special payment is to be reduced by the amount of the crude oil equalization tax receipts credit shown on the individual's tax return for his taxable year ending in 1978. This amount of the credit to be subtracted from the special payment is to be adjusted for any mathematical errors or other adjustments made to the tax return before June 1, 1979, but not for any subsequent adjustments. (Presumably adjustments made prior to June 1 will be posted to the IRS Master File, which will be used to administer the check for double payments, and adjustments made after that date will not be so posted.) For joint returns, one-half of the crude oil equalization tax receipts credit is to be allocated to each spouse for the purpose of determining the special payment.

The committee intends that these special payments be made as follows: the Social Security Administration will prepare a computer tape consisting of the names and (to the extent possible) the social security numbers of beneficiaries of social security and railroad retirement programs for May 1979 and of SSI beneficiaries for June 1979. The Social Security Administration will process this tape to ensure that beneficiaries of more than one of these programs are listed only once,

[4] This includes recipients of special monthly benefits (under sec. 228 of the Social Security Act) for uninsured persons who attained age 72 before 1968 and who had no Social Security.

that nonresidents are excluded, and that child social security beneficiaries (other than disabled adult children) are deleted. Shortly after August 1, 1979, the Social Security Administration will send this tape to the Internal Revenue Service.

The IRS will administer the actual screening for double payments of the special payment and the tax credit. The IRS will attempt to match each social security, SSI or railroad retirement beneficiary with a tax return filed for a taxable year ending in 1978 (and which will, therefore, have been posted on the 1978 IRS Master File). It will then reduce the amount of any beneficiary's special payment by the amount of any crude oil equalization tax receipts credit shown on the Master File. Having performed these calculations, the IRS will submit the appropriate information to the Treasury, which will make the actual payments.

The Secretary of the Treasury is to be primarily responsible for eliminating double payments under these rules. The Secretary of Health, Education and Welfare, the Railroad Retirement Board and the appropriate State agencies are required to provide to the Secretary of the Treasury whatever information and data are found by him to be necessary in order to make the determinations (such as eligibility for, and amounts of, payments) required under these provisions. They are also to process these data as directed by the Secretary of the Treasury.

Solely for purposes of these rules, a waiver of the otherwise applicable Federal disclosure laws is provided to enable the Secretary of the Treasury to collect, analyze and distribute information and data necessary for him to execute the requirements of this provision. The Secretary of the Treasury is also required to establish safeguards to prevent use and disclosure of this information for any purpose other than that provided by this bill.

The committee intends that the rules designed to prevent payments not cause significant delays because of the unavailability of necessary information in useful form. The bill consequently provides that the Secretary of the Treasury may waive some of these rules to prevent double payments if he concludes that waiting for the necessary information to be available in a usable form would cause significant delay or would unduly increase the administrative cost of the program. When he makes such a waiver, the Secretary is to report to Congress the reasons for the waiver and the circumstances surrounding it.

It is foreseeable that these rules will cause some individuals to receive a payment under this provision and a tax credit which total more than the individual would otherwise be entitled to receive. The bill provides that a recipient will not be liable to repay any erroneous or excessive payments resulting from incorrect application of the rules against double payments unless these payments have resulted from fraud or gross negligence. Similarly, the Federal, State and local officers responsible for such double or excessive payments are relieved from liability in the absence of fraud or gross negligence.

The committee intends that payments under this provision should not change an individual's eligibility for federal or federally assisted aid programs. The cost of identifying and making the adjustments might well exceed any savings in assistance funds were the payments

to be taken into account for these purposes. The committee has included a provision under which payments under this section of the bill are not to be considered income or (in 1979 and 1980) as resources for purposes of determining who is eligible to receive aid or assistance, or the amount or extent of aid or assistance, under any federal or federally assisted program. For this purpose the concept of aid or assistance is intended to include all assistance benefits including those made in a form other than cash, such as a reduced rental and eligibility for a loan. This requirement is to be treated as a condition for federal financial participation in any such state or local aid or assistance program for the first calendar quarter of 1980.

Payments received under this provision are not to be considered income to the recipient for purposes of the Federal income tax laws.

3. Special payment to AFDC recipients

The bill also includes a special payment to persons who receive aid to families with dependent children (AFDC) as relatives with whom dependent children were living, spouses of such relatives living with such relatives, or other adults living in the house whose needs are taken into account in determining AFDC benefits.

Generally, the amount of this special payment will equal the amount of the crude oil payment. However, in the case of payments to a relative with whom a dependent child is living who is either not married or not living with his or her spouse, the amount of the AFDC payment will be twice the crude oil payment.

This AFDC payment is to be made by the States and the District of Columbia. (Puerto Rico and the possessions are not eligible for the AFDC payment because the bill provides a special payment to residents of these places, described below.) Individuals are to be eligible only if they receive AFDC for June 1979 in a check issued no later than June 30, 1979, and the amount of their special payment is to be reduced by the amount of any special payment to them as social security or railroad retirement beneficiaries. (AFDC recipients are ineligible for SSI.) Because of the difficulty in coordinating the AFDC payment with the tax credit, there is no requirement that the AFDC payment be reduced by the amount of the tax credit.

The federal government is to reimburse the States for the full amount of all payments made under this program, plus an additional amount to cover administrative costs equal to $2.00 for each AFDC relative with whom dependent children were living. (In other words, the reimbursement will be $2.00 for each AFDC family.)

It is intended that each State, as soon as possible, provide the Secretary of the Treasury with an estimate of the cost of paying its June 1979 AFDC recipients the special payment. When the Secretary of the Treasury has reviewed this estimate and found it satisfactory (using any information or assistance which he may require of the Secretary of Health, Education, and Welfare), a letter of credit is to be issued to the account of the State providing funds for the State to draw against in making the special payment and to compensate the State for costs of administering the payment.

The bill provides for the furnishing of information by the States and the Secretary of Health, Education, and Welfare to the Secretary

of the Treasury to enable him to exercise his responsibility under this section of the bill, and it contains a limitation on the use and disclosure of this information. There is also a waiver of the rules to prevent double payments and of the disclosure rules and a relief from liability similar to the provisions applicable to the special payment to social security, SSI, and railroad retirement beneficiaries. Like the other special payments, the AFDC payment is to be disregarded in determining eligibility for or benefits under federal or federally assisted aid programs and is not to be considered income for the federal income tax.

To the extent necessary and possible, existing administrative rules and procedures pertaining to the AFDC program are to be followed in making the special payment required by this section. This includes existing audit and reconciliation procedures and the rules, functions and obligations pertaining to the rights of individuals. However, the committee emphasizes that administrative delays should be reduced as much as possible in order to produce prompt receipt of the payments by qualified beneficiaries. Thus, the administrative authorities are not expected to follow, for example, the specific quality control procedures and sanctions described in title 45, sections 205.40 and 205.41 of existing federal regulations.

4. Other special payments

Even with the tax credit and the special payments to social security, SSI, railroad retirement and AFDC beneficiaries, there would be adults who would not receive any benefit under the rebate program. To ensure that every adult receives some compensation for the higher energy costs which result from the crude oil equalization taxes, the bill includes a "roundup payment," which may be claimed by any individual who, on December 31, 1978, is age 18 or older and is a resident of the United States and who files the appropriate form with the Treasury Department. (The committee intends that the Treasury make provision for married couples to claim the roundup payment by filing a joint return.)

The amount of the roundup payment will be the amount of the crude oil payment, described above, for single persons and for married persons who file separate returns; and it will be twice the crude oil payment for married couplies who file joint returns and single heads of households. The amount of the roundup payment to any individual will be reduced by any crude oil equalization tax receipts credit shown on that individual's tax return for the taxable year ending in 1978 and by the amount of any other special payment to which he is entitled. For a joint return, the crude oil equalization tax receipts credit will be prorated between the spouses for this purpose.

The roundup payment will be limited to people who file the appropriate form with the Treasury Department on or before December 31, 1979. These forms will have to contain the individual's social security number. The committee intends that the Treasury make these forms available shortly after the other special payments are made.

The roundup payment will be disregarded in determining eligibility for and benefits under federal or federally assisted aid programs, and will not be considered income for federal income tax purposes.

5. Payments to Puerto Rico and possessions

The crude oil equalization tax receipts credit is available only to persons subject to the U.S. individual income tax (excluding nonresident aliens), and the special payments are available only to residents of the 50 States and the District of Columbia. Residents of Puerto Rico and the U.S. possessions, however, will experience an increase in oil prices because refineries which sell oil to these areas will pay some crude oil equalization tax and also will lose their benefits under the old oil entitlements program, which will be phased out as the crude oil equalization taxes are phased in. The committee, therefore, believes that Puerto Rico and the possessions should be made eligible for the benefits of the rebate program.

The committee believes that the most efficient way to conduct a rebate program for Puerto Rico and the possessions would be to have the local governments administer the program themselves. Thus, the bill authorizes payments to the governments of Puerto Rico and the possessions contingent on their submitting an acceptable plan to the Secretary of the Treasury for the distribution of these amounts to their residents in a manner similar to the program of tax credits and special payments contained in this bill for the United States. To be acceptable, such a program will have to minimize the administrative costs involved. The amount of the payments to Puerto Rico and the possessions will include both the amounts to be distributed to residents of those places and a reimbursement for administrative costs.

6. Trust fund

The bill creates a Crude Oil Equalization Taxes Trust Fund and appropriates into that trust fund the revenues attributable to the equalization taxes for 1978 and received in the Treasury before January 1, 1980. The precise amount appropriated to the trust fund will be the gross revenues from the equalization taxes, reduced by the reduction in federal income taxes resulting from absorption of part of the tax by businesses and the tax refund to refineries who use crude oil to produce natural gas liquids. The bill authorizes an appropriation from the trust fund for the special payments, the tax credits in excess of tax liability, the payments or reimbursements for administrative costs of the special payments, the payment to Puerto Rico and the possessions, and the heating oil refund. The trust fund is to terminate after December 31, 1979, and all funds remaining in the trust fund and not obligated for expenditure are to be returned to the general fund of the Treasury on that date.

7. Heating oil refund

The bill provides what is, in effect, an exemption from the crude oil equalization tax for heating oil used in residences, churches, schools and hospitals. This is accomplished by providing a refund of the tax to distributors of heating oil for each gallon they sell to one of these users, contingent on the distributor's passing through this refund to these consumers as lower prices.

The heating oil refund will be a fixed amount per gallon, which will be determined yearly on or before December 1 of the preceding year by the Secretary of the Treasury in consultation with the Secretary

of Energy. This amount will be determined by first estimating the gross revenues to be derived from the equalization taxes for the calendar year in question, then by reducing this estimate by the estimated reduction in Federal income taxes for that year expected to result from absorption of part of the equalization taxes by businesses, and finally by dividing this difference by the estimated number of gallons of petroleum and petroleum products to be consumed in the United States during that calendar year. It is expected that the heating oil refund will be 1.3 cents per gallon in 1978, 2.6 cents in 1979, 4.1 cents in 1980. (The Treasury is to round off the actual figure to the nearest one-tenth of a cent.)

The refund is payable for all heating oil distributed to an exempt structure, regardless of whether the crude oil is produced or refined in the United States.

To be eligible for the refund, heating oil must be placed into the tank of an "exempt structure," defined to be a building or other structure 80 percent or more of whose internal usable space is used as a residence, hospital, school or church. Residences include both homes and apartments, but not hotels. Schools, for this purpose, include public or private elementary schools (including kindergartens and nursery schools), secondary schools, vocational schools, business schools, junior colleges, teachers colleges, normal schools, professional schools, universities, scientific or technical institutions and other institutions for furnishing education for adults. They do not include institutions in which more than 20 percent of the student course hours are normally devoted to courses in bartending or personality development; sales or sales management courses which do not provide specialized training within a specific vocational field, unless the institution offering such a course submits a justification showing that at least one-half of the persons completing the course over the preceding two-year period have been employed in the sales or sales management field; or courses which are avocational or recreational in character. For schools, hospitals and churches, the heating oil refund is only provided for structures used in connection with their functions as schools, hospitals or churches, as the case may be.

Heating oil is defined as residual fuel oil and number 2 distillate fuel oil.

The committee was concerned that the heating oil refund would impose a hardship on distributors, who would have to reduce prices to customers and only subsequently would receive refunds from the Treasury. To alleviate this hardship, the bill provides that distributors may claim monthly advance payments with respect to estimated sales which will qualify for the heating oil refund. Provision for claiming such advance payments and effecting periodic reconciliations will be made under regulations prescribed by the Secretary of the Treasury.

The heating oil refund which any distributor may receive with respect to any one residence will be limited to a maximum amount, which is to be determined by the Secretary of the Treasury and is to be based on the heating oil consumption of a representative home in each region of the country. The Secretary may revise his estimate of this maximum amount of heating oil eligible for the refund during the year based on weather conditions in each region.

Effective dates

The crude oil and natural liquid equalization taxes are applicable to first purchases of crude oil and sales to end users of natural gas liquids after December 31, 1977, and before October 1, 1981. The tax credit and special payments are effective for taxable years beginning in 1978. The heating oil refund is effective for sales of heating oil after December 31, 1977, and before October 1, 1981.

Revenue effect

The crude oil and natural gas liquid equalization taxes are expected to produce a revenue gain of $1.5 billion in fiscal year 1978, $5.3 billion in fiscal year 1979, $9.4 billion in fiscal year 1980, and $12.3 billion in fiscal year 1981.

The home heating oil refund is expected to be $0.1 billion in fiscal year 1978, $0.5 billion in fiscal year 1979, and $0.8 billion in fiscal year 1980. The crude oil equalization tax receipts credit is expected to reduce budget receipts by $1.8 billion in fiscal year 1978 and $0.8 billion in fiscal year 1979. The special payments will involve outlays of $0.8 billion in fiscal year 1979.

Energy savings estimate

It is estimated that the crude oil and natural gas liquids equalization taxes will reduce the consumption of oil by the equivalent of from 430,000 to 650,000 barrels per day in 1985. This estimate assumes continuation of price controls in their present form and extension of the equalization taxes through 1985.

D. EXCISE TAX ON BUSINESS USE OF OIL AND NATURAL GAS; CREDIT AGAINST THE TAX FOR QUALIFYING INVESTMENTS

1. Excise Tax on Business Use of Oil and Natural Gas (Sec. 2041 of the bill secs. 4991–4995 of the Code)

Present law

Under present law, natural gas prices for gas which is sold in interstate commerce are regulated by the Federal Power Commission. Gas which is sold intrastate is not subject to Federal price control.

Historically, the price of natural gas sold in interstate commerce has been controlled at levels ranging from about 14 cents per thousand cubic feet ("mcf") to 34 cents per mcf, depending on the area of the country where the gas was produced and sold. Interstate gas has sold at levels substantially below those prices charged for an equivalent amount of energy in the form of oil (even in periods when oil prices were far below current levels). Beginning in 1974, prices for gas which is newly committed to interstate commerce have been standardized on a national basis and have increased substantially, so that gas newly dedicated to interstate commerce is now selling at a rate of approximately $1.45 per mcf. However, much gas is selling at prices below this rate under old contracts which were made before the recent round of price increases.

The FPC has authority to permit "spot sales" of interstate gas at higher than controlled prices during limited periods of emergency. In addition, under the Emergency Natural Gas Act of 1977, Congress authorized the President to permit sales of gas at uncontrolled prices to prevent local natural gas emergencies, but this authority expires July 1, 1977, unless it is extended.

The price paid by consumers for natural gas which is delivered to their homes and businesses is regulated at the State level by public utility commissions. Generally, current pricing policies favor bulk industrial users of natural gas. However, these customers are usually "interruptible," which means that in time of shortage, their gas is shut off first.

Under the Energy Supply and Environmental Coordination Act of 1974, the Federal Energy Administration may prohibit new or existing utility power plants or major industrial fuel burning installations from burning petroleum or natural gas if certain findings are made. For existing plants, the FEA must show that the plant has the practical capability to burn coal, that coal and transportation facilities are available, that coal burning would not cause adverse environmental effects, and that, in the case of a power plant, a conversion will not impair the reliability of electric service. For new plants, the FEA may

order that coal be used unless the reliability or adequacy of service is likely to be impaired or an adequate and reliable supply of coal is not expected to be available.

Reasons for change

The committee believes that the urgency of the energy problem requires a special measure designed specifically to reduce the consumption of oil and natural gas by large industrial and utility users. The cost of oil to these users must be raised to reflect the growing threat which unchecked oil imports pose to the security of the United States. The cost of natural gas must be raised because the existence of long-term regulated contracts has kept the price of natural gas below its replacement cost, thus encouraging too much consumption. At the same time, the revenue from the taxes used to achieve these cost increases should be employed to provide incentives for the purchase of new equipment which burns fuels other than oil or gas. The committee has therefore designed a combination of taxes and incentives which, it believes, will achieve a substantial reduction in oil and gas use.

The committee has taken great care to exempt from taxation categories of oil and gas consumption in which no substantial reduction in the use of oil and gas, either through conservation or conversion, appears to be achievable or in which the use of oil or natural gas is necessary for environmental reasons. The committee has divided those categories which would not be exempt into three classifications, or Tiers, each of which is taxed at a different rate to reflect variation in conversion and conservation potential. To prevent excessive administrative costs and to focus the tax on the relatively small number of companies which account for the great majority of industrial energy consumption, the committee would also allow all users to consume a certain quantity of oil and natural gas exempt from taxation.

The tax on natural gas used by industries varies inversely with the user's cost of natural gas, so that firms which pay a low price for their gas would pay a correspondingly higher tax, and vice versa. Thus, this tax would make the cost of natural gas nearly uniform among users, thereby minimizing one of the most disadvantageous results of the current system of natural gas pricing. On the other hand, the tax on oil would be a flat tax per unit of use, because there is relatively little variation in the price of oil.

To provide a strong incentive for the purchase of equipment which burns fuels other than oil and gas, the committee would allow firms a 100 percent credit against their consumption tax for each dollar spent on such equipment and on associated pollution control and fuel handling equipment. Because the committee believes that utilities' new facilities will burn coal even without an incentive, utilities would receive the credit only to the extent that they phase down or replace an existing oil- or gas-fired boiler. To provide a conversion incentive for firms which would have too little users tax liability to be helped by this credit, the committee would allow such firms to elect, instead, an additional 10-percent credit against their income tax liability.

Because this tax is intended as a measure to encourage the conservation of oil and natural gas, it is imposed not only under the taxing power of the Congress, but also under the power to regulate commerce,

Explanation of provision

The tax applies generally to both users of oil and gas as a fuel in a trade or business. Raw material uses of oil and gas (for example, as feedstocks) are thus not affected by this tax. Users of less than the 50,000 barrels of oil or its equivalent in natural gas are not subject to the tax.

A. Rates and Structure of Tax

1. Oil and gas subject to tax

Under the bill, the tax is imposed on certain trade or business uses (known as "taxable uses") of oil and natural gas. The structure and rate of tax are different for these two fuels, however.

For this purpose, "oil" is defined to mean refined petroleum products, other than gasoline,[1] crude oil and any natural gas liquids other than those which have an API gravity [2] of 110 or more. "Natural gas" means any natural gas, petroleum or a product derived from either petroleum or natural gas which has an API gravity of 110 or more. Natural gas includes methane (ordinary natural gas), as well as propane and butane. Any substances of a kind which are not generally marketable for use as a fuel are not taxed under this section. Under present technology, petroleum coke and blast furnace gas are examples of fuels not generally marketable. Of course, the tax is not imposed on oil or natural gas which is produced from other substances, such as coal gasification or liquefaction.

2. Categories of use (Tiers)

The committee has classified different taxable uses in several tiers in order to take into account the varying potential for conversion and conservation. Use in a boiler or gas- or oil-fired turbine or other combustion engine (except for use included in Tier 3) is categorized as Tier 2 use and is generally subject to the highest tax. The committee believes that substantial conversion potential exists for uses in this tier.

Tier 3 generally applies to electric utilities. It includes the use of oil and natural gas (1) in the production of electricity for sale to another person (not under common control), (2) for use by a producer in a plant with a rated capacity of 100 megawatts or more of electricity, or (3) in the production of steam by a regulated public utility (as defined in Section 7701(a)(33) of the Code) whose principal activity is the production of electricity for sale. The committee believes that substantial conversion potential also exists for uses in this tier. However, because large boilers are involved, a substantial lead time may be necessary for any conversion. For that reason, no tax is imposed on this Tier until 19983. (A user who uses a boiler for both Tier 2 and Tier 3 uses (for example, in cogeneration), must allocate the fuel to the Tiers on the basis of the energy used for the two purposes.)

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[1] Gasoline is defined, as in Code section 4082(b), to mean all products commonly or commercially sold as gasoline which are suitable for use as a motor fuel.

[2] API gravity is the standardized specific gravity of crude oil and refined products established by the American Petroleum Institute (API), now used worldwide.

Tier 1 includes use of oil or natural gas in combustors other than boilers, since the committee believes a significant potential for conservation of oil and natural gas exists for these uses. Examples of Tier 1 uses include many types of lime kilns and cement kilns.

3. Tax rates on oil

The tax which is imposed on uses of oil is shown in the following table:

	The tax per barrel is—		
	Tier 1	Tier 2	Tier 3
If the taxable use occurs during calendar year:			
1979	$0.30	$0.30	None
1980	.60	.60	None
1981	1.00	1.00	None
1982	1.00	1.45	None
1983	1.00	2.00	$1.50
1984	1.00	2.50	1.50
1985 or thereafter	1.00	3.00	1.50

Beginning with the tax for 1981, the rates shown in this table are to be adjusted for any inflation occurring between 1979 and the year preceding that of the taxable use. For this purpose the implicit deflator for the gross national product for the calendar year (as determined by the Department of Commerce), is to be used as the index of inflation. For example, if the 1979 value of the deflator were 165.69 and the 1980 value were 174.81, the ratio of the 1980 value to the 1979 value is 1.055. The actual tax rate for both Tier 1 and Tier 2 uses in 1981 would therefore be $1.00 multiplied by 1.055, or $1.06 when rounded to the nearest whole cent (as the bill provides).

4. Tax rates on natural gas

The tax on natural gas used in Tier 1 or Tier 2 uses is computed separately for each use. In general, the Tier 2 tax is designed to raise the industrial cost of natural gas to the equivalent cost of No. 2 distillate oil (without the users tax). Thus, the tax has a variable rate, pegged to a target price. The tax is the excess of the target price over the individual users acquisition cost. The exact tax will vary according to the region of use, the Tier of use and the extent to which the gas was purchased on an interruptible basis.

When fully phased in, in 1985, the target price for Tier 2 use will be the cost of an equivalent amount of energy in the form of No. 2 distillate oil. For Tier 1 use, the target price will be 30 cents (adjusted for inflation) per million BTU lower than the cost of No. 2 distillate oil. Thus, for Tier 1 and Tier 2 use, the tax will be computed in several steps. (Tier 3 use is subject to a flat rate of tax, as discussed below.)

First, the Secretary of Energy is to announce by March 31 of each year the BTU equivalency price of No. 2 distillate oil for each region.

This price is to be the average price per barrel of all such oil sold within the region in the preceding calendar year. Applicable import license fees and severance taxes applying to such oil are to be included in these announced prices. To arrive at a BTU equivalency price for each million BTUs of natural gas, the price per barrel is divided by 5.8 million. (A thousand cubic feet of natural gas equals about 1 million BTUs.)[3] For purposes of this computation, the Secretary of the Treasury is to divide the United States into appropriate regions.

Second, the "natural gas target price" is to be determined for each region and each Tier by substracting from the BTU equivalency price an amount from the following table:

	The amount subtracted for tier 1 is—	The amount subtracted for tier 2 is—
If the taxable use occurs during calendar year:		
1979	$1.35	$1.05
1980	.70	.40
1981	.65	.35
1982	.55	.25
1983	.50	.20
1984	.45	.15
1985 or thereafter	.30	0

Beginning in 1981, all numbers in the above table are to be adjusted upward for any inflation which has occurred between 1979 and the year preceding that of the taxable use, in a manner similar to that in which the tax on oil is adjusted for inflation. Thus, using the previous example, if the inflation adjustment for 1981 were 1.055, then the subtraction amount for that year would be $.69 (65 cents times 1.055 rounded to the nearest cent) for Tier 1 and $.37 for Tier 2.

These two steps are to be done by the Secretary and the results are to be published in the Federal Register.

Each firm will then calculate its average cost per million BTU of natural gas which it used in each region and Tier. This cost does not include increases in State users taxes after April 20, 1977, but does include a reasonable allowance for transportation costs, not to exceed the cost which would be incurred in an arm's-length transaction. (Transportation costs of users who own their own pipelines or trucks are to be determined as if they incurred transportation costs in an arm's-length transaction.) To determine the tax rate applying to each separate category of energy use, the firm would subtract this average cost from the natural gas target price. The total tax liability is deter-

[3] In cases where natural gas liquids are consumed for a taxable use, the BTU equivalency price is to be determined by reference to the actual BTU content of the liquids.

mined by multiplying the applicable tax rate by the quantity of gas consumed in the corresponding use and adding all the resulting amounts.

For any gas purchased under interruptible contracts the tax applicable to such gas is reduced to 90 percent of the amount as calculated above. The bill specifically defines interruptible contracts to mean a contract or schedule which anticipates and permits interruptions by the supplier on short notice in non-emergency situations. Interruptible customers ordinarily have the capability of switching to alternative fuels on very short notice when informed by suppliers that gas deliveries will be temporarily terminated. Only those interruptible contracts which serve the purpose of promoting the efficiency of operation of the pipeline would be recognized for the purpose of this discount.

For example, consider the case of a firm which has three plants. The first plant is located in Region A, uses natural gas in a Tier 1 use, and purchases its gas on an interruptible basis; the second plant is located in Region A, uses its gas in a Tier 2 use, and purchases its gas on a firm (rather than interruptible) basis; and the third plant is located in region B, uses natural gas in a Tier 1 use, and purchases its gas on a firm basis. The following table illustrates the computation of the tax based on rates in effect in 1981:

Item	Plant		
	1	2	3
(1) BTU equivalency price for applicable region (per million BTU)[1]	$3.80	$3.80	$4.00
(2) Subtraction amount for applicable tier (adjusted for inflation)[2]	$.69	$.37	$.69
(3) Natural gas target price [(1)−(2)/ (per million BTU)	$3.11	$3.43	$3.31
(4) User acquisition cost per million BTU[3]	$2.75	$3.00	$2.80
(5) Tax rate [(3)−(4)] (per million BTU)	$.36	$.43	$.51
(6) Quantity of gas used (million BTU)	150,000	200,000	300,000
(7) Preliminary tax liability [(5) times (6)]	$54,000	$86,000	$153,000
(8) Provisional tax liability (90 percent of line (7) if interruptible service, 100 percent of line (7) if firm service)	$48,600	$86,000	$153,000

[1] The BTU equivalency price for natural gas would be announced by March 31, 1981, would be based on the average price of distillate oil sold in 1980 in the applicable region.

[2] The subtraction amount is the amount subtracted from the BTU equivalency price and is adjusted for inflation. This is done to phase-in the full tax on natural gas which equalizes, the cost of natural gas and the price of distillate oil. The figures in this table are from the example discussed further above.

[3] The user acquisition cost is the actual cost of natural gas to the user and is computed individually for each plant.

Actual tax liability would be less than the amount shown in item 8 of the table, however, because of the provision for an exempt amount (see discussion below).

If a firm has more than one tier of use or type of service at a single plant, then each tier and/or service type is treated as a separate use for the purpose of calculating the applicable tax.

In the case of natural gas which is used by gas producers or by any business under common control with the producer, or which was not acquired in an arm's-length transaction, the user acquisition cost is not to exceed the maximum lawful price applicable with respect to the sale of the gas under relevant laws regulating this sale.

The tax on natural gas used for Tier 3 uses is not imposed through 1982; the tax is 55 cents per million BTU for 1983, 65 cents for 1984 and 75 cents for 1985 and thereafter. These tax rates would also be adjusted for inflation, in a manner similar to that in which the tax on oil is adjusted for inflation. The Tier 3 tax, however, is subject to a cap, so that the tax cannot bring the cost of gas used for Tier 3 purposes above the BTU equivalency price of residual fuel oil, including the business use tax imposed on that oil. (There is no adjustment for gas purchased under interruptible contracts in connection with this cap.)

5. Liability for tax

The tax on taxable uses of oil and gas must be paid by the user on or before July 1 of the calendar year following the taxable use.

B. Exempt Amount

1. General exemption

In addition to exempt uses, discussed below, firms would also be able to exempt from taxation the BTU content of 50,000 barrels of oil. For this purpose, a barrel of oil is to be assumed to contain 6 million BTUs so that the exempt amount is equal to 300 billion BTUs. For example, a firm whose total use of natural gas was 150 billion BTUs would be able to exempt 150 billion BTU's, or 25,000 barrels, of oil. The taxpayer would be free to allocate this exempt amount among the various tiers of taxable use and, in the case of natural gas, among regions and types of service, and between oil and natural gas in such manner as the taxpayer may elect.

For the purpose of determining the exempt amount, persons who are members of the same controlled group of corporations and trades or businesses which are under common control are treated as one taxpayer. The term "controlled group of corporations" has the same meaning given to this term by section 1563(a) of the Internal Revenue Code except that a 50 percent control test is to be used (rather than an 80 percent test). The determination of whether other trades or businesses are under common control is to be made in a similar way under regulations prescribed by the Secretary.

The exempt amount for any taxpayer is to be divided among the persons treated as one taxpayer in proportion to their taxable use during the calendar year or, if all such persons agree, in such proportions as they agree upon.

2. Additional exempt amount in cases of competitive disadvantage

If any taxpayer owns a plant which competes in the same región with other firms whose plants are exempt from the tax because the

other firms' use of fuel is less than the BTU content of 50,000 barrels, and the Secretary finds that this exemption causes the taxpayer to be at a substantial competitive disadvantage relative to the other plants, the Secretary is to provide an additional exempt amount for these disadvantaged plants to the extent necessary to alleviate the resulting competitive problem. The names of any taxpayers and plants receiving additional exemptions are to be published in the Federal Register.

C. Exempt Uses

For uses of oil and natural gas which have little conversion or conservation potential, the committee has provided certain exemptions from the tax. Because the tax applies only to the use of the products as fuel, uses of oil and natural gas as raw materials, including use as petrochemical feedstocks, use in the production of carbon black, and use of products as a lubricant or wax are not subject to tax. Also exempt is the use of oil or natural gas in (1) residential facilities, such as apartments and hotels, (2) in transportation including vehicles, aircraft, vessels and pipelines, (3) on a farm for farming purposes, (4) in a shopping center, office building or other facility, which is not an integral part of a manufacturing, processing or mining facility, and (5) in exploration for and development, extraction, transmission, or storage of crude oil, natural gas, or natural gas liquids. Exemptions are also provided for certain process uses, uses by existing facilities which must use oil or gas for environmental reasons, new facilities and qualifying cogenerators which obtain exemptions under other parts of this bill, and other individual firms or uses for which there is little significant potential for conversion or conservation.

1. Specific exemptions

Use in residential facilities.—Use of petroleum or a petroleum product as a fuel in an apartment, hotel, motel, or other residential facility is exempted because the committee bill has not imposed any users tax on use of oil to heat or cool residences. Thus, the committee concluded that the same treatment should be accorded other accommodations which are largely residential in use. For these purposes, boarding houses, nursing facilities, day-care facilities, hospitals, and institutions for the disadvantaged are to be treated as residential facilities.

Use in transportation.—Use in a vehicle, aircraft or vessel is not taxed because existing excise taxes generally cover this use. Use in the compressors employed in pumping materials through pipelines are also included in this exemption. Use of petroleum or of a petroleum product as a fuel in heating or cooling a vehicle, vessel, or aircraft also is to be exempt because, in most cases, this fuel is supplied from the same source that propels the vehicle, vessel, or aircraft. To attempt to distinguish between these two uses would be administratively difficult, if not impossible.

Use on a farm for farming purposes.—Use on a farm for farming purposes was exempted because most farm uses would be exempt under the 50,000 barrel exemption. A use on a farm for farming purposes means use in the trade or business of farming on a farm situated in the United States. The term "farm" includes facilities for stock, dairy,

poultry, fruit, and fur-bearing animals; the term also includes truck farms, plantations, ranches, nurseries, ranges greenhouses, other similar structures used primarily for the raising of agricultural or horticultural purposes, and orchards.

The term "farming purposes" would include drying of grains and feed grasses and irrigation pumping.

Use in non-manufacturing commercial buildings.—Use of petroleum or petroleum products in a nonmanufacturing commercial building is exempt unless it is in integral part of a manufacturing, processing or mining facility. Because the committee intends to focus the tax on the largest users of energy (see "Exempt Amount" above), most owners of nonmanufacturing commercial buildings would be exempt from the tax even in the absence of a specific exemption.

Use in extraction of crude oil and natural gas.—Fuels used in exploring, extracting, transmitting, or storing crude oil and natural gas (or natural gas liquids) are exempt from this tax to avoid creating any disincentive to their production. This exemption does not apply to oil or natural gas used in a refinery.

2. Exempt process uses

Oil and natural gas may be used for several basic purposes. One use is for burning in a boiler, turbine or other internal combustor to produce steam or electricity. However, oil and natural gas are also employed in "process use", where the fuel is used in the manufacturing process itself.

In certain instances, there are substantial conversion or conservation possibilities in connection with process uses because the process involved could be performed correctly and economically with the use of some other fuel. However, there are other instances where the nature of the manufacturing process is such that there is no reasonable substitute for oil and natural gas. This would be true in cases where, for instance, the use of coal or some other fuel would damage the product or would increase the cost to such an extent that it would have a severe adverse impact on profitability.

For these reasons, the committee bill exempts certain process uses. (Process uses which are not exempt are subject to the Tier 1 tax.)

The exemption applies if there is no adequate substitute fuel (1) which may be used in place of the oil and natural gas without having a material adverse effect on the manufacturing process or the quality of the manufactured goods, and (2) the use of which is economically and environmentally feasible.

The determination of which process uses are covered by this exemption is to be made by the Secretary on a use-by-use basis. In determining these use-by-use exemptions, the Secretary is to examine, for each process use, whether a fuel other than oil or natural gas could be used in a manner which satisfies the above criteria. The substitute fuels to be examined would depend on the nature of the processes and on the technology which is available at the time of the determination. The most common fuel which would be evaluated as a possible substitute would be coal and its derivatives, but in particular situations substituting the use of fuels other than coal might be practical.

In making this evaluation, the Secretary is also to consider the possibility of indirect as well as direct uses of alternative fuels. For ex-

ample, some processes may be typically carried on in facilities large enough so that it would be economical for a firm to convert coal into low BTU gas or into electricity which could then be used to provide the necessary heat.

Material adverse effects on the quality of the goods are those which, from the point of view of the consumers of such products, would make them less desirable. Alternative fuels (other than oil and gas) could cause such effects in processes which now require direct application of a steady, even flame to the product, or in processes which require that the fuel not contaminate the product, or in processes which require precise temperature control to achieve the desired quality. Also, a substitute fuel would not be satisfactory if it impaired the reliability of whatever equipment might be used with it.

If an alternative fuel could be found which could be used without the adverse effects on the manufacturing process and product quality as described above, then the Secretary would also have to determine whether the use of this fuel is economically and environmentally feasible. (Environmental feasibility would be judged according to the standards discussed in the next section.)

In determining whether it is economically feasible to use a fuel other than oil or natural gas, the Secretary must also weigh the increase in oil and gas cost that would occur if the tax were imposed, as well as the rebates and credits available under other sections of this Act for equipment which could use the alternative fuel. The Secretary is also to consider capital and operating costs of using the alternate fuel. If, after taking these considerations into account, the Secretary found that the alternative substance could be used without significantly decreasing the ability of the average or typical firm engaged in the process under consideration to earn an adequate rate of return in this activity, then use in this process would not be exempt from the tax.

Examples of processes in which the use of oil and natural gas would generally be exempt if such determinations were to be made today include singeing fabrics in the textile industry, heat used in dye setting in the textile industry, very small process heaters and molecular sieve regeneration in the chemical industry, melting high-quality glass and glass forming and annealing in the glass industry, and the use of oil and natural gas in reheating, annealing and heat treating in the fabricated metals industry. If new technologies which may be developed in the future could make conversion feasible in one or more of these industries, then such uses would no longer be exempt. But under present technology, the use of substitute fuels for these uses are not practical based on the best information available to the committee.

This list set forth above is not intended to be all inclusive, and the committee anticipates that the Secretary will prescribe additional exempt uses by regulations as soon as practicable after enactment of this legislation.

3. Existing facilities subject to environmental regulations

The committee does not believe that a tax should be imposed on the use of oil or natural gas where these fuels must be used to comply with certain environmental regulations. Under the committee bill, if

a boiler or combustor was in existence or under construction on April 20, 1977 (or if on this date there was a binding contract for the construction of a new facility which would encompass such equipment), and the use of coal in this equipment or facility would be precluded by Federal or State air pollution regulations, then the use of natural gas or oil would not be subject to taxation. However, this exemption does not apply to new combustors or boilers which serve the purpose of either expanding an existing facility or replacing old equipment.

The exemption is only available, however, if State regulations precluding the use were in effect on April 20, 1977, or if the Secretary determines, after consultation with appropriate Federal and State agencies, that the adoption of the State regulations are necessary to meet a requirement of Federal law. Regulations of any local agencies which have jurisdiction under a Federally-approved State Implementation Plan under the Clean Air Act (or other Federal air pollution laws) would also be taken into account if these regulations were in existence on that date or they are necessary to meet a requirement of Federal law. If at any time the prohibition under the regulations is lifted, this exemption no longer applies.

4. Exemptions from the tax for new facilities affected by Title 1 of the National Energy Act

Sections 104 and 106 of the Energy Supply and Environmental Coordination Act (ESECA), as amended by proposed section 601 of H.R. 6831[4] would allow the Federal Energy Administration to exempt certain new facilities, either temporarily or permanently, from the prohibition orders which would otherwise be issued under ESECA. The committee does not feel it would be appropriate to impose a tax on any such exempt facilities, so use of oil and gas in these facilities would be automatically exempt from the tax for the duration of the exemption under ESECA.

Section 104 of ESECA generally prohibits new power plants from burning oil or natural gas. Power plants covered by these rules are those which contain single units capable of consuming fuel at a heat input rate of at least 100 million BTUs per hour or a group of units capable of consuming fuel at a heat input rate of at least 250 million BTUs per hour.

ESECA provides for exemptions from this prohibition for new power plants which show that there is no alternative site at which it can acquire an adequate and reliable supply of alternate fuel or in which the burning of such fuel would not be precluded by physical or environmental factors, or for which the use of an alternate fuel would not be financially feasible.

There is also an exemption from the prohibition orders for peak-load power plants or for new oil and gas-fired plants whose construction is necessary to maintain reliable electric generation service.

Because there would appear to be little potential for conversion from oil and gas under these circumstances, the committee does not believe

[4] Section references to ESECA are to the Energy Supply and Environmental Coordination Act as amended by Title 1 of this bill as introduced.

that a tax should be imposed on the use of these fuels at such facilities.

Section 106 of ESECA provides exemptions from similar prohibitions which would cover new "major fuel-burning installations" which are facilities other than power plants which satisfy similar fuel consumption standards. Exemptions from prohibition orders are available (1) when such units are precluded from use of oil or gas because an adequate and reliable supply of alternate fuel is not available, (2) when physical and environmental factors make the use of alternative fuel infeasible, or (3) when the use of an energy source other than natural gas and petroleum is not technically feasible in direct firing due to the contamination of the product or inability to maintain a satisfactory flame control, and substitution of steam for direct heat is not possible due to requirements of the process. Since there would appear to be little conversion potential in these units, the committee bill exempts use of oil and natural gas in such units from the tax.

5. Exemption for qualifying cogenerators

Section 109 of ESECA, as amended by Title I of H.R. 6831,[5] would allow the FEA to grant an exemption from mandatory conversion or prohibition orders if it is found that the economic and other benefits of co-generation are unobtainable unless petroleum or natural gas may be used in such a facility. A qualifying co-generation facility is one that produces electric energy and other forms of useful energy. Also, such a facility must meet requirements that the FEA might specify and must offer each electric utility to which such facility would be directly connected an opportunity to operate it on terms which are agreed to by the parties. If an exemption is granted under this section, the committee bill exempts the use of oil and gas at this facility from taxation so that the energy benefits of cogeneration would not be discouraged.

6. Discretionary exemptions and reclassification

The committee bill also provides a procedure to allow individual firms to ask the Secretary to reclassify all or part of their use of oil and natural gas into a Tier taxed at a lower rate or to exempt any such use from the tax entirely, regardless of the Tier into which such use is classified in the bill.

In considering such requests, the Secretary is to take into account the potential for conversion or conservation in the use of oil and natural gas and would also consider environmental, economic, as well as technological factors relevant to the individual case.

For example, if the Secretary determined that for an individual firm or plant or type of use within a plant, that there was no significant potential for reducing oil or gas use (through conservation or conversion), then this use could be exempted from the tax (or moved to a lower tier.) For example, a mining facility too remote to allow economical transportation of coal and which had boilers which did not have conservation potential might be considered by the Secretary for reclassification.

[5] Under this bill as introduced.

On the other hand, most firms building new facilities (not covered by one of the specific exemptions discussed above) would be expected to take account of the tax before erecting the new facilities. For example, if in 1979, a firm builds an oil-fired boiler, it could not in 1980 claim an exemption simply because it would be uneconomical to replace a 1-year old boiler. The firm in question would be expected to know that its use of oil in the new facility would be subject to tax.

Similarly, the Secretary could take into account normal business practice is assessing the merits of such requests. A utility could not claim exemptions for all its "peak-load" power plants, for example, if the Secretary determined that the utility had more such plants than were necessary to meet the pattern of electricity demand in the region served by the utility.

D. Authority To Suspend Tax

The committee bill provides that if a situation arises in which the President determines that this tax would have an adverse economic effect, the President is to have the authority to submit to the Congress a plan for the suspension of this tax, or the tax on any classification of use, for up to one year. This plan would have to describe the considerations which caused the President to propose the suspension. The suspension would take place only if neither House of Congress adopts a resolution of disapproval within 15 days of its submission.

2. Credit Against Tax on Business Use of Oil and Natural Gas (Sec. 2051 of the bill and secs. 4996, 4997, 4998 and 4999 of the Code)

Explanation of provision

In general

The bill provides a credit for investments in qualifying alternative energy property which may be offset directly against the oil and gas consumption tax liability. The credit generally is an amount equal to The credit is limited to the user tax liability for the calendar year,

Qualified energy investment generally is the cost of alternative energy property, referred to as "section 4996 property" placed in service by the taxpayer during the calendar year together with the qualified progress expenditures for such property during the year.

The credit is limited to the user tax liability for the calendar year, but any excess investment may be carried forward and treated as qualified energy investment for the following calendar year.

As discussed in more detail below, the taxpayer is generally required to elect to take this credit, or an increased investment credit on his qualified energy equipment.

Of course, where a credit for the tax is allowed, no income tax deduction is available for the amount of the tax which was offset by the credit.

Alternative energy property

A credit for investments in qualified alternative energy property (referred to as section 4996 property in the bill) may be claimed against liability for the oil and gas users tax. Generally, the credit is allowed against investments in property which either directly (for example, coal-fired boilers) or indirectly (for example, certain pollution control equipment) relate to the installation by industrial firms and electric utilities of equipment or facilities that will make possible shifts from oil and natural gas to other fuels.

All property that qualifies for the credit must fulfill five general criteria, some of which parallel certain basic qualifications for the regular investment tax credit. The bill requires that the alternative energy property be tangible property—

(1) which is used by the taxpayer in the taxpayer's trade or business,

(2) for which depreciation (or amortization) is allowable,

(3) which has a useful life of 3 years or more,

(4) which is not used predominantly outside the United States, and

(5) which is new property.

The bill expressly excludes buildings and the structural components of buildings from eligibility for the credit against the users tax. Property used in the trade or business of leasing is also ineligible for the credit.

The bill requires that the determination of the useful life of property be made as of the time the particular property is placed in service. Determinations that property is not used predominantly outside the United States must be made in a manner similar to the method of making such determinations for purposes of the same requirement in the regular investment credit under subparagraphs (A) and (B) of Code section 48(a)(2). The general rule reflected in the regulations issued under these subparagraphs provides that property which is physically located outside the United States during more than 50 percent of the taxable year is considered to be used predominantly outside the United States during that year. Limited statutory exceptions, principally applicable to property used in transportation or communications, permit some property used predominantly outside the United States to qualify for the regular investment tax credit, and therefore for this special credit as well.

The definition of new property hinges on the date, April 20, 1977, which was the day when the President publicly announced his legislative energy proposals. The term new property covers two categories of property. The first is property whose construction, reconstruction, or erection is completed by the taxpayer on or after April 20, 1977. In determining the credit for this first category of new property, the taxpayer may take into account only the portion of the property's basis which is properly attributable to construction, reconstruction, or erection on or after April 20, 1977. The second category of new property is property acquired by the taxpayer on or after April 20, 1977, provided that the property's original use begins with the taxpayer and that this use begins on or after April 20, 1977.

In general, alternative energy property is defined as specific types of equipment whose primary fuel is an alternate substance, that is a fuel other than oil, natural gas or their products, or as equipment designed to use fuels other than oil, natural gas or their products, particularly equipment related to using coal as a fuel. Alternative energy property specifically includes the following six general types of property.

(1) *Boilers.*—A boiler which uses an alternate substance, that is any substance other than oil, natural gas or oil and natural gas products, as its primary fuel (i.e., more than 50 percent) is the first type of alternative energy property. Equipment used to modify an existing boiler so that the primary fuel would be an alternate substance would also qualify as alternative energy property.

For this purpose, oil means crude oil, refined petroleum products, and natural gas liquids. Natural gas, gasoline, and substances not generally marketable for use as a fuel are not considered oil. Natural gas means natural gas, petroleum, or a natural gas or petroleum product, provided that the natural gas, petroleum, or one of their products, has an API gravity (i.e., relative density of oil to water) of 110 or more. Substances not generally marketable for use as a fuel are not considered natural gas.

Equipment used to modify existing equipment that is used in existing electric generating facilities may be eligible for a partial credit, if the existing boiler in the facility uses a mixture of oil or natural

gas and an alternative substance after the modification, even though oil or natural gas continues to be its primary fuel. The alternative substance must provide at least 25 percent and not more than 50 percent of the total fuel used by the boiler. In order to qualify as as existing boiler or existing facility, 50 percent or more of the basis of the boiler or facility, respectively must be attributable to construction, reconstruction, or erection before April 20, 1977. Boilers qualifying for the partial credit are called qualified oil-alternative substance boilers. The procedures used to compute the partial credit are discussed below in the section, Other rules.

(2) *Burners.*—A burner for a combustor (other than a boiler) can also be treated as alternative energy property, if the primary fuel for the burner will be an alternate substance or a combination. The eligible investment includes equipment which is located on-site at the burner and which is necessary to bring the alternate substance to the burner. Among the burners within this category are burners for a lime kiln or cement kiln which use an alternate substance as a fuel.

(3) *Advanced technology equipment.*—Advanced technology equipment includes equipment used to produce energy nuclear, hydroelectric, or geothermal power. The definition of this type of alternative energy property does not include the fuel, the turbines, nor any equipment beyond the turbine stage. In a nuclear power plant, for example, eligible equipment would be limited to the nuclear steam supply system.

(4) *Gasification equipment.*—The definition of alternative energy property also covers investments in equipment for converting any substance other than oil, natural gas, and products of oil and natural gas into synthetic gas.

(5) *Pollution control equipment.*—The credit against user tax liability is also available for pollution control equipment, such as scrubbers and electrostatic precipitators, which Federal, State or local governmental regulations require to be installed on or in connection with a boiler, a burner, or gasification equipment which itself qualifies as alternative energy property. The credit, however, does not apply to any equipment which is installed on or in connection with property which, as of April 20, 1977, was using coal, and was required to be installed by Federal, State, or local governmental regulations in effect on April 20, 1977.

(6) *Handling equipment.*—Equipment used for the unloading, transfer, storage, reclaiming from storage, and preparation (including washing, crushing, drying, and weighing at the point of use) of a fuel other than oil, gas, and their products qualifies as alternative energy property, if the fuel is to be used in other types of alternative energy property, i.e., a boiler, a burner, advanced technology equipment, gasification equipment, or pollution control equipment which itself qualifies for the credit. Handling equipment is also treated as alternative energy property, if it is used in a facility which uses coal as a feedstock to manufacture chemicals or other products (except coke). No equipment for the transportation of fuel to the site of its use is covered by this provision. Thus, for example, coal slurry pipelines and railroad cars would not qualify for the users tax credit.

(7) *Plans and designs.*—Alternative energy property includes the costs of the plans and designs for boilers, burners, advanced technology equipment, gasification equipment, pollution control equipment, and handling equipment which themselves constitute alternative energy property.

Period covered by credit

In determining the amount of the credit, property will be treated as placed in service under the rules which apply to the regular investment tax credit. In addition, qualified progress expenditures are to be taken into account under rules similar to the rules under the regular investment tax credit relating to qualified progress expenditures. These expenditures are to be taken into account only where the taxpayer, including a taxpayer who is exempt from the income tax, elects to treat "qualified progress expenditures" as a part of the base for which he can claim a credit against the users tax.

No credit shall be allowed for any calendar year after 1990 except to the extent of any carryovers arising from qualifying investments made in years prior to 1991 and for expenditures for property the physical construction, reconstruction or erection of which began before January 1, 1991.

Credit limited to users tax

The credit for any calendar year is limited to the users tax for that year. However, because of the large lead time required in certain cases to make qualifying energy investments, the bill provides that the users tax for 1979 and for 1980 (including any tax carried forward from 1979) in excess of the qualified energy investment for each such year may be carried forward and treated as a users tax imposed in the following year. Where any credit is allowed in 1980 or 1981 solely as a result of the tax carryover from the previous year, the credit so allowed shall be treated as an overpayment and shall be refunded or credited to the taxpayer under the usual rules relating to overpayments. In addition, the amount of the overpayment is to be included in taxable income.

Rules concerning elections

The credit against the users tax is allowed only where the taxpayer has made an election pursuant to section 4999(a) between the users tax credit or the energy tax credit discussed below. The election must be made on the taxpayer's income tax return for his first taxable year ending after December 31, 1978 in which the taxpayer has qualified energy investment. Once an election is made, it applies to all taxable years. It may be revoked only with the consent of the Secretary or his delegate. The election shall be effective for all qualified energy investment made by the taxpayer.

Where the taxpayer has made an election to take the credit against the users tax with respect to any qualifying energy investment, the property shall not be treated as qualified property for purposes of the investment credit under section 38. Thus, no energy investment credit against the income tax will be allowed, and the regular investment credit will be allowed only to the extent that the current year's invest-

ment exceeds the users tax, and only if the taxpayer elects to forego any carryover against the users tax.

Because utilities are not subject to the users tax until 1983 (and therefore have no tax against which to credit their qualified energy investment), a regulated public utility has until its first taxable year ending after December 31, 1982 in which it has qualifying energy investment to make the election. Where a utility which elects the users credit had claimed the investment credit against its income tax for qualifying energy investment for years prior to the year for which the election is made, its income tax for the taxable year in which the election is made shall be increased by recapturing in full its investment credit (both regular and energy percentages) for all qualifying energy investment claimed in prior years. In this situation, the investment credit carrybacks and carryovers shall be adjusted under the usual adjustment rules of section 47(a)(4) of the code. Thus, under this approach a utility may claim the investment credit for taxable years ending on or before December 31, 1982, and then for its first taxable year ending after December 31, 1982, it may elect the credit against the users tax for all these investments. However, it will then be subject to a full recapture of the investment credit for these expenditures.

In the case of trades or businesses under common control, the amount of the credit shall be determined on the basis of the tax and credit for the entire group. Thus, the tax and the investments of the entire group are to be taken into account, and the investments of one taxpayer of the group may be offset against the tax of another member. However, in order to offset the investment of one member of a group against the tax of another member, a consolidated users tax return must be filed. The Secretary of the Treasury shall prescribe by regulation rules for making a consolidated users tax return.

Since all entities under common control are treated as one taxpayer for purposes of applying the users tax credit, an election will be effective for all members of the group under common control. Where any entity in the controlled group makes the election under section 4999(a), the election shall be effective for all entities in the group. Where entities with inconsistent elections become related, the Secretary or his delegate shall prescribe rules for the treatment of the related entities. In addition, where any taxpayer is not required to file an income tax return, the Secretary or his delegate shall provide the time and manner for making the election.

For purposes of these rules, taxpayers under common control include all members of the same controlled group of corporations, as that term is defined in section 1563, but with a 50-percent control test (instead of 80 percent), together with other entities whether or not incorporated, which are under common control. The Secretary shall prescribe rules consistent with the principles of section 1563 in applying the control test.

Recapture

The bill provides rules similar to the rules of the regular investment credit providing for a recapture of the credit where qualifying property is disposed of or ceases to be qualifying property within 7 years from the time the property is placed in service by the taxpayer.

The recapture is phased down so that where property is held 3 years or more but less than 5 years, only two-thirds of the credit is recaptured and where property is held 5 years or more but less than 7 years, only one-third of the credit is recaptured. The Secretary is to prescribe rules similar to the rules under section 47 for the treatment of property which ceases to be progress expenditure property and to adjust the credit carryovers. Any increase in the users tax by reason of a disposition shall be available to be offset by the credit from other qualifying energy investment.

Other rules

Special rules for utilities.—In the case of a regulated public utility (as defined in section 7701(a)(33)) whose principal activity is the sale of electricity, a credit shall be allowed for a boiler only to the extent that a boiler, which was in existence on April 20, 1977, and used oil or natural gas as its primary fuel on that date, is replaced or phased down. A boiler shall be treated as phased down only where the boiler was used more than 1500 hours in 1976 and will not be used more than 1500 hours in any year following the year in which the new boiler is placed in service (or after 1983 where the new boiler was placed in service before 1983).

The determination of the extent to which an oil boiler is replaced or phased down shall be on the basis of its capacity in terms of megawatts. For example, if a new boiler with a capacity of 80 megawatts is placed in service and a boiler with a capacity of 20 megawatts is phased down, 25 percent of the qualified energy investment with regard to the new boiler shall be taken into account in computing the credit. Where an oil boiler is converted into a boiler using an alternate substance, the replacement rule shall be considered satisfied, but the modified boiler shall not be treated as an eligible "old boiler" in the event it is subsequently replaced.

The bill allows utilities to treat qualified progress expenditures as qualifying investment for any calendar year where the utility certifies to the Secretary or his delegate that the eventual replacement or phase-down of the old boiler will occur in the year following the year in which the new boiler is placed in service, provided the new boiler is to be placed in service within 3 years after the end of the first year for which the certification is effective. In addition, the taxpayer must agree to a reasonable extension of the period of limitations for assessing any additional users tax which may be due in the event the replacement or phase-down does not in fact occur in accordance with the certification.

Further, the bill provides that where a taxpayer has treated a new boiler as qualifying investment and subsequently the phased down boiler is used more than 1500 hours but not more than 2000 hours (measured on the basis of use at full capacity and excluding any use when petroleum products are not consumed), the taxpayers' users tax on the oil or gas used in the additional hours shall be double the normal users tax. In the case of oil, the tax would be $3 per barrel ($1.50 regular tax and $1.50 additional tax). The additional tax would not be eligible for the rebate and could not be reduced by reason of the 50,000 barrel exempt amount (discussed above in connec-

tion with the tax). Where the phased-down boiler was used more than 2000 hours, the new boiler is to be treated as having been disposed of in the year in which that excess use occurs and the normal disposition rules will apply. Where a utility runs a boiler solely to keep it in operating condition, it is not to be considered as having used the boiler for purposes of applying this provision.

The committee does not intend the penalty tax or the recapture provision for utilities to apply in circumstances where the utility is prevented from using the replacement boiler by an act of God, a strike which prevents delivery of coal to the replacement facility, or damage by storm, fire or flood, etc., to the replacement facility. Therefore, to the extent practicable, the committee anticipates that the Secretary will prescribe regulations suspending applicability of the penalty tax and the recapture provision during periods when the utility is unable to comply with the phase-down requirement because of these circumstances.

In addition, where a facility was in existence or under construction on April 20, 1977 and on that date (1) it was contemplated that the facility would include one or more boilers which would use oil or gas as its primary fuel or (2) the facility did include one or more such boilers, and after April 20, 1977, the construction of such boiler or boilers is modified to use a primary fuel other than oil or gas, any boiler so modified will be treated as having replaced an existing boiler and will therefore be eligible to be treated as qualified energy investment.

With regard to the treatment of the credit for ratemaking purposes, the bill provides that rules similar to the existing rules under section 46(f) relating to the investment credit shall apply. The Secretary or his delegate is to prescribe rules to carry out the purposes of this provision including rules with respect to the time and manner of making elections similar to the elections described in section 46(f).

Industrial development bonds.—Where the qualified energy investment is financed by the proceeds of any industrial development bond, the interest on which is tax exempt by reason of section 103, only 50 percent of the investment is to be taken into account in determining the amount of the credit against the users tax.

Special rule for boilers which use mixtures.—In the case of a qualified oil-alternative substance boiler which uses a fuel mixture of oil and an alternate substance, such as coal, the credit shall be allowed only to the extent of the "oil savings percentage". This percentage is the lesser of two percentages.

The first percentage is the percentage derived from a fraction, the numerator of which is the non-oil or gas energy measured in BTUs which will be supplied to the boiler as a direct result of the modification in the normal course of operations and the denominator is the total energy so supplied.

The other percentage is the one derived from a fraction, the numerator of which is the decrease in oil and gas energy used by the boiler, as a direct result of the modification, over a period of time of normal use over the life of the boiler and denominator of which is the oil and gas energy which would have been used in the boilers over the same period of time if no modification had been made.

Thus, if a taxpayer modifies an existing oil boiler to burn a mixture of coal and oil which normally will consist of 40 percent coal and 60 percent oil, and as a result of the modification, the use of oil will decrease by 35 percent, the "oil savings percentage" will be 35 percent—the lesser of 35 percent (35/100) or 40 percent (40/100).

Under these rules, only a decrease in oil and natural gas use resulting from the modification is taken into account; any decrease resulting from reduced use of the boiler will not be taken into consideration.

Effective date

The tax applies to uses of oil and natural gas after December 31, 1978. The credit against the tax is available for qualified investment made on or after April 20, 1977.

Revenue effect

The business use tax and credit offset is estimated to increase net budget receipts by $383 million in fiscal year 1980, by $99 million in fiscal year 1981, and by $633 million in fiscal year 1985. (See table 4 in part IV.B for more details on the estimated budget effects.)

Energy Savings Estimate of Business Use Tax and Energy Tax Credits

It is estimated that as a result of the taxes on business use of oil and natural gas, and the related rebate and energy investment tax credits, consumption of natural gas and oil will be reduced by the equivalent of from 580,000 to 850,000 barrels per day in 1985. This estimate does not take account of the coal conversion provisions of Title I of this bill, and if these provisions are enacted, the additional savings from the business use tax and credits would be lower.

E. BUSINESS ENERGY CONSERVATION, CONVERSION AND ADVANCED TECHNOLOGY TAX CREDITS AND DEPRECIATION CHANGES

Present Law

Investment tax credit

Under present law, an investment tax credit of 10 percent (which reverts to 7 percent after 1980) is allowed generally for tangible personal property which is placed in service in a trade or business. (The credit can be as high as 11½ percent for corporations with qualified employee stock ownership plans.) However, structural components of buildings, including insulation, storm windows and doors, solar energy equipment, etc., generally do not qualify for the credit. Otherwise eligible property placed in service in hotels and other businesses which cater to transients is eligible for the investment credit, but property placed in service in hotels and apartments which have predominantly permanent residents does not qualify for the credit.

The investment credit is also allowed for tangible property (other than buildings or their structural components) which is used in manufacturing, production, extraction, or as an integral part of furnishing transportation, communications, or electrical, gas, or other utility services, even though such tangible property may otherwise be considered real (and not personal) property under local law.

The extent to which the investment credit is available depends upon the estimated useful life used to depreciate or amortize the property for tax purposes. The determination of the useful life is made at the time the property is placed in service. No investment credit is allowed if the property has an estimated useful life of less than 3 years. Where the useful life is greater than 3 years but less than 5 years, the investment credit is allowed on one-third of the taxpayer's cost for the property; if the useful life of the property is greater than 5 years but less than 7 years, the credit is allowed on two-thirds of the cost, and the credit is allowed on the entire cost where the property has a useful life of 7 years or more. If the property on which the investment credit was claimed is later sold or otherwise ceases to be qualified property for the taxpayer before the end of its estimated useful life, the credit may be partially or entirely recaptured to reflect the taxpayer's reduced holding period.

Generally, the amount of the investment credit a taxpayer may apply against his income tax liability in any one year cannot exceed the first $25,000 of tax liability plus 50 percent of the tax liability in excess of $25,000. Special limitations have been provided for public utility property, under which the 50 percent limit was increased to 100 percent for 1975 and 1976, and is 90 percent for 1977, after which it declines by 10 percentage points in each succeeding year until it returns to the generally applicable 50-percent limit in 1981. Similar

increases in the tax liability limitation are available (under the Tax Reform Act of 1976) to railroads and airlines, which are allowed to apply their investment credits against 100 percent of their tax liability for 1977 and 1978, and the limitation is reduced by 10 percentage points in each subsequent year until it returns to 50 percent in 1983.

Investment tax credits are not refundable. However, credits which are not applied against tax liability in the year they are earned may be carried back for 3 taxable years and carried forward for 7 years. In applying credits against tax liability for a particular tax year, the first-in first-out method is generally required, under which the credits earned in prior tax years are applied first, then the credits earned in the current year or later years are used.

Depreciation and amortization

Present law also allows taxpayers to claim tax deductions for the decline in value of assets used in a trade or business or for the production of income. These depreciation or amortization deductions are to reflect the reduction in the taxpayer's cost basis in the property due to use of the property and obsolescence.

Items of property which qualify as depreciable or amortizable property include buildings, machinery and equipment. Land is not depreciable, but a real property interest may be allowed depletion, if it is subject to mining of natural resources or oil and natural gas production.

The taxpayer may claim depreciation deductions over the period which is the estimated useful life of the particular property. The estimated remaining useful life generally may be redetermined during the life of the asset where the change in useful life is significant and there is a clear basis for the redetermination.

Present law authorizes the use of the straight-line method of depreciation (under which depreciation deductions are claimed ratably over the useful life of the asset) or one of several accelerated methods, such as the double declining balance and sum-of-the-years' digits methods, under which deductions in the early years of the useful life are substantially greater than those available under the straight-line method.

In order to reduce uncertainty about the proper useful lives for depreciation of business and productive assets, the Congress has approved the class life asset depreciation range system (ADR). Under ADR, specified asset depreciation periods are used to compute depreciation for classes of assets covered by these rules. A taxpayer who elects this system is entitled to use depreciation periods which are within a range of 20 percent higher or lower than the regular ADR class lives. Special rules apply where assets under the ADR system are retired before the end of the depreciation period; for example, a loss from an ordinary retirement of an asset may not be deducted in the year the asset is retired.

In lieu of depreciation deductions which would otherwise be allowable, the owners of certain types of assets may elect to amortize these assets on a straight-line basis over a period which is usually substantially shorter than the actual useful life of the asset. This special treatment is available for certain pollution control equipment, which

may be amortized over a 60-month period. If this election is made, only one-half of the regular investment tax credit is allowed.

Industrial development bonds

Under present law, the interest income derived from obligations of a State or local government generally is exempt from Federal income tax. This rule does not extend to industrial development bonds whose proceeds are used by a taxpaying enterprise in its trade or business, except for those situations where the proceeds of the bonds are used by a taxpaying enterprise for specified exempt purposes. Exceptions have been provided where the proceeds are used to acquire or construct solid waste disposal facilities, and air or water pollution control facilities.

Reasons for Change

In reviewing the use of energy by the various sectors of the economy, the committee was informed that in 1975, industry used 20.5 quadrillion Btu's, or 36 percent of the total 56.5 quadrillion Btu's consumed for all purposes. The committee noted that industry has relied increasingly on oil and natural gas in the past two decades, rather than on coal, and that conservative use of all energy sources has been a rare practice. In view of the vulnerability of the economy to possible disruptions in the supply of natural gas and oil, and in view of potential savings of oil and gas through more prudent use, the committee believes it is essential to encourage industry to conserve oil and natural gas and to convert, when economically and technically feasible, to sources of energy other than oil and natural gas. Accordingly, the committee has provided for a limited period of time, a series of tax credits which are designed to encourage conservation and conversion and the development of advanced energy technology.

Consistent with these objectives, the committee bill denies the regular investment tax credit and accelerated depreciation methods for the purchase of new oil or natural gas fueled boilers and combustors which are not exempt from the oil and natural gas user taxes. The committee believes that in providing a positive incentive for conversion and conservation in the form of additional tax credits, and a disincentive in the form of the denial of certain current tax advantages, industry will be motivated to make significant efforts to conserve its use of scarce oil and natural gas as well as to convert to other forms of fuel.

Explanation of Provision

A. Business Energy Credits

1. In general.

In order to encourage greater use of energy sources other than oil and natural gas and to increase energy conservation by business, the bill provides a special investment tax credit that is in addition to the regular investment tax credit, for a limited period of time.

The business energy credit is available at a rate of 10 percent for certain types of property, called energy property, during the period after April 19, 1977, and before January 1, 1983. If eligible property is constructed by the taxpayer, the business energy credit will

be available only if construction is completed during the period after April 19, 1977, and before January 1, 1983, and only to the extent of costs incurred during this period. If the taxpayer makes progress expenditures and elects to claim this credit for the progress expenditures, the credit is available only to the extent of progress expenditures made during this period. Property purchased by the taxpayer must be both acquired and placed in service during this period.

2. Rules of general application

The committee's bill adds this business energy credit to the regular investment credit provisions. (Eligibility for the special energy credit under this provision, however, does not affect the eligibility of the property for the regular investment credit under present law.) As a result, the rules for applying the regular investment credit will also generally apply to the business energy investment credit. For example, business energy credits will be absorbed using the first in-first out (FIFO) rules which apply to the regular investment credit. Business energy credits may also be carried back for three years and carried forward for seven years, as is the case with the regular investment credit.

Several changes to the regular investment credit rules are made, however, for purposes of applying the business energy investment credit. First, the business energy credit for alternative energy property (for which the credit against the use tax has not been elected) may be offset against 100 percent of the taxpayer's income tax liability, rather than the generally applicable limitation of 50 percent of tax liability (in excess of $25,000). This increased limitation applies only to alternative energy property; it does not apply to the other categories of property eligible for the business energy credit. The 100 percent limitaton also will be available for carrybacks and carry forwards of credits attributable to alternative energy property, including those carried to tax years before 1977 and after 1982.

A second change to the generally applicable investment credit rules involves the elimination of the lodging limitation (sec. 48(a)(3)) for purposes of the business energy credit. As a result, the business energy credit is available both for energy property installed in connection with a lodging facility which provides accommodations to transients (for which the regular investment credit may be claimed for qualifying property under present law) and for energy property installed in connection with facilities (such as apartment houses) which predominantly provide long-term accommodations (for which the regular investment credit is generally not available under present law).

A special rule is also provided for energy property that is partially or entirely financed by industrial development bonds, whose interest is exempt from Federal income tax under present law. In this situation, the business energy credit will be 5 percent, instead of the 10 percent rate which is generally available.

For the purposes of the business energy credits, the term industrial includes agricultural to reflect the committee's intent that energy property used in connection with an agricultural operation or process also will qualify for the energy investment credit.

3. *Energy property defined*

In order to qualify as business energy property eligible for this special investment credit, the property must fall within one of the following five categories: (1) alternative energy property for which the credit against the oil and natural gas use tax has not been elected, (2) cogeneration property, (3) advanced technology property, (4) specially defined energy property, and (5) recycling equipment. These categories are explained in detail below.

To qualify as energy property, the property must be an integral part of, or used in connection with, a building or other structure located in the United States. Where the taxpayer is constructing the energy property, construction, reconstruction or erection must be completed after April 19, 1977. Similarly, property purchased by the taxpayer must be acquired after April 19, 1977, and its original use must be by the taxpayer and must begin after April 19, 1977. (As already noted, the credit is available only to the extent of costs incurred after this date and before January 1, 1983.) In addition, the property must be property for which depreciation or amortization is allowable and must have a useful life of three years or more.

For purposes of determining the eligibility of cogenerating property, advanced technology property and specially defined energy property for the energy investment credit, it is generally required that this property or equipment be used in connection with an existing building and, where applicable, an existing industrial or commercial process, as of April 20, 1977.

Except in the case of nuclear facilities, a building or facility will be considered to be existing, if it has been substantially completed before April 20, 1977; that is, at least 50 percent of the taxpayer's basis in the building or facility must be attributable to construction, reconstruction, or erection which occurred before April 20, 1977. In the case of nuclear powerplants, the facility will be considered an existing building or facility if a construction permit was issued and construction had actually begun by April 19, 1977.

For all categories of energy property other than alternative energy property, this credit will be available only if the equipment meets performance and quality standards (relating to energy savings) prescribed by the Secretary (after consultation with the Secretary of Energy) which are in effect at the time the property is acquired or construction is begun.

If property qualifies as both alternative energy property or as one of the other categories of energy property, it will be treated as alternative energy property eligible either for the credit against the use tax or this business energy investment credit, at the election of the taxayer.

4. *Alternative energy property*

The term energy property is defined to include alternative energy property. This category refers to property which is defined as alternative energy property under section 4998(b) but with respect to which the credit against the business use tax has not been elected. The types of property which are included within the meaning of alternative energy property are boilers, burners, advanced technology equipment, equipment to produce synthetic gas, pollution control equipment,

and handling equipment to be used in conjunction with other types of alternative energy property, as well as the plans and designs for such alternative energy property. A detailed explanation of alternative energy property appears above in the explanation of the credit against the tax on the business use of oil and natural gas.

If an election is made under section 4999(a) to claim a credit of the oil and natural gas use tax for all or part of taxpayer's investment in alternative energy property, the business energy credit will not be available for any of the investment, including that portion which is not offset by the use tax credit. However, the regular investment credit will be available for that part of the investment which is not offset by the use tax credit, to the extent that this property would be eligible for the regular investment credit under present law.

If the taxpayer is a regulated electric utility, the business energy credit for alternative energy property (if this rather than the use tax credit is elected) will be allowed for a new boiler only to the extent that an existing oil or natural gas fueled boiler (as of April 20, 1977) is replaced or phased down. Similar rules are provided under the use tax credit for these situations. The rules used to apply the use tax credit to the electric utility phasedown or replacement of a boiler are extended, by reference, to the business energy credit.

5. Cogeneration property

To qualify as energy property, cogeneration property must be installed in connection with an existing facility and must result in an expansion in the facility's cogenerating capacity (including the start of cogenerating activity). Under the bill, cogeneration property means property which produces steam, heat, or some other form of useful energy, (other than electricity) for industrial, commercial, or space heating purposes, and which also produces electricity.

In this context, cogeneration equipment includes the addition of equipment to produce or distribute steam, heat, or other energy from an existing electric generating facility and also the electrical generating equipment which is added to an existing boiler or other energy production or conversion system which produces steam or another form of energy other than electricity.

It is intended that cogeneration property include steam and heat distribution systems that are added to an existing electric generating facility. In addition, it covers an electrical generating turbine which is added to an existing industrial or commercial boiler or other heat-producing source.

Where a taxpayer has an operational cogenerating capacity in place on April 20, 1977, the credit will be available only to the extent that additional or replacement cogeneration equipment increases the cogenerating capacity of the facility. For this purpose, the eligible investment is determined from either the incremental capacity (in terms of megawatts) to produce electricity or the incremental capacity to produce steam (in terms of pounds per hour) or other forms of heat.

6. Advanced technology property

Advanced technology property is defined as equipment which uses solar, geothermal or wind energy to provide heat, cooling or electricity

in connection with an existing industrial or commercial building, and where applicable, an existing industrial process.

In the case of solar and wind energy equipment, the credit applies to such equipment (and parts solely related to the functioning of such equipment) which use solar and wind energy (either separately or to supplement each other) to provide heat, cooling, hot water or electricity. Generally, a solar energy equipment system involves the transformation of sunlight into heat or electricity through the use of such devices as solar cells or other collectors, storage systems for electricity and for hot air or hot water (including rock beds), heat exchangers to utilize captured and stored energy, and related equipment, such as fans and thermostats. The credit for wind equipment similarly applies to the windmill or other devices to harness outdoor moving air to provide electricity and other forms of energy and includes storage and transfer systems to distribute this energy.

The credit for geothermal equipment includes equipment, such as turbines and steam distribution systems, used in connection with a building or structure. Eligible property in this category does not include either (1) any type of equipment connected with a geothermal well or (2) steam distribution systems between a geothermal well and the point at which the steam enters the building or structure or other facility which utilizes the steam for application within the building or structure. While the credit does cover geothermal steam distribution systems within a building, it does not cover electrical distribution systems except for those which are integrally related to a geothermal steam powered generating turbine.

7. Specifically defined energy property

This category of eligible property generally consists of equipment added to an existing building or process to conserve energy by recovering and further utilizing heat or unburned gases which would otherwise be wasted and which are contained in gases and fluids. Eligible property includes:

(1) recuperators, which are configurations of equipment which consist in part of fixed heat transfer surfaces between two gas flows and which are used to recover energy, usually in the form of waste heat, from combustion exhaust gases in order to preheat incoming combustion air;

(2) heat wheels, which are items of equipment consisting, in part, of regenerators which rotate through two gas flows and which are used to recover energy, usually in the form of waste heat, from exhaust gases to preheat incoming gases;

(3) regenerators, which are devices used to recover energy by efficiently storing heat while exposed to high temperature gases and then releasing heat when exposed to low temperature gases;

(4) heat exchangers, which are equipment consisting, in part, of fixed heat transfer surfaces separating two fluids which are used to recover energy, usually in the form of waste heat, from high temperature fluids of industrial processes for transfer to low temperature fluids;

(5) waste heat boilers, which are boilers that use waste heat, usually in the form of combustion exhaust gases, as a primary energy source;

(6) heat pipes, which are devices that consist, in part, of sealed heat transfer chambers containing a working fluid which is alternatively vaporized and condensed as it travels from one end of the chamber to the other and are used to recover energy, usually in the form of waste heat, from high temperature fluids to heat low temperature fluids;

(7) automatic energy control systems, which are equipment used to control energy usage for environmental space conditioning or for manufacturing processes in ways which automatically minimize such energy usage;

(8) turbulators, which are small baffles placed in the upper passes of the firetubes of boilers to increase the rate of transfer of heat from combustion gases to the firetube surface;

(9) preheaters, which are equipment that consists, in part, of a fixed heat transfer surface separating two fluids and are used to recover energy, usually in the form of waste heat from either combustion exhaust gases or steam, to preheat incoming combustion air or boiler feedwater;

(10) combustible gas recovery systems, which are equipment used to recover unburned fuel from combustion exhaust gases; and

(11) economizers, which are configurations of equipment used to recovery energy from combustion exhaust gases to preheat boiler feedwater.

In addition to these types of property, the Secretary is authorized to specify other similar items of energy conservation equipment eligible for this credit.

8. Additional equipment

Additional eligible items of specially defined energy property include equipment added to existing industrial or commercial facilities which burn oil or natural gas, or use oil or natural gas as a feedstock, to modify these facilities to use coal, waste (such as biomass) or other combustible by-products as a fuel or feedstock in replacement of at least 25 percent of the oil or natural gas used before the modification. This credit will be available where the use of an alternate fuel or feedstock is at least 25 percent but not more than 50 percent. In the case of equipment that uses the mixture as a fuel (but not as a feedstock), this equipment will be treated as alternative energy property eligible either for the credit against the use tax or the energy tax credit, if the alternate fuel comprises more than 50 percent of the energy consumed. Qualifying investment in this category would include the costs of replacing or modifying existing combustors and burners to enable the facility to use this fuel mixture. Related pollution control equipment (such as scrubbers and electrostatic precipitators) and handling equipment would also qualify under this category if these two types of property satisfy the relevant requirements set forth in section 4998(b), concerning pollution control equipment and handling equipment which qualify as alternative energy property.

9. Recycling equipment

The final category of property which qualifies for the energy investment credit is equipment used to recycle solid waste. The credit here

is limited to solid waste recycling equipment because equipment to recover and recycle waste heat and gases is included under the specially defined energy property category.

Equipment covered under this category must be used exclusively for one of two purposes, either to sort or otherwise prepare solid waste for recycling or to process (recycle) the solid waste materials. This would include, for example, equipment which separates recyclable solid waste from a mixture of waste materials. Equipment which functions exclusively to prepare solid waste materials would also be covered. For example, processes which apply a thermal, mechanical or chemical treatment to waste to condition or prime the materials so they will respond properly to the recycling process are included. Equipment in the actual recycling function is also included up to the point where a refined material has been created which can be used to the same extent as materials from one or other virgin substances to fabricate an end product.

It is intended that eligible property in this category will include both equipment to recycle post-consumer waste materials (for example, cans and bottles that have been used by the consumer and recovered) and also industrial fabricating waste materials such as trimmings from a metal stamping process. It is also intended that on-site loading and transportation equipment which is integrally related to the sorting, preparation and recycling equipment should also be eligible for the credit. This would include, for example, equipment to load solid waste into a sorting or preparation machine and also a conveyor belt system which transports the solid waste materials from separation equipment to another machine in the recycling process. Such transportation equipment, as trucks, which transfer solid wastes between geographically separated sites, such as between collection points and recycling plants, will not be recycling equipment.

It should be emphasized that equipment will be eligible as recycling property only if it is capable of processing solely solid waste materials; the credit is not available where the equipment may also be used to process virgin materials. It is the capability of the equipment rather than its actual use that is the relevant factor for this determination.

Unlike the other categories of energy property which limit eligible equipment to that used in connection with existing structures and processes, the credit for recycling equipment is available where used in connection with a new building and industrial or commercial process. However, in order to prevent windfall benefits to taxpayers who are already engaged in recycling and who wish to replace their existing equipment in order to obtain this special investment credit, the committee intends that the credit be available only to the extent that the equipment results in an increase in the taxpayer's recycling capacity.

B. Investment Tax Credit for Business Insulation Property

Business insulation property which is a structural component of a building would be eligible for the regular investment tax credit, if placed in service during the period from April 20, 1977 through December 31, 1982. This provision applies to business insulation property that presently is not eligible for the investment tax credit. The criteria that are employed ordinarily to determine whether property is eligible

for the credit would apply to this property; for example, the property must have a useful life of at least 3 years, and partial credits are allowed for useful lives of 3 through 6 years.

Business insulation property is defined as property which is specifically and primarily designed to reduce the heat loss of gain of an existing commercial or industrial building or facility in or on which the insulation property is installed. In addition, such insulation must be new property, have a useful life of at least three years, and meet performance and quality standards prescribed in regulations by the Secretary of the Treasury after consultation with the Secretary of Energy. This regulatory authority is to be applied prospectively only, and thus, these standards will not apply to insulation property purchased prior to the promulgation of such standards.

Qualifying property includes not only insulation, but also a variety of other items designed to reduce heat loss or gain, including double glazing, reflective glass coatings, storm doors and windows, and weatherstripping.

To be qualified, business insulation property must be added on or in a building or facility which was in existence and placed in service before April 20, 1977. Expenditures for such insulation are to be treated as made when the installation of the insulation is completed. Accordingly, the time of payment or accrual of such expenditures is not to be taken into account in determining whether such expenditures qualify for the credit.

C. Denial of Investment Tax Credit and Accelerated Depreciation for Certain Property

Under the committee bill, several tax incentives would be repealed for new investments in certain energy property. In particular, the committee bill deletes air conditioning and space heating units (that is, those not considered structural components) from the definition of tangible personal property so that such property no longer will be eligible for the regular investment tax credit. Boilers or other combustors fueled by oil or natural gas also would be denied the regular (or any additional) investment tax credit, unless the use of coal or another alternate substance is precluded by existing Federal or State air pollution regulations, or unless the use of such a boiler or other combustor is an exempt use under sec. 4992(b) of the bill.

An exempt use of oil or natural gas is defined by sec. 4992(b) as a use in a residential facility, in transportation (including by pipeline), on a farm for farming purposes, in a shopping center, office building or wholesale or retail establishment, in any other facility which is not an integral part of manufacturing, processing or mining, or use in the exploration or development, extraction, transmission or storage of crude oil, natural gas, or natural gas liquids, and an exempt process use.

In addition, new oil or natural gas boilers would be required to use straight-line depreciation, rather than any accelerated depreciation method, and the useful life of such property must equal the class life prescribed by the Secretary, without regard to the 20 percent variance in class life available under sec. 167(m)(1) of the Code.

The denial of the investment tax credit would apply to property placed in service after June 20, 1977, but the denial would not apply to

property which is constructed, reconstructed, erected or acquired under the terms of a binding contract to which the taxpayer was a party on June 20, 1977, and at all times thereafter. This provision would pertain only to contracts in which the construction, reconstruction, erection, or acquisition of property is itself the subject matter of the contract and would not apply to a contract with a person other than the builder or supplier under which the taxpayer becomes obligated to construct, reconstruct, erect or acquire property. A contract which is binding on the taxpayer on June 19, 1977, would not be considered binding at all times thereafter if it is substantially modified after that date.

D. Depreciation Allowance for Early Retirement or Replacement of Oil or Gas Boilers

Special treatment is provided under the bill for depreciation of a natural gas or oil-fueled boiler or other combustor which is retired or replaced before the end of its originally determined useful life. The committee has concluded that this treatment will encourage early retirement of such facilities and is necessary because it is uncertain whether redeterminations of useful life may be used in some of these situations under present law.

Under this amendment, the taxpayer will be authorized to redetermine the useful life of an oil or natural gas fueled combustor and use this shortened useful life to depreciate the remaining basis in the property (net of any salvage value). If this treatment is elected, the taxpayer may use only the straight-line method for depreciation of the remaining basis. In order to qualify for this treatment, the taxpayer must establish to the satisfaction of the Secretary that there is a reasonable foundation for the conclusion that the combustor will in fact be retired or replaced at the end of the shortened useful life. The taxpayer will be eligible to use this treatment beginning with the taxable year in which the Secretary approves the application of the taxpayer to redetermine the useful life of the combustor under this provision.

In order to prevent abuse of this provision, it is intended that the allowance of a shortened depreciable period will not be available where the existing oil or gas fueled combustor will be replaced with another oil or gas fueled combustor.

For example, if a taxpayer had an oil-fueled boiler with 10 years of remaining life (out of a total use life of 20 years), and the taxpayer established to the satisfaction of the Secretary of the Treasury that the boiler would be retired in two years, the taxpayer would have available to him during those two years, as additional depreciation deductions, the remaining eight years of depreciation taken on a straight-line basis. In each of the two years, the taxpayer would be able to take as additional depreciation deductions the value of four of the eight remaining years straight-line depreciation.

If the taxpayer does not, however, retire or replace the boiler on or before the date established with the Secretary, he then is liable for the difference between the taxes he would otherwise have paid during the period and the taxes he actually paid. He must also pay interest, at a rate determined under section 6621, on the amount of the difference of such taxes. For example, suppose that a taxpayer has a boiler with

a useful life of 20 years and which has an initial basis of $1 million. Suppose also that in 1979 the taxpayer is in the tenth year of the useful life of the boiler and is using double declining balance depreciation. The taxpayer then establishes to the satisfaction of the Secretary that he will replace the boiler by the beginning of the 13th year of its useful life. Accordingly, the taxpayer would claim in years 11 and 12 additional depreciation of $80,400: the depreciation deduction that otherwise would be taken from year 13 through year 20 amounts to $160,800 and one-half of it ($80,400) may be deducted in each of the two years. If the taxpayer is in the 48-percent bracket, the additional depreciation deductions result in $38,592 less in tax in each of the two years. This reduction in tax represents the tax benefit to the taxpayer.

Were the taxpayer not to replace the boiler in year 13 as initially promised, he would have to recompute his taxes, and pay $77,184 in deficiencies as well as interest on the additional tax benefit. If the section 6621 interest rate is 9 percent, then he would owe $3,473 in interest in year 11 and $3,473 in year 12.

Effective dates

The business energy and insulation credit provisions generally will be effective for qualifying property placed in service after April 19, 1977, to the extent of expenditures incurred after that date. The denial of investment credit and depreciation limitation provisions will be effective for property placed in service after June 20, 1977, except for property under binding contracts in effect on that date. The provision concerning the redetermination of depreciable useful lives for oil and gas fueled boilers will be effective for taxable years ending after the date of enactment.

Revenue effect

The investment credit provisions will result in a net decrease in budget receipts of $681 million from fiscal year 1978 through fiscal year 1985. The credits for alternative energy conservation property will produce a decline in receipts of $3.3 billion through fiscal years 1978–83; the annual fiscal year loss will be $409 million in 1978, $415 million in 1979, $516 million in 1980, $673 million in 1981, $789 million in 1982, and $491 million in 1983.

Denial of the investment credit and accelerated depreciation for new oil and natural gas burners and boiler and air conditioning and space heaters will increase receipts by $822 million through fiscal years 1978 and 1985. The annual gain averages about $100 million each fiscal year.

The revenue effects are shown in greater detail in the tables in section IV of this report.

Energy savings estimate for business use tax and energy tax credits

It is estimated that, as a result of the energy investment tax credits, the taxes on business use of oil and natural gas and the credits against the use taxes, consumption of natural gas and oil will be reduced by the equivalent of 580,000 to 850,000 barrels per day in 1985.

F. ENERGY TAX INCENTIVES

1. Intangible drilling costs of oil and gas wells (sec. 2071 of the bill and sec. 57 of the Code)

Present law

Under present law, the operator of an oil or gas well may elect to deduct intangible drilling and development costs as an expense rather than capitalize the costs and recover them through depletion and depreciation deductions. Under the Tax Reform Act of 1976, the deduction for intangible drilling costs 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 is treated as a tax preference item for purposes of the minimum tax for individuals. Generally, intangible drilling and development costs are defined as those expenditures made by the owner of the operating interest for wages, fuel, repairs, hauling, supplies, etc., incurred in preparing a drill site, drilling and cleaning a well, and constructing assets which are necessary in drilling the well and preparing it for production (such as derricks, pipelines, and tanks).

In the Tax Reduction and Simplification Act of 1977, the Congress provided that for taxable years beginning only in 1977 intangible drilling and development costs (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. However, this rule would not apply for future years unless there is further Congressional action.

Reasons for change

The classification of certain intangible drilling expenses as a tax preference item under the minimum tax in order to curtail the use of oil and gas tax shelters resulted in a disincentive for increased exploration by individuals in the business of exploring for oil and gas and developing oil and gas properties. This disincentive has a significant impact, particularly on independent producers, who do most of the exploratory drilling for new oil in the United States.

The committee believes that by applying the preference only where intangible drilling costs exceed oil and gas production income the preference will not constitute a major disincentive to those individuals in the oil and gas business, but will continue to limit the ability of outside investors to reduce the income tax paid on their wage and salary income through the use of tax shelters.

Explanation of provision

The committee provision extends for all future years the minimum tax provision on intangible drilling costs of individuals currently applicable for 1977. As a result, intangible drilling cost deductions for oil or gas wells would be included in the minimum tax base of indi-

viduals only to the extent that intangible drilling and development costs, over the amount of those costs amortizable on the basis of a 10-year life or under cost depletion, exceed the taxpayer's income from oil and gas properties. Income from oil and gas properties is to be determined first with reference to the rules for determining gross income from oil and gas properties for purposes of percentage depletion (sec. 613(a) of the Code, without regard to the limitations under sec. 613A). Net income from oil and gas properties is gross income from oil and gas properties reduced by the amount of deductions properly attributable to that gross income (and deductions attributable to oil and gas properties with no gross income), except that no reduction is to be made for those intangible drilling costs subject to the minimum tax (i.e., those incurred on successful wells).

Effective date

These provisions are to be effective upon enactment and apply to taxable years ending after December 31, 1977.

Revenue effect

The provision limiting the minimum tax on intangible drilling costs for oil and gas to the amount in excess of net related income is estimated to reduce budget receipts by $19 million in fiscal 1978, $32 million in fiscal 1979, $37 million in fiscal 1980, and $74 million in 1985.

Energy savings estimate

There is no estimate of the increase in the supply of oil, gas, or geothermal energy which would result from the enactment of this provision.

2. Geothermal tax provisions (secs. 2072 and 2073 of the bill and secs. 57, 263, 465, 613, and 1254 of the Code)

Present law

Under current law, it is unsettled as to whether the production of geothermal steam and associated geothermal resources qualifies for either a percentage depletion deduction or the intangible drilling cost deduction. However, in *Reich* v. *Commissioner*, 454 F. 2d 1157 (9th Cir. 1972), aff'g, 52 T.C. 700 (1969), the court held that the production of geothermal steam entitled the taxpayer to both deductions to the extent that the deductions were available for gas wells.[1] Nevertheless, the Internal Revenue Service apparently is not following the *Reich* decision in cases arising outside of the Ninth Circuit.

Except in the case of certain small producers, the Tax Reduction Act of 1975 generally eliminated the depletion allowance for oil and gas. That Act, however, did not affect the issue of whether geothermal resources qualify for percentage depletion. As a result, the 22-percent depletion deduction allowable to gas wells immediately prior to the 1975 Tax Reduction Act still is available for geothermal energy if courts should decide, as did the *Reich* court, that certain geothermal wells are gas wells and that the other requirements for depletion are met.

Even if the decision of the *Reich* court is not followed, under present law expenditures incurred in connection with the exploratory phase of geothermal energy which result in dry holes are deductible at the time when the well (or leasehold) is abandoned. Moreover, to the extent that these costs result in new processes or technology, it is possible under present law that these costs would be considered to be research and experimental expenditures subject to the election to be deducted currently or to be amortized over a 60-month period. For example, in Revenue Ruling 74–67, 1974–1 C.B. 63, the Internal Revenue Service held that certain costs of developing a method for the hydraulic mining of hard minerals, including a portion of the cost of drilling wells, are deductible as research and experimental expenditures. However. under current law the costs of determining the existence. location, extent, or quality of any oil, gas, or other mineral deposit are not deductible as research and experimental expenditures, and must be capitalized.

[1] In the *Reich* case, the Tax Court had held that the product of the taxpayers' geothermal steam wells was a gas, and that the taxpayers as a result were entitled to expense currently their intangible drilling costs (sec. 263(c) of the Code). The court held further that the plaintiffs were entitled to the then 27½ percent depletion deduction allowance for their product because (1) their product was steam, not inexhaustible earth heat, (2) the particular geothermal wells in question were exhaustible, (3) steam is a gas, and (4) the exclusion from the right to depletion of "water" in section 613(b)(7) of the Code does not exclude steam from the depletion allowance.

To the extent that geothermal wells are determined to be gas wells, as they were by the *Reich* court, the minimum tax, the recapture provisions and the at risk rules which the Tax Reform Act of 1976 applied to oil and gas wells would apply to geothermal wells. Under the Tax Reform Act of 1976, the deduction for intangible drilling costs on oil and gas wells is treated as a tax preference item for purposes of the minimum tax to the extent that it exceeds the amortization which would have been allowed on the basis of a 10-year life or cost depletion. The Tax Reduction and Simplification Act of 1977 provided, however, that for taxable years beginning only in 1977 the excess of the intangible drilling and development costs, over the amount amortizable, which further exceeded oil and gas production income, would constitute a tax preference item. This bill (sec. 2071) extends the 1977 provision to future years.

The Tax Reform Act of 1976 also provided for the recapture of certain intangible drilling and development costs upon the disposition of oil and gas properties. The amount subject to recapture is the amount deducted for intangible drilling and development costs reduced by the amount which would have been deductible had those intangible costs been capitalized and deducted through cost depletion. The amount recaptured is to be treated as ordinary income; it cannot exceed the gain realized or the difference between the fair market value of the property transferred over the basis in the property. The recapture rule generally applies regardless of any other provision of the Code which otherwise would provide for nonrecognition and applies on a property-by-property basis.

In addition, the Tax Reform Act of 1976 provided that the amount of any loss (otherwise allowable for the year) which may be deducted in connection with exploring for, or exploiting, oil and gas resources cannot exceed the aggregate amount with respect to which the taxpayer is at risk with respect to the property at the close of the taxable year (i.e., generally the amount of an otherwise allowable loss for the year cannot exceed the taxpayer's basis reduced by any nonrecourse borrowing to which the property is subject). The at risk limitation applies to all taxpayers except corporations which are not subchapter S corporations or personal holding companies.

Reasons for change

To encourage the exploration for, and the drilling and development of, geothermal wells and to accord geothermal resources uniform tax treatment, the committee decided to provide for all geothermal resources incentives similar to those provided for in the case of oil and gas.

Explanation of provisions

The committee bill provides taxpayers with the option to deduct currently, rather than to capitalize, intangible drilling and development costs related to the exploration for, and the development of, geothermal deposits. Geothermal deposits are defined by the bill to mean geothermal reservoirs consisting of natural heat which is stored in rocks or in an aqueous liquid or vapor (whether or not under pressure). The election to capitalize or to deduct intangible drilling

costs must be made prior to the expiration of the time for filing claims for credit or refund of any overpayment of tax imposed with regard to the taxpayer's first taxable year to which the bill is effective and for which intangible drilling costs are paid or incurred. Prior to the expiration of this period, but not thereafter, the election may be changed or revoked.

The bill also provides that the excess of the intangible drilling and development costs over the amount of those costs which would have been amortizable on the basis of a 10-year life and which further exceed the taxpayer's income from the production of geothermal resources constitutes a tax preference item for purposes of the minimum tax on individuals. Since some geothermal resources may be renewable to some extent, the bill provides that the amortizable amount which reduces the amount of the preference is to be determined on a 10-year life basis in all cases, rather than allowing the option of computing cost depletion on that resource. To ascertain the amount of the intangible drilling and development costs over the amount amortizable, which is subject to the minimum tax, the taxpayer's income from oil and gas properties is to be determined separately from the calculation of income from geothermal properties.

The committee's bill also provides that gain on the disposition of geothermal properties will be subject to recapture (i.e., treated as ordinary income rather than capital gain) to the extent that the amount of the intangible drilling cost deductions exceed the amount which would have been allowable had the costs been capitalized and deducted through cost depletion.

Furthermore, the committee's bill provides that the amount of any loss (otherwise allowable for the year) which may be deducted in connection with exploring for, or exploiting, geothermal deposits cannot exceed the aggregate amount with respect to which the taxpayer is at risk at the close of the taxable year, as determined under existing law (sec. 465). The at risk limitation applies to all taxpayers other than corporations which are not subchapter S corporations or personal holding companies.

In addition, the committee bill provides a 10-percent allowance for percentage depletion for all geothermal resources regardless of whether or not the geothermal resource would qualify for depletion under present law and regardless of whether or not the resource in fact is renewable. However, the amount of allowable depletion with respect to any property in any year may not exceed the taxpayer's adjusted cost basis in that property.[2]

[2] For example, assume that the taxpayer's basis in the property is $100,000, and that gross income from the property for year one is $600,000. The allowable percentage depletion deduction for year one (assuming that the 50-percent net income from the property and the 65-percent taxable income limitations do not apply) will be $60,000 ($600,000 × 10 percent), thereby reducing the basis of the property to $40,000. If the gross income from the property for year two is $600,000, the allowable percentage depletion deduction for year two will be $60,000. However, since the adjusted basis of the property at the beginning of year two is $40,000 (assuming both that no deductions which reduce basis, or downward adjustments to basis, were made in year one), only $40,000 of the otherwise permissible percentage depletion deduction of $60,000 is allowable. The excess $20,000 may not be deducted in year two or in any subsequent year, and no depletion deduction will be allowable for future years, unless the adjusted basis of the property is increased.

Effective date

The provisions relating to the deduction for intangible drilling costs, to the minimum tax, to recapture, and to the at risk rules apply with respect to wells commenced on or after April 20, 1977, in taxable years ending on or after that date.

The section relating to the provision for a 10-percent depletion allowance applies to taxable years beginning after December 31, 1977.

Revenue effect

The revenue loss from permitting the expensing of intangible drilling costs for geothermal discovery and development is estimated to be $5 million in fiscal 1978, $10 million in fiscal 1979, and to increase to $54 million by fiscal 1985.

The revenue loss attributable to the provision of a percentage depletion allowance at a 10-percent rate for all geothermal resources is estimated to be $1 million for fiscal years 1978–1980, and $2 million per year thereafter.

Energy savings estimate

It is estimated that the additional energy that would be made available due to the provision for the expensing of intangible drilling cost for geothermal discovery and development would reduce energy demand for fossil fuels in 1985 by the equivalent oil amount of from 60,000 to 110,000 barrels per day.

The energy savings attributable to the provision of a 10-percent percentage depletion allowance for geothermal resources is unknown.

G. REREFINED LUBRICATING OIL

(sec. 2074 of the bill and sec. 4093 of the Code)

Present law

Present law imposes a manufactures excise tax of 6-cents-per-gallon on lubricating oil (other than cutting oils) sold in the United States by the manufacturer or producer (sec. 4091). Also, a manufacturer of lubricating oil is liable for the tax if he uses the oil himself rather than selling it (unless the oil is used in manufacturing a product which is subject to a manufacturers excise tax). The net revenues from the tax (after refunds or credits for nonhighway use) go into the Highway Trust Fund (through September 30, 1979).

Cleaning, renovating, or refining used oil is not considered to be manufacturing, so the sale of recycled or rerefined oil by a refiner is not subject to the excise tax. However, where new lubricating oil is mixed with waste or rerefined oil, this does constitute manufacturing, and the excise tax is imposed on the portion of the mixture which consists of new lubricating oil.

Although present law taxes most sales of lubricating oil, present law also allows a tax refund or credit where lubricating oil is used for any purpose other than lubricating a highway motor vehicle. No refund is available where the oil, including rerefined oil, was exempt from tax in the first place. However, present law also denies the exemption where part of the oil was exempt from tax. As a result, when new oil and rerefined oil are blended, a tax is imposed on the new oil portion of the blend, but no refund or tax credit is available. Thus the tax laws provide a disincentive to the use of new or recycled oil.

In nontax areas, Congress has recently acted to encourage the use of recycled oil. Under section 383 of the Energy Policy and Conservation Act (Public Law 94–163), various Federal agencies are instructed to encourage the recycling of used oil, and to promote the use of the oil so processed or rerefined. The purpose of this mandate is to reduce the consumption of new oil by using recycled oil where appropriate, and to reduce environmental hazards and wasteful practices associated with the disposition of used oil. Recycled oil is to be tested to determine the uses for which it is substantially equivalent in performance to new oil; existing Federal rules pertaining to the labeling of recycled oil are to be changed so that recycled oil which is substantially equivalent to new oil will not be labeled to connote that it is less than equivalent to new oil for a particular purpose. In addition, the Act instructs Federal officials to revise procurement practices to encourage the procurement of recycled oil for military and nonmilitary uses wherever such recycled oil is available at prices competitive with new oil produced for the same use.

Reasons for change

To encourage the conservation and use of previously used oil, as well as to promote the disposition of spent additives in an environmentally acceptable manner, the committee's provision would remove the excise tax disincentive to the use of rerefined oil.

Explanation of provision

The provision exempts the sale of lubricating oil from the 6-cents-per-gallon manufacturer's excise tax where the lubricating oil is sold for use in mixing with 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 with regard to the portion of the new oil that does not exceed 55 percent of the mixture.

Effective date

This provision is effective for sales on or after the first day of the first calendar month beginning more than 10 days after the enactment of the Act.

Revenue effect

The exemption from the 6-cents-per-gallon excise tax for lubricating oil mixed with waste or rerefined oil will reduce revenues by about $3 million per year. These revenues would otherwise go into the Highway Trust Fund (through September 30, 1979).

Energy savings estimate

It is estimated that this provision will result in negligible energy savings.

H. ANNUAL REPORT ON ENERGY AND REVENUE EFFECTS OF THE BILL

(Sec. 2075 of the Bill)

Present law

Present law does not require a periodic report by an agency of the Executive branch on the revenue gain or loss or the energy savings from the provisions of a particular bill on a continuing basis. Annual reports are required, however, of Cabinet officers and the heads of independent agencies, in which the complete range of the agencies' activities for the year are described. In addition, annual reports to the Congress are required regarding the operations of the various trust funds—such as the Airport and Airway Trust Fund, the Highway Trust Fund, and the Social Security Trust Fund.

Reasons for change

The energy problem will continue for some time. This bill will not solve it but rather represents a beginning in dealing with a long-term situation. To assist the Congress in assessing the need for future legislation and developing subsequent programs, an evaluation of the revenue impact and energy saving effectiveness of the provisions of this bill is necessary.

Explanation of provision

The bill requires the President to submit an annual report to the Congress every August after 1977. The report is to provide estimates of the amount of revenue increases or decreases resulting from each of the provisions of this bill and an evaluation of the extent to which each of the provisions has resulted in increased energy conservation and production.

The bill also requires that the President provide such other information as he determines is relevant for an evaluation of the provisions of the bill. The committee expects the President to include in his report the petroleum (or natural gas) savings resulting from each provision and the extent to which shifts from petroleum and natural gas to other materials has occurred as a result of each provision.

Effective date

This provision will become effective on date of enactment of this Act.

The following sections of the report have been omitted:

D—Committee on Ways and Means—Rept. 95-496, Part III
VI—Budget Effects of Title II of H.R. 6831 and Vote of the Committee in Reporting the Title (pages 253-254)
VII—Other Matters to be Discussed under House Rules (pages 255-260)
VIII—Changes in Existing Law Made by Title II of H.R. 6831 (page 261)
IX-XXI—Supplemental, Additional, and Minority Views (pages 263-295)
E—Committee on Interstate and Foreign Commerce—Rept. 95-496, Part IV (pages 297-376)

Calendar No. 484

95TH CONGRESS 1st Session } SENATE { REPORT No. 95-529

ENERGY PRODUCTION AND CONSERVATION TAX INCENTIVE ACT

REPORT

OF THE

COMMITTEE ON FINANCE
UNITED STATES SENATE

ON

H.R. 5263

together with

ADDITIONAL, SUPPLEMENTAL AND DISSENTING VIEWS

OCTOBER 21, 1977.—Ordered to be printed

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Senate Report No. 95–529

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Calendar No. 484

95TH CONGRESS } SENATE { REPORT
1st Session } { No. 95-529

(Numerals at top of page indicate official report page numbers)

ENERGY PRODUCTION AND CONSERVATION TAX INCENTIVE ACT

OCTOBER 21, 1977.—Ordered to be printed

Mr. LONG, from the Committee on Finance, submitted the following

REPORT

together with

ADDITIONAL, SUPPLEMENTAL, AND DISSENTING VIEWS

[To accompany H.R. 5263]

The Committee on Finance, to which was referred the bill (H.R. 5263) to suspend until the close of June 30, 1980, the duty on certain bicycle parts, having considered same, reports favorably with an amendment and with an amendment to the title and recommends that the bill as amended do pass.

House bill.—H.R. 5263 as it passed the House would continue until June 30, 1980, the existing suspension of duties on certain bicycle parts.

Committee bill.—The substance of the House bill has been approved by the Senate as a provision of H.R. 2982. The committee amendment strikes all after the enacting clause, and inserts in lieu thereof the committee's decisions with respect to energy production and conservation tax incentives. The amendment is shown in italic in the bill as reported.

I. OVERVIEW

Need for an energy program

The Nation's excessive reliance on oil imports and the inability to satisfy domestic natural gas demand with domestic supply pose a serious threat to the U.S. economy and national security. Presently, the United States is importing nearly half its oil, and last winter tens of thousands of workers were laid off their jobs because their employers could not obtain natural gas. Clearly, the country needs immediate action to reduce demand for imported oil and to increase domestic supply of oil and gas.

This bill uses tax incentives in an effort to reduce demand for energy, to induce conversion from oil and gas to more abundant domestic energy sources, and to increase U.S. production of a broad range of energy sources. The committee believes this approach will be more effective than an approach which relies largely on tax increases to reduce demand for energy. Also, unlike the House bill (title II of H.R. 8444), which emphasized reducing consumption, the committee's bill balances incentives for conservation and incentives for increased energy production. The cost of these tax incentives will be very small in relation to the economic and strategic costs of failing to take decisive action to deal with the energy import problem.

It is estimated that these incentives will reduce oil imports in 1985 by about 2 million barrels per day.

Summary of major tax provisions

Insulation credit.—The committee bill includes a tax credit of 20 percent of the initial $2,000 of expenditures on home insulation and other residential energy conserving components (for a maximum credit of $400). This credit may exceed tax liability (that is, it is a refundable credit).

Renewable energy source equipment credit.—Homeowners would also be eligible for a credit for renewable energy source equipment, which includes solar, wind and geothermal energy systems. The credit would be 30 percent of the first $2,000 of expenditures and 20 percent of the next $8,000 (for a maximum credit of $2,200). This credit would also be refundable.

Business energy investment credit.—The committee bill contains a business energy investment credit which is a considerably more effective incentive than the comparable credit in the House bill. This new credit would be available in addition to the regular 10-percent investment tax credit. The rate of the new credit would be 40 percent for alternative energy property, which includes geothermal, solar, wind, hydroelectric, nuclear, coal, ocean thermal, tidal and biomass energy property as well as certain equipment related to the business use of energy sources other than oil and gas. For utilities, the credit would be available only to the extent that existing oil- or gas-fired power plants are replaced or phased down.

The rate of the additional investment credit would be 10 percent for property used in the cogeneration of electricity and other useful forms of energy, certain kinds of property used by businesses to conserve energy by modifying existing buildings or processes (called specially defined energy property), recyclingg equipment, equipment used to produce geopressurized methane gas, vehicles used for vanpooling, and energy saving devices for cars, trucks and buses used by businesses.

The 40-percent business energy investment credit and the 10-percent credit for specially defined energy property would be refundable and available to tax-exempt charitable organizations and State and local governments.

Additional incentives.—The committee bill contains language which is intended to give the conferees flexibility, with respect to any new taxes which may be in the bill agreed to by the conference, to use a portion of the revenues raised by such taxes to provide tax and other economic incentives for increased energy production, conservation and conversion to alternative sources of energy and to mitigate adverse consequences, such as inequities, resulting from the energy situation.

Energy trust fund.—The committee bill also provides that a portion of any funds which may be raised by new taxes in the bill be used for an energy trust fund, which would finance outlays for energy production, energy conservation and energy-efficient forms of transportation.

Other provisions

Tax provisions

Other energy-related tax provisions in the committee's bill include the following changes:

—Extension through September 30, 1985, of the existing 4-cent-per-gallon tax on gasoline and other motor fuels, which otherwise is scheduled to decline to 1½ cents per gallon after September 30, 1979.

—Removal of the 2-cents-per-gallon refund or credit for gasoline and other fuels for motorboat and other nonbusiness, off-highway use.

—Exemption from the 4-cent gasoline tax for gasoline-alcohol blends (gasahol) if such blends contain at least 10 percent ethanol and/or methanol and if the alcohol is made from agricultural or forestry products; and a reduction in the tax rate to 3 cents per gallon for gasahol containing alcohol made from other products (such as coal).

—A tax credit for intercity bus companies, which would be used to reduce rates and improve or expand bus terminal facilities and to purchase or improve buses and bus equipment.

—Repeal of the 10-percent excise tax on buses and the 8-percent excise tax on bus parts.

—Exemption of privately-owned intercity, local and school buses from excise taxes on fuels, tires, tubes and tread rubber, and lubricating oil.

—A $300 tax credit for the purchase of electric cars for personal use.

—Exemption from income tax of employees for energy-efficient transportation provided by employers.
—Exemption of rerefined lubricating oil from the excise tax on new oil.
—Extension of the existing 10-percent investment tax credit to business insulation.
—An increase in the rate of percentage depletion from 5 percent to 10 percent for peat used directly or indirectly for fuel.
—An allowance for percentage depletion and for expensing of intangible drilling costs for geothermal energy under rules similar to existing provisions for oil and gas.
—Provision of 10-percent depletion and expensing of intangible drilling costs and geological and geophysical costs for geopressurized methane gas.
—A $3 per barrel tax credit for production of shale oil, and a 50-cent per mcf credit for production of geopressurized methane gas and gas from other nonconventional sources.
—Permanent exemption from the minimum tax for intangible drilling costs to the extent of oil and natural gas production income.
—Tax exemption for industrial development bonds used for bioconversion facilities and for coal liquefaction and gasification facilities.

Nontax provisions

In addition, the committee bill includes the following nontax provisions relating to reports by the President and the President's authority with respect to oil imports:
—An annual report to the Congress by the President on the energy saving and revenue effects of the bill.
—Limitation of the President's power to impose tariffs, license fees, or quotas on crude oil imports to wartime or actual hostilities and limitation of his authority to adjust imports of refined petroleum products to adjustments necessary for national security.

II. REASONS FOR THE BILL

The United States is faced with an extremely serious energy problem. Consumption of oil is rising rapidly while domestic production is declining. The resultant dependence on oil imports poses a serious threat to our economic wellbeing, our national security and our ability to conduct an independent foreign policy. For natural gas, where large quantities of imports are not available, the result of rising demand and declining domestic production has been severe gas shortages, which last winter caused widespread layoffs of workers in businesses dependent on natural gas. Clearly, the United States must curtail the growth in demand for imported oil, encourage conservation of oil and gas, increase domestic production of energy, and accelerate the shift to more abundant domestic sources of energy. This bill is designed to move toward these goals by providing a variety of tax incentives.

The Finance Committee's bill differs significantly from the House-passed energy tax provisions (title II of H.R. 8444). The House bill relies heavily on energy-related tax increases designed to encourage conservation by raising the price of oil and gas to consumers and by increasing the price of fuel inefficient automobiles, and relies relatively little on positive tax incentives. The committee bill takes a different approach and attempts to induce consumers of oil and gas to conserve energy and convert to alternative energy sources through the appropriate tax incentives. The tax provisions of the House bill also place relatively little emphasis on increased domestic production of energy. The committee believes that conservation, by itself, cannot do the full job of meeting the nation's energy needs; therefore, the committee's bill provides major tax incentives for the production of such new sources of energy as geopressurized methane gas, oil shale, geothermal resources and bioconversion.

Energy consumption and production trends

Table 1 shows recent trends in U.S. energy consumption and production. Energy consumption grew steadily until 1974, declined in 1974 and 1975, and grew rapidly again in 1976.[1] Domestic energy production grew until 1972, although at a slower rate than demand, and has been declining since then. In 1950 domestic energy production exceeded consumption, but by 1976 it was only about 80 percent of consumption.

---

[1] Energy is measured in quadrillions of British thermal units, or Btu's. A Btu is the amount of energy needed to raise the temperature of one pound of water by one degree Fahrenheit. A 42-gallon barrel of crude oil contains 5.8 million Btu's. Natural gas contains about one million Btu's per thousand cubic feet (mcf). One million barrels of oil per day equals about two quadrillion Btu's, or quads, per year; and one trillion cubic feet of natural gas is about one quad per year.

(6)

Table 1.—U.S. energy consumption and production

[Quadrillion Btu's]

Year	Consumption	Domestic production	Domestic production as percent of consumption
1940	23.91	25.09	104.9
1950	33.99	34.35	101.1
1960	44.57	41.55	93.2
1965	53.34	49.07	92.0
1967	58.27	54.83	94.1
1968	61.76	56.58	91.6
1969	64.98	59.41	91.4
1970	67.14	62.48	93.1
1971	68.70	61.67	89.8
1972	71.90	62.94	87.5
1973	74.55	62.37	83.7
1974	72.60	61.14	84.2
1975	70.56	60.13	85.2
1976	74.24	59.83	80.6

Sources: *Monthly Energy Review* (1972–76) and *Statistical Abstract of the United States 1976* (1940–71).

The United States must reverse this trend towards greater dependence on energy imports. This will require a combination of curtailing the growth of energy demand through conservation and increasing the domestic production of energy.

The possibilities for energy conservation can be seen by comparing U.S. energy consumption per capita with that of other countries with high standards of living. This comparison is made in table 2, which shows that U.S. energy consumption per capita is twice that of Germany and Sweden and more than three times that of Switzerland. In all three of these countries, the average standard of living is not markedly different from that in the United States.

About one-half of the difference in per capita energy consumption between the United States and Europe occurs in the transportation sector. European automobiles get much higher gas mileage than U.S. autos and are used less. About one-quarter of the difference is due to the greater energy consumption in homes, even after adjustments for differences in climate. Residences in Sweden, Germany and Switzerland are better insulated than those in the United States; air conditioning is used less in these countries; the United States contains larger homes and a larger proportion of less energy-efficient single-family homes; and U.S. homeowners heat their homes to higher temperatures than do European homeowners. European industry also is more energy-efficient than U.S. industry.

These data show that significant energy conservation is possible without a major change in living standards if people are willing to

Table 2.—Energy consumption per capita in various countries, 1974

Country	Consumption of energy—coal equivalent (million metric tons)	Consumption of energy per capita (kilograms of coal equivalent)
United States	2,433.5	11,485
Germany	353.0	5,689
United Kingdon	306.5	5,464
France	227.6	4,330
Italy	178.6	3,227
Japan	421.0	3,839
Sweden	47.4	5,804
Switzerland	23.3	3,608
World total	7,953.0	2,100

Source: *Statistical Abstract of the United States 1976.*

concentrate on saving energy. The committee's bill contains tax incentives designed to encourage such behavior.

Conservation alone, however, is not sufficient to solve our energy problem. The United States contains substantial energy resources which businesses have not found profitable to develop at past and current energy prices. These include oil from shale, geopressurized methane gas, geothermal energy, energy from bioconversion, and other energy sources. These energy sources are not now largely exploited and will be expensive to develop. Yet some of these sources may be the key to the long-term future of the American economy, and it is essential that the United States move quickly to develop as many of them as feasible.

Oil supply and demand

Because the United States and many of its allies are so heavily dependent on oil imports from only a few countries, the need to restrain demand and increase supply is especially serious for oil. Table 3 shows the U.S. supply and demand for petroleum in the past two decades. Since 1955, demand has grown from 8.49 million barrels per day (mbd) to 17.44 mbd. U.S. production of petroleum did rise between 1955 and 1970, but at a slower rate than demand; consequently, there was a gradual rise in imports. Since 1970, however, U.S. oil production has declined, and the growth in oil imports has accelerated rapidly. In 1976, oil imports were 7.3 mbd—42 percent of consumption; and in the first half of 1977, oil imports accounted for almost half of domestic consumption. This dependence on imported oil is an obvious threat to national security.

The committee bill contains several incentives to encourage oil conservation and conversion from oil to other energy sources. Also, it provides significant incentives for production of expensive, unconventional energy sources which are not now being used in the United

Table 3.—U.S. oil demand, supply and imports, 1955–76

[In millions of barrels per day]

Year	U.S. demand for petroleum	U.S. production of crude oil	U.S. production of natural gas liquids	U.S oil imports
1955	8.49	6.81	.77	1.25
1956	8.82	7.15	.80	1.44
1957	8.86	7.17	.81	1.57
1958	9.15	6.71	.81	1.70
1959	9.49	7.05	.88	1.78
1960	9.81	7.04	.93	1.82
1961	9.99	7.18	.99	1.92
1962	10.41	7.33	1.02	2.08
1963	10.75	7.54	1.10	2.12
1964	11.03	7.61	1.16	2.26
1965	11.52	7.80	1.21	2.47
1966	12.10	8.30	1.28	2.57
1967	12.57	8.81	1.41	2.54
1968	13.40	9.10	1.50	2.84
1969	14.15	9.24	1.59	3.17
1970	14.71	9.64	1.66	3.42
1971	15.23	9.46	1.69	3.93
1972	16.37	9.44	1.74	4.74
1973	17.31	9.21	1.74	6.26
1974	16.65	8.77	1.69	6.11
1975	16.32	8.38	1.63	6.06
1976	17.44	8.12	1.60	7.30

Source: Independent Petroleum Association of America (1955–71) and *Monthly Energy Review* (1972–76).

States. Together these tax incentive provisions will reduce oil imports by about 2 million barrels per day by 1985.

Natural gas supply and demand

It is also essential that the demand for natural gas be reduced and U.S. gas production be increased. Production of natural gas in the United States peaked in 1972 at 22.6 trillion cubic feet and has declined at an alarming rate since then, amounting to 19.9 trillion cubic feet in 1976. Most of this decline has been reflected in reduced sales to interstate pipelines. The result has been widespread layoffs in industries dependent on natural gas and the inability of homeowners in many areas to obtain natural gas hookups.

The committee bill contains significant tax incentives for conservation of natural gas and conversion from gas to other sources of energy. In addition, the bill creates substantial tax incentives to develop more expensive sources of gas, such as geopressurized methane and gas from tight rock formations (such as from Devonian shale and coal seam methane deposits).

III. SUMMARY OF THE BILL

A. Residential Energy Credits

1. Residential insulation and energy conservation credit

The committee bill provides a refundable credit of 20 percent on the first $2,000 of cumulative expenditures on home insulation and other energy conserving components for a maximum credit of $400. The credit is to be available for installations made from April 20, 1977, through December 31, 1985.

Insulation means materials that will reduce the heat loss or heat gain of a residence. Attic, floor and wall insulation made of fiberglass, rock wool, cellulose or styrofoam are examples of insulating materials. Energy conserving components include a replacement furnace or boiler providing more efficient energy utilization, a replacement burner for a furnace which provides increased combustion efficiency, devices to modify flue openings, electrical or mechanical ignition systems that replace a gas pilot light, exterior storm or thermal doors or windows, any automatic energy-saving setback thermostat, any heat pump replacing an electrical resistance heating system, exterior caulking or weatherstripping of doors or windows, meters which display the cost of energy usage, and fluorescent replacement lighting systems.

The expenditures must be made for a principal residence that was in existence on April 20, 1977. Vacation homes and other residences do not qualify for the credit, nor do residences that were constructed after April 20, 1977, or were substantially completed after that date. If a taxpayer moves to another principal residence after taking the credit on a previous principal residence, qualifying property would be eligible for another $400 credit for the new residence before January 1, 1986.

Owners and renters will be eligible for the credit. Cooperatives and condominium housing owners are each eligible for the credit up to the $400 maximum on their proportionate shares of the common qualifying expenditures. Joint occupants of a principal residence must allocate the credit.

2. Residential renewable energy source equipment credit

A refundable credit up to $2,200 is to be available on the first $10,000 of expenditures on solar, wind and geothermal energy equipment. The credit is 30 percent of the first $2,000 spent and 20 percent of the next $8,000 spent for installations of this equipment from April 20, 1977, through December 31, 1985.

Eligible equipment covers equipment that uses solar or geothermal energy to heat or cool, or to provide hot water for a principal residence, and equipment that uses wind to generate electricity and other forms of energy. This equipment need only be installed in connection with a residence rather than in or on it. Qualifying equipment does not include backup systems of conventional heating or cooling equipment.

For solar, wind, and geothermal energy equipment, the principal residence may be either an existing or newly constructed residence. Owners and renters are eligible for the credit. Members of cooperative and condominium associations are each eligible for the credit to the maximum amount for their proportionate shares of the common qualifying expenditures. Joint occupants of a principal residence must allocate the credit.

B. Transportation Tax Provisions

1. Extension of excise tax on gasoline and other motor fuels

The current Federal excise taxes of 4 cents a gallon on gasoline and other motor fuels will be continued at that rate through September 30, 1985. These taxes are currently scheduled to be reduced to one and one-half cents a gallon after September 30, 1979. The committee took no action at this time on the current Highway Trust Fund, which will continue to receive these funds under present law through September 30, 1979.

2. Exemption or reduction of rate of fuels taxes for gasahol

Gasahol that is at least 10 percent ethanol or methanol made from agricultural or forestry products would be exempted from the Federal excise taxes on motor fuels on or after January 1, 1978, and before October 1, 1985. Between these dates, gasahol that is at least 10 percent ethanol or methanol made from nonagricultural and nonforestry products would be subject to Federal excise taxes of 3 cents a gallon (rather than 4 cents a gallon).

3. Removal of certain refunds of excise taxes on motor fuels and lubricating oil

The committee bill repeals the 2-cents-a-gallon reduction (through refund, credit, or exemption) of the excise taxes on gasoline and special motor fuels, and the refund (or credit) of the 6-cents-a-gallon tax on lubricating oil, with respect to gasoline, special fuels, and lubricating oil used (1) for nonbusiness, off-highway purposes (such as lawn mowers, snowmobiles, etc.) and (2) in motorboats (whether or not such use is business use). To the extent that increased revenues are attributable to fuels used in motorboats, they will be transferred to the Land and Water Conservation Fund (as are the present fuels taxes attributable to motorboat use).

4. Repeal of excise taxes on buses and bus parts

The 10-percent excise tax on buses and the 8-percent excise tax on bus parts and accessories are repealed. Parts and accessories that may be interchangeable between trucks and buses will be taxed on sale unless the purchaser provides the manufacturer with an exemption certificate which indicates that the part or accessory is purchased for use on a bus. If tax-paid parts are acquired from a dealer and are used on a bus. a credit or refund is to be available.

5. Removal of excise taxes on items used with certain buses

The bill removes the excise taxes on tires, inner tubes, tread rubber, and lubricating oil sold for use on or in connection with privately

owned intercity, local, and school buses. It also provides a credit or refund for the taxes imposed on gasoline and other motor fuels to the extent the fuels are used in qualified operations of privately owned intercity, local, and school buses.

6. Tax credit for vans used in vanpooling

The bill provides that, if an employer purchases a new van with a useful life of at least 3 years, seating nine or more persons (including the driver) and substantially all the use of the van is for transporting employees to and from work, the employer is entitled to the full 10-percent investment credit and the additional, special 10-percent business energy investment credit.

7. Exclusion from income of certain employer-furnished transportation

The committee bill also provides that, in the case of a taxpayer who is an employee, gross income does not include the value in excess of the employee's cost of transportation to or from work furnished by an employer, if such transportation is in a commuter van.

8. Tax credit for electric motor vehicles

New electric cars purchased for personal use by individuals on or after April 20, 1977, and before January 1, 1986, will be eligible for a tax credit equal to the first $300 of the purchase price. A qualified electric motor vehicle is a 4-wheeled vehicle manufactured for use on public roads that is powered by an electric motor which receives electric current from rechargeable storage batteries or other portable sources.

9. Intercity bus credit

The bill provides a refundable tax credit for intercity bus operators based on the operator's bus passenger miles and the per passenger mile fuel efficiency of the taxpayer's intercity buses in comparison to the per passenger mile fuel efficiency of automobiles. It is designed so that the operator is required to use the credit (estimated to be about $200 million per year for the industry) for fare reductions and investment in equipment and terminals: 50 percent of the credit will be earmarked for fare reductions and the remaining 50 percent will be earmarked for investment in terminals and equipment.

C. Business Energy Credits

1. Refundable tax credit for alternative energy property and specially defined energy property

A 40-percent credit is provided for certain conversion property, called alternative energy property, and a 10-percent credit is provided for certain conservation property, called specially defined energy property, during the period after April 19, 1977, and before January 1, 1986. These credits are in addition to any regular investment credits to which such property may be entitled. If eligible property is constructed by the taxpayer, the credit will be available only for construction that is completed during the period after April 19, 1977, and before January 1, 1986, to the extent of costs incurred during this period.

The credit is refundable, so that the amount which the taxpayer is allowed is not limited by tax liability. Charitable, educational, re-

ligious and other organizations which are exempt from Federal income tax under Code section 501(c)(3), electric utility cooperatives exempt under sec. 501(c)(12), as well as State and local governments, are eligible to receive the credit. Any excess of the credit above tax liability may be claimed as a refund.

These credits will be applied using rules generally similar to the regular investment credit provisions. As a result, the rules for applying the regular investment credit, such as the rules which limit the extent to which any credit to a utility may be flowed through to its customers, will also generally apply to the alternative energy property investment credit. Special rules are provided in a number of areas; for example, the credit will be allowed only to the extent an existing oil or natural gas fueled boiler owned or used by an electric utility is phased down. The loading and structural component limitations are also made inapplicable to such property. In addition, recapture of credits will occur if the property ceases to be qualifying property, and the credits are reduced where such property is financed by industrial development bonds (except in the case of bioconversion equipment) or federal grants.

In order to qualify, equipment must be new property and located within the United States, with a useful life of three years or more.

Alternative energy property.—In general, alternative energy property is equipment involved in the use of an alternate substance (one other than oil, natural gas, or a derived product) as a fuel or feedstock. The following types of property are specifically included:

(a) a boiler whose primary fuel will be an alternate substance:

(b) a burner and equipment necessary to supply fuel to a combustor other than a boiler for which the primary fuel will be an alternate substance;

(c) equipment used in the production of energy by nuclear power, but not including turbines or equipment beyond the turbine stage, or by hydroelectric power, including turbines and equipment up to (but not including) the electrical transmission stage;

(d) equipment for converting an alternate substance in a synthetic fuel;

(e) equipment to produce a chemical feedstock from coal or lignite;

(f) equipment which modifies an existing facility to replace the use of oil or natural gas as a fuel or feedstock with at least 25 percent coal or another alternate substance;

(g) pollution control equipment required to be installed in equipment described above (other than equipment required on April 20, 1977, to be installed on a facility using coal);

(h) equipment used for unloading, transferring, storing, reclaiming from storage and preparation of an alternate substance for use in the equipment described above or in a facility which uses coal as a feedstock for products other than coke;

(i) equipment to convert ocean thermal and tidal power into useful energy;

(j) equipment to convert solar and wind energy into useful energy;

(k) equipment used to produce, distribute or use energy from a geothermal deposit but not including electrical transmission, in the case of electricity generated by geothermal power, and

(l) plans and designs for any other qualifying alternative energy property.

Specially defined energy property.—This category of property is generally equipment which, when added to an existing production or processing activity, reduces energy consumption. The following items of property, specifically covered here, qualify for the credit if they are added to existing buildings, industrial processes and utility facilities: recuperators; heat wheels; regenerators; heat exchangers; waste heat boilers; heat pipes; automatic energy control systems; turbulators; preheaters; combustible gas recovery systems; economizers, and industrial heat pumps.

In addition to these types of property, the Secretary is authorized to specify other similar items of energy conservation equipment eligible for this credit, including modifications which are made to existing industrial processes (such as modifications to smelters or alumina electrolytic cells) the principal purpose of which is the reduction in the amount of energy consumed or heat wasted.

2. Business energy conservation credit

There would generally be an additional 10-percent business energy tax credit for investments by business in qualified property intended to reduce the amounts of oil, natural gas, or other energy consumed in heating or cooling a building or used in an industrial process.

The credit would be available for investments in qualifying property made after April 19, 1977, and before January 1, 1986.

Qualifying property.—For the business energy tax credit, qualifying property includes equipment to start or expand the cogenerating capacity in an existing facility, to recycle solid waste to recover solid recyclable materials, burn solid waste as a fuel, or convert solid waste into a fuel and to recover oil from oil shale rock and gas from geopressurized water deposits and also commuter vans and energy saving equipment added to existing trucks.

In order to qualify, property or equipment under these categories generally must be new property which would be used in connection with a vehicle, building or facility in existence or substantially completed by April 20, 1977.

3. Business insulation credit

For purposes of the regular investment credit, insulation installed in connection with an existing building or industrial facility would be qualifying property through 1985. Insulation includes storm doors and windows, thermal glass and double glazing.

D. Tax Incentives for Alternative Energy Sources

1. Coal gasification and liquefaction and bioconversion facilities—use of tax-exempt industrial development bonds

The committee amended sec. 103 of the Code (relating to interest earned on certain governmental obligations) to provide that tax-exempt industrial development bonds can be used for the financing of

coal gasification and liquefaction facilities for the furnishing of synthetic gas, or liquid fuels. The amendment also provides that tax-exempt industrial development bonds may be used for the financing of bioconversion facilities for the conversion of municipal and agricultural wastes, and other organic matter, into energy, or into synthetic gaseous, liquid, or solid fuels.

2. *Geothermal tax provisions*

A current deduction would be allowed for intangible drilling costs related to the exploration and development of geothermal resources. To the extent that these intangible drilling costs exceed the taxpayer's income from the production of geothermal resources, these costs would be subject to the minimum tax on preference income.

In addition, the committee bill provides percentage depletion for geothermal deposits at the rate established generally for oil and gas. The committee amendment also provides that gain on the disposition of geothermal properties will be subject to recapture. In addition, the amount of any loss (otherwise allowable for the year) which may be deducted in connection with exploring for, or exploiting, geothermal deposits cannot exceed the aggregate amount with respect to which the taxpayer is at risk at the close of the taxable year.

3. *Geopressurized methane gas*

A current deduction would be allowed for geological and geophysical exploration costs, and for intangible drilling costs related to the exploration for, and development of, geopressurized methane gas. To the extent that the intangible drilling costs exceed the taxpayer's income from the production of geopressurized methane gas, these costs would be subject to the minimum tax on preference income.

In addition, the committee bill provides percentage depletion at a 10-percent rate for geopressurized methane gas. Gain on the disposition of geopressurized methane gas properties will be subject to recapture. The amount of any loss (otherwise allowable for the year) that may be deducted in connection with exploring for, or exploiting, geopressurized methane gas cannot exceed the aggregate amount with respect to which the taxpayer is at risk at the close of the taxable year.

In addition, the committee bill provides a production credit of 50-cents per thousand cubic feet of geopressurized methane gas produced by the taxpayer.

4. *Credit for production of oil and gas from nonconventional sources*

The committee bill provides a $3 per barrel tax credit for the production of oil from shale. A tax credit of 50-cents per thousand cubic feet of gas has been provided for gas produced during the taxable year from all geopressurized methane gas properties and from all tight rock formation properties. The credits only apply to domestic production.

5. *Percentage depletion for peat*

The committee bill increases the percentage depletion allowance from a 5-percent rate to a 10-percent rate for peat used as a fuel, or otherwise used to produce energy.

E. Additional Tax Incentives; Energy Trust Fund

The bill includes a provision which is intended to give the Senate conferees flexibility in attempting to reach agreement with the House on this bill. The committee bill provides that no new taxes in this bill, such as the gas guzzler tax, the crude oil equalization tax and the industrial user tax in the House bill, are to go into effect unless they are accompanied by tax and other economic incentives for energy conservation, conversion and production as well as provisions to mitigate undesirable consequences of the energy situation, such as inequities. This provision is intended to give the conferees flexibility in devising suitable uses for any revenue raised by new taxes or other positive incentives to accompany any tax increases.

In addition, the bill establishes a trust fund to finance energy-related outlays, including spending for energy-efficient transit. All outlays from the trust fund will be subject to the normal authorization and appropriation process. Revenues from any new taxes added by the bill would be appropriated into the trust fund.

F. Limitation of President's Authority to Adjust Oil Imports

The President's discretionary authority to adjust imports of petroleum and petroleum products under section 232(b) of the Trade Expansion Act of 1962 and titles I and V of the Trade Act of 1974 is nullified except for military or defense emergencies involving actual hostilities or for situations where the national security requires adjustments in the imports of refined petroleum products.

G. Other Provisions

1. Minimum tax on intangible drilling costs for oil and gas wells

The committee extended without time limit the provision in present law relating to the minimum tax on intangible drilling costs. As a result, the minimum tax on preference income applicable to intangible drilling costs for oil and gas wells would be modified to treat these intangible costs as a preference income only to the extent they exceed the taxpayer's oil and gas production income.

2. Rerefined lubrcating oil

New lubricating oil would be exempt from the 6-cents-per-gallon excise tax, if it is combined with rerefined oil and the new oil makes up 55 percent or less of the mixture. If the new oil in the mixture exceeds 55 percent of the contents, the exemption would apply only to the new oil that would make up 55 percent of the mixture. In any case, the mixture must contain at least 25 percent waste or rerefined lubricating oil in order to qualify for the exemption.

3. Annual report on energy savings and revenue effects

Beginning in August 1978, the President will report each year to the Congress on the savings in energy use accomplished, the revenue received, and the revenue disbursed under each specific program contained in the committee bill.

4. Reconciliation with budget resolution

The Secretary of the Treasury is authorized to postpone the effective dates of tax reductions in the bill to a date no later than October 1, 1978, to the extent necessary to ensure that the revenue floor ($397 billion) in the Second Concurrent Resolution on the Budget for fiscal year 1978 is achieved.

The bill includes a sense-of-the-Senate resolution that the Senate conferees, to the extent practicable, should keep the revenue loss from the bill in fiscal year 1978 at no more than $972 million, which is the revenue loss from the House energy bill and is the amount anticipated in the Second Budget Resolution.

IV—Budget and Energy Savings Effects (pages 19-29) omitted

V. EXPLANATION OF ENERGY TAX PROVISIONS

A. RESIDENTIAL ENERGY CREDITS

1. Residential Insulation and Other Energy-Conserving Component Credit (sec. 1011 of the bill and new sec. 44C of the Code)

Present law

Under present law, no special tax credit or deduction is allowed for the installation of insulation or other energy-conserving components in or on a taxpayer's residence. However, if these installations constitute capital improvements to a residence, the amount of the expenditures involved are added to the taxpayer's basis in the residence for purposes of determining gain or loss on a subsequent sale of that residence.

Reasons for change

A substantial portion of our domestic energy consumption is used to heat or cool residences. Currently, about 23.7 percent of U.S. domestic energy consumption, or about 7 percent of total world demand, is used for residential purposes. Surveys have indicated that many residences in the United States are not adequately insulated.

Because of the substantial energy savings that may be effected by proper insulation of homes and other energy-conserving measures, and to reduce the potential problems in the event of any future energy shortages (such as the 1973–74 shortage which resulted from the oil embargo), the committee's bill includes a refundable income tax credit to provide homeowners and tenants with an incentive to conserve energy by immediate installations of insulation and other energy-conserving components.

The committee is mindful of potential supply problems that the fiberglass insulation industry might encounter. Thus, while the credit is provided for a limited number of years, that period of time was made sufficient in length (through 1985) so that the demand generated for this insulation by the credit would not be sharply increased in any one year.

The committee hopes that the States and localities will recognize the need for enacting laws in the immediate future which provide property tax exemptions for increases in value resulting from insulation and other energy-conserving component improvements.

Explanation of provisions

Nature, amount, and period of credit

The committee's bill provides a refundable income tax credit for insulation and other energy-conserving component expenditures for installations in or on the principal residence of the taxpayer. The credit is 20 percent of the first $2,000 of qualifying expenditures. Thus, the maximum credit would be $400.

This credit is to be refundable. Thus, the credit will be applied against the taxpayer's tax liability, and, to the extent it exceeds the amount of tax liability, the taxpayer would be entitled to a refund. However, individuals whose residences are the subjects of weatherization grants under the nontax energy provisions of the National Energy Conservation Policy Act (title II, H.R. 5037, passed by the Senate, September 13, 1977) are not to be entitled to the credit. It is anticipated that the amount of any loan issued under these provisions would be reduced by the amount of the credit allowed.

In determining the credit, the $2,000 maximum allowable expenditures amount is to be reduced by previous expenditures by the taxpayer which were taken into account in computing the credit for prior taxable years. An individual will be eligible for the maximum credit each time he changes his principal residence. Thus, an individual would be eligible for the maximum credit for qualifying expenditures on his new principal residence, notwithstanding the allowance of the credit for qualifying expenditures on his previous principal residence and notwithstanding the allowance of the credit to a prior owner of the individual's new principal residence.

The entire cost of insulation or other energy-conserving component property is allowed toward the credit only if at least 80 percent of the use of the property is for personal residential purposes. If less than 80 percent of its use is for personal residential purposes, the amount is reduced proportionately. For example, if an expenditure of $3,000 is made, but only 50 percent of the use of the property installed is for personal residential purposes (the other 50 percent of use being for business purposes), the allowed credit would be $300 (the allowable credit on $1,500, which is 50 percent of $3,000). For purposes of this provision, use for a swimming pool is not to be treated as personal residential use.

In order to avoid administrative burdens which could result from a credit for only a small amount of qualified expenditures in a year, a minimum credit amount of $10 for any taxable year is required with respect to any tax return (joint or separate) if any credit is to be allowed. This minimum credit requirement applies to the aggregate of the credits claimed for a taxable year for renewable energy source expenditures and for insulation and other energy-conserving component expenditures.

The credit is to be available for expenditures made on or after April 20, 1977, and before January 1, 1986.

When qualified expenditures are treated as made

Expenditures for insulation and other energy-conserving components (including expenditures for installation) are to be treated as made when the original installation of the property is completed. Consequently, for purposes of this provision, the time of payment or accrual of amounts for insulation or other energy-conserving components would not be determinative of when the expenditures for such property have been made.

Qualifying residences

In order to qualify for the credit, installations of insulation or other energy-conserving components must be in or on an individual's prin-

cipal residence, and that residence must be located in the United States, Guam, or the U.S. Virgin Islands. The credit is available, however, only with respect to residences the construction of which was substantially completed before April 20, 1977. Owners and renters will be eligible for the credit; moreover, an individual who owns stock in a cooperative housing association or who is a member of a condominium management association [1] will be treated as having expended an allocable share of amounts expended by the association for insulation and other energy-conserving components and will be eligible for the maximum $400 credit.

The cooperative stockholder's allocable share of the qualifying expenditures is to be the same as his proportionate share of the cooperative's total outstanding stock. The condominium management association's member's allocable share is to be the amount he is assessed by the association as a result of the energy conservation expenditures.[2]

The determination of whether a dwelling unit is used by a taxpayer as his principal residence will be made under principles similar to those applicable to section 1034 of the Code (relating to a sale or exchange of a principal residence) except that ownership of the dwelling unit will not be required for renters. Moreover, in making this determination, the period for which a dwelling will be treated as a taxpayer's principal residence will include the 30-day period immediately preceding the date the dwelling unit would, under principles similar to those applicable to section 1034, be treated as being used as the taxpayer's principal residence. Thus, installations which are completed within the 30-day period immediately preceding the date the residence would (but for this provision) be treated as being used as the taxpayer's principal residence will be eligible for the credit.[3]

Qualifying property

The credit applies to qualifying insulation and other energy-conserving components. The credit is to be allowed also for the original installation of qualifying insulation (or of a qualifying energy-conserving component) in a residence. Therefore, expenditures for such purposes as the reinstallation in the fall of storm windows which had been taken down in the spring are not to qualify for the credit. Expenditures for installing insulation or other energy-conserving components removed from one structure and placed on the taxpayer's principal residence will also not qualify because of this requirement.

Insulation is defined as any item specifically and primarily designed to reduce, when installed in or on a dwelling or water heater, the heat loss or gain of the dwelling or water heater.

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[1] For these purposes, the term "condominium management association" means an association meeting the requirements of section 528(c)(1) of the Code, other than subparagraph (E) of that subsection (which requires an election to be taxed under section 528), with respect to a condominium project substantially all of the units of which are used as residences.

[2] In most cases, an individual renting a residence from a member of a condominium management association could not obtain the credit because he would not be assessed for any of the association's expenditures. However, qualifying expenditures made directly by this individual would be eligible for the credit.

[3] It is contemplated that the date when habitation of the dwelling unit by the taxpayer begins would constitute in most cases the date the dwelling would be treated (but for this provision of the bill) as being used as the taxpayer's principal residence.

Except for items which qualify as "other energy-conserving components" (such as storm or thermal windows or doors), items which qualify for this credit are to be primarily and specifically designed for use as insulating materials. Materials which are primarily structural or decorative in purpose would not qualify. For example, carpeting, drapes, wood paneling, and exterior siding would not qualify although they may have been designed in part to have an insulating effect. Moreover, the replacement of an existing wall or the addition of a new wall (except for the qualifying insulation installed in the wall) would not qualify for credit. Attic, floor, and wall insulation made of fiberglass, rock wool, cellulose, or styrofoam are examples of insulating materials qualifying for the credit.

The term "other energy-conserving component" means any item (other than insulation) which is:

(1) a replacement furnace or boiler which is designed to provide more efficient energy utilization by improved heat generation or lowered heat losses;

(2) a furnace replacement burner designed to achieve a reduction in the amount of fuel consumed as a result of increased combustion efficiency;

(3) a device for modifying flue openings designed to increase the efficiency of operation of the heating system;

(4) an electrical or mechanical furnace ignition system which replaces a gas pilot light;

(5) a storm or thermal window or door for the exterior of the dwelling;

(6) any automatic energy-saving setback thermostat;

(7) caulking or weatherstripping of an exterior door or window;

(8) any heat pump which replaces an existing electrical resistance space heating system;

(9) meters which display the cost of energy usage;

(10) fluorescent replacement lighting systems; or

(11) an item of a kind which the Secretary of the Treasury specifies by regulations as increasing the energy efficiency (by conversion or otherwise) of the dwelling.

In promulgating regulations, the Secretary is to consider, among other things, whether polyester window film, attic fans, fireplace jets, and glass fireplace screens constitute items of a kind which increase the energy efficiency of a dwelling. In exercising his authority under this provision, the Secretary is to take into account the relative supply of the type of energy used by the component or equipment under consideration.

The Secretary is directed to prescribe guidelines setting out the criteria which an equipment item must meet if it is to be added to the list of qualifying equipment. The Secretary is also directed to establish procedures under which a manufacturer might apply to have a product added to the qualifying expenditure list. It is contemplated that included among the criteria in making this determination will be whether the item would be available to consumers at a competitive and reasonable price.

The heat pump equipment for which the credit may be claimed includes the heat pump and the parts solely related to the functioning of

the heat pump. It is usually necessary to use conventional heating units as "back-ups" to the heat pump for use or supplemental use during periods when the outdoor temperature falls below approximately 25 degrees Fahrenheit. However, the credit is not to be available for expenditures for these back-up units.

Qualifying storm or thermal windows or doors are to include any multiglazing arrangement whereby a pane of glass is so affixed that it is separated from another pane of glass (or thermal-type window) by air in a space which tends to be enclosed, such as by window sills or other structures containing the glasses; they are also to include heat-absorbing or heat-reflective glazed windows and doors and heat-absorbing or heat-reflective window and door materials. Where an additional pane of glass, plexiglass or other appropriate material is added to an existing window to create the insulating air space, it may be installed either inside or outside the existing exterior opening.

Meters which display the cost of energy usage would include computerized electricity meters and meters which show the cost of energy used by a particular appliance.

In the case of both insulation and other energy-conserving components, the original use of the property must commence with the taxpayer. Both must also be reasonably expected to remain in operation three years and meet performance and quality standards prescribed by the Secretary (after consultation with the Secretary of Energy, Secretary of Housing and Urban Development and other appropriate agencies, such as the National Bureau of Standards). Performance standards would include standards relating to safety in both the installation and operation of the insulation and other energy-conserving components. However, the performance and quality standards will not apply to insulation and other energy-conserving components purchased prior to the promulgation of such standards. The committee is concerned with the potential for consumer fraud in the absence of definitive standards which are to apply to the insulation and energy-conserving components qualifying for the credit. Thus, it is the committee's desire that the regulations establishing these standards be promulgated by the Secretary without unnecessary delay.

In determining whether an item for which the credit is claimed is eligible, and in determining whether a particular item meets performance and quality standards, on-site inspections which are not already authorized and used by a governmental agency in the assessment and collection of income taxes are prohibited, except with the written consent of the resident claiming the credit.

Expenditures by joint occupants

If two or more individuals install qualifying property in or on a dwelling jointly occupied by them as their principal residence, the amount of the credit for any calendar year is to be determined by treating all of the joint occupants as one taxpayer. Thus, a total of $2,000 of qualifying expenditures may be made for that residence, rather than $2,000 for each of the occupants. The amount of the credit allowed to each occupant is to be apportioned according to the same ratio as the amount of qualifying expenditures made by that occupant bears to the total amount of qualifying expenditures made by all the occupants.

The fact that a joint occupant may be unable to claim his credit because his allowable credit does not equal the $10 minimum credit amount is to have no effect upon the computation of the amount of the allowable credits for the other joint occupants.

The maximum expenditure amount ($2,000) is to be reduced by the aggregate of prior years' expenditures on the residence by any of the joint occupants, which expenditures were taken into account in computing the credits for such years. This aggregate amount of prior years' expenditures is not broken down and is not applied in the current year to take account in any way of the specific expenditures of the individual occupants in prior years. For example, assume A and B have together made prior years' qualifying expenditures of $1,600 (A has made qualifying expenditures of $1,200 and B has made qualifying expenditures of $400) on their principal and jointly occupied residence. In the current year, each makes qualifying expenditures of $300, for a total of $600 of current expenditures. Of the $400 of expenditures qualifying for the credits ($2,000 – $1,600), $200 will be allocated to A ($300/$600×$400) and $200 will be allocated to B ($300/$600×$400). The fact that A had previously computed his credit in prior years with respect to $1,200 out of the total $1,600 of expenditures is not relevant to the apportionment of expenditures made in the current year.

Effect on tax basis of residence

In order to avoid a double tax benefit (allowance of a credit and also a reduced gain on a subsequent sale of the residence), the bill requires that any increase in basis of the residence on account of qualified expenditures for insulation or other energy-conserving components be reduced by the amount of the credit which is allowed with respect to the expenditures. The amount of allowed credit would include that part of the credit which was refunded to the taxpayer. For example, assume a taxpayer made $2,000 of qualified expenditures which would normally increase the tax basis of his home by that amount. Assuming the taxpayer was allowed the maximum credit allowable in this case, $400 (of which $200 was refunded to him), the taxpayer's basis in his residence would be increased by only $1,600 (the $2,000 of expenditures minus the $400 allowed credit).

Of course, an owner of a residence would not be entitled to an increase in tax basis with respect to qualifying expenditures of a lessee who uses the residence as his principal residence.

Effective date

The amendments made by this provision are to apply to taxable years ending on or after April 20, 1977, for expenditures made on or after that date and before January 1, 1986.

Revenue effect

This provision is estimated to reduce receipts by $446 mmillion for fiscal year 1978, $616 million for fiscal year 1979, and $992 million for fiscal year 1985.

Energy savings estimate

It is estimated that as a result of the tax credit provisions for residential insulation, oil imports will be reduced by 300,000 barrels of oil per day in 1985.

2. Residential Renewable Energy Source Equipment Credit (sec. 1011 of the bill and new sec. 44C of the Code)

Present law

Under present law, no special tax credit or deduction is allowed for solar, wind, or geothermal energy equipment installed in connection with a residence. However, if installations constitute capital improvements to a residence, the amount of the expenditures involved are added to the taxpayer's basis in the residence for purposes of determining gain or loss on a subsequent sale of that residence.

Reasons for change

Residential use of oil and natural gas energy represents a major portion of the country's total consumption of these fossil fuels. In view of the substantial potential oil and natural gas savings that could result from the use of alternate-energy-source measures for residential purposes, the committee believes that it is appropriate to encourage residential use of solar, wind, geothermal, and other renewable energy source equipment.

At the same time, the committee recognizes that solar, wind, and geothermal energy equipment technology is presently at an early stage of commercialization. In view of this, the committee feels that there is a need to encourage the purchase and installation of this equipment. Thus, the committee decided to provide a credit for a limited number of years in order to accelerate the purchase and installation of this equipment and the development of solar, wind, geothermal, and other renewable energy source technology.

The committee recognizes that presently the most practical and least costly method of use of solar energy is with respect to hot water heaters. In order to encourage the use of solar energy in this manner, the committee decided to provide a two-tiered credit structure, with the first $2,000 of expenditures (the approximate cost of many solar hot water heaters) subject to a higher level of credit (30 percent) than the next $8,000 of expenditures (subject to a 20-percent credit).

Presently, as many as twenty-three States provide tax incentives (principally, property tax exemptions) with respect to residential use of solar energy equipment. The committee hopes that the other States and localities will recognize the need to enact laws in the immediate future which provide property tax exemptions for increases in value resulting from solar, wind, geothermal, and other renewable energy source equipment improvements.

Explanation of provisions

Nature, amount, and period of credit

The committee's bill provides a refundable income tax credit for renewable energy source expenditures for installations in connection with the principal residence of the taxpayer. Renewable energy source expenditures include expenditures for solar, wind, and geothermal

equipment; they also include expenditures for equipment which the Secretary, by regulation, specifies as using any other form of renewable energy and which results in an overall energy savings. The credit is 30 percent of the first $2,000 of qualifying expenditures and 20 percent of the next $8,000 of qualifying expenditures. Thus, the maximum credit on the total qualifying expenditures of $10,000 ($2,000 plus $8,000) is to be $2,200.

This credit is to be refundable. Thus, the credit will be applied against the taxpayer's tax liability, and, to the extent it exceeds the amount of tax liability, the taxpayer would be entitled to a refund. Individuals who obtain loans under the nontax energy provisions of the National Energy Conservation Policy Act (Title II, H.R. 5037, passed by the Senate, September 13, 1977) are nevertheless to be entitled to the refundable credit for the amount of their qualifying expenditures, but it is anticipated that the amount of any loan issued under these provisions would be reduced by the amount of the credit allowed.

In determining the credit, the maximum allowable expenditures (the first $2,000 subject to a 30-percent credit and the next $8,000 subject to a 20-percent credit) are to be reduced by previous expenditures by the taxpayer which were taken into account in computing the renewable energy source credit for prior taxable years. Thus, if a taxpayer expended $2,500 for renewable energy source equipment in 1978 and obtained a credit of $700 ($600 of the credit representing 30 percent of $2,000 plus $100 of the credit representing 20 percent of $500), and he expended another $2,000 for renewable energy source equipment in 1979, his credit for 1979 would be $400, or 20 percent of $2,000.

An individual will be eligible for the maximum credit each time he changes his principal residence. Thus, an individual would be eligible for the maximum credit for qualifying expenditures on his new principal residence, notwithstanding the allowance of the credit for qualifying expenditures on his previous principal residence and notwithstanding the allowance of the credit to a prior owner of the individual's new principal residence.

The entire cost of a renewable energy source property is allowed toward the credit only if at least 80 percent of the use of the property is for personal residential purposes. If less than 80 percent of its use is for personal residential purposes, the amount is reduced proportionately. For example, if a full expenditure of $10,000 is made, but only 50 percent of the use of the property is for personal residential purposes (the other 50 percent of use being for business purposes), the allowed credit will be $1,200 (the allowable credit on $5,000, which is 50 percent of $10,000). For purposes of this provision, use of a swimming pool is not to be treated as personal residential use.

In order to avoid undue administrative burdens due to de minimis claims, a minimum credit amount of $10 for any taxable year is required with respect to any tax return (joint or separate) if any credit is to be allowed. This minimum credit requirement applies to the aggregate of the credits claimed for a taxable year for renewable energy source expenditures and for insulation and other energy-conserving component expenditures.

The credit is to be available for expenditures made on or after April 20, 1977, and before January 1, 1986.

When qualified expenditures are treated as made

Generally, renewable energy source property expenditures are to be treated as made when the original installation of the property is completed. Consequently, for purposes of this provision, the time of payment or accrual of amounts for renewable energy source energy property would not be determinative of when the expenditures for such property have been made.

However, in the case of renewable energy source energy expenditures in connection with the construction or reconstruction [1] of a dwelling, the expenditures are to be treated as made when the taxpayer commences original use of the dwelling as his principal residence. Reoccupation by a taxpayer of a reconstructed dwelling, which he occupied as his principal residence prior to reconstruction, would not constitute the commencing of the original use of the dwelling as his principal residence. In this situation, the general rule stated above, i.e., time when original installation is completed, is to apply in determining when the renewable energy source property expenditure was made.[2]

Qualifying residences

In order to qualify for the credit, installations of renewable energy source equipment must be in connection with an individual's principal residence, and that residence must be located in the United States, Guam, or the U.S. Virgin Islands. The credit is available for existing and newly constructed and reconstructed dwellings. Owners and renters will be eligible for the credit; moreover, an individual who owns stock in a cooperative housing association or who is a member of a condominium management association [3] will be treated as having expended an allocable share of amounts expended by the association for renewable energy source property and will be eligible for the maximum $2,200 credit.

The cooperative stockholder's allocable share of the qualifying expenditures is to be the same as his proportionate share of the cooperative's total outstanding stock. The condominium management association's member's allocable share is to be the amount he is assessed by the association as a result of the renewable energy source expenditures.[4]

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[1] The term "reconstruction" contemplates the destruction and replacement of most of a dwelling's major structures (i.e., floors, walls, ceiling).

[2] It is contemplated that during the period of reconstruction, when the taxpayer must temporarily reside in another dwelling, the reconstructed dwelling would continue to be treated as (assuming it originally was) the taxpayer's principal residence.

[3] For these purposes, the term "condominium management association" means an association meeting the requirements of section 528(c)(1) of the Code, other than subparagraph (E) of that subsection (which requires an election to be taxed under section 528), with respect to a condominium project substantially all of the units of which are used as residences.

[4] In most cases, an individual renting a residence from a member of a condominium management association could not obtain the credit because he would not be assessed for any of the association's expenditures. However, qualifying expenditures made directly by this individual would be eligible for the credit.

The determination of whether a dwelling unit is used by a taxpayer as his principal residence will be made under principles similar to those applicable to section 1034 of the Code (relating to sale or exchange of a principal residence) except that, in relation to renters, ownership of the dwelling unit will not be required. Moreover, in making this determination, the period for which a dwelling will be treated as a taxpayer's principal residence will include the 30-day period preceding the date the dwelling unit would, under principles similar to those applicable to section 1034, be treated as being used as the taxpayer's principal residence. Thus, installations which are completed within the 30-day period preceding the date the residence would (but for this provision) be treated as being used as the taxpayer's principal residence will be eligible for the credit.[5]

Qualifying property

The credit for solar energy property applies to solar equipment (and parts solely related to the functioning of such equipment) which, when installed in connection with a dwelling, uses solar energy to heat or cool the dwelling or to provide hot water for use within the dwelling. Expenditures in connection with the leasing of solar energy equipment (as well as those for the acquisition of this equipment) will qualify for the credit. Subject to the expenditure limitations (30 percent of the first $2,000 and 20 percent of the next $8,000), the yearly solar equipment lease payments will be eligible for the credit. Generally, a solar energy equipment system involves the transformation of sunlight into heat or electricity through the use of such components as collectors (to absorb sunlight and create hot air), rockbeds (to store hot air), thermostats (to activate fans which circulate the hot air) and heat exchangers (to utilize the hot air to create hot water).

The credit for solar energy property applies to "passive solar systems" as well as "active solar systems," or any combination of both these systems. An "active solar system" is based on the use of mechanically forced energy transfer, such as the use of fans to circulate solar generated energy. "Passive solar systems" are based on the use of conductive, convective, or radiant energy transfer, such as the use of portions of a residential structure which serve as solar furnaces so as to add heat to the residence. However, expenditures for materials and components which will serve a significant structural function in the dwelling (e.g., extra-thick walls) would not be eligible for the credit.

The credit for wind energy property applies to wind energy equipment (and parts solely related to the functioning of such equipment) which, when installed in connection with a dwelling, uses wind energy to produce energy (in any form) for personal residential purposes. Generally, wind energy equipment involves a windmill which uses wind to generate electricity and other mechanical forms of energy.

The credit for geothermal energy property applies to geothermal equipment (and parts solely related to the functioning of such equip-

[5] It is contemplated that the date habitation of the dwelling unit by the taxpayer begins would constitute in most cases the date such unit would be treated as being used as the taxpayer's principal residence.

ment [6]) which uses geothermal energy to heat or cool a building or to provide hot water for it. The geothermal equipment must be equipment which is necessary to distribute or use geothermal steam and associated geothermal resources (as defined in sec. 2(c) of the Geothermal Steam Act of 1970—30 U.S.C. 1001(c)). Generally, geothermal energy is derived from geothermal deposits from geothermal reservoirs consisting of natural heat stored in rocks or in an aqueous liquid or vapor (whether or not under pressure). This includes hot brine, dry heat (that may be produced with the use of such a substance as freon) and hot water (such as that which may be used directly to heat a building equipped with a heating unit employing hot water heating).

Renewable energy source property need only be installed in connection with a dwelling, rather than in or on it. Thus, a "collector" (which absorbs sunlight) forming part of a solar energy system need not be installed on the roof or any structure of a house in order to qualify for the credit. Furthermore, qualifying property could include a windmill, solar collector or geothermal well and distribution system jointly owned by a number of families living in separate residential structures.

Renewable energy source property does not include conventional heating or cooling systems which serve to supplement ("backup") the renewable energy source equipment in heating or cooling the residence. Renewable energy source property also does not include expenditures for a swimming pool used as an energy storage medium or any other energy storage medium which serves a dual purpose.

In the case of renewable energy source property, the original use of the property must commence with the taxpayer. This property must also be reasonably expected to remain in operation for at least five years and meet performance and quality standards prescribed by the Secretary of the Treasury (after consultation with the Secretary of Energy, Secretary of Housing and Urban Development and appropriate other agencies, such as the National Bureau of Standards). Performance standards would include standards relating to safety in both the installation and operation of the renewable energy source property. However, the performance and quality standards will not apply to property purchased prior to the promulgation of such standards. The committee is concerned with the potential for consumer fraud in the absence of definitive standards which are to apply to the property qualifying for the credit. Thus, it is the committee's desire that the regulations establishing these standards be promulgated by the Secretary without unnecessary delay.

Pursuant to his authority under the Code (sec. 7805), the Secretary may promulgate regulations (in addition to those relating to performance and quality standards) which specify the solar, wind, and geothermal energy equipment qualifying for the credit. The Secretary is authorized to promulgate regulations which would add to the list of qualifying property those devices which rely on renewable energy sources and which would result in an overall energy savings. The Secretary is directed to prescribe guidelines setting out the criteria which an equipment item must meet if it is to be added to the list of

[6] Thus, expenditures for pipes serving both geothermal and nongeothermal functions would not be eligible for the credit.

qualifying equipment. The Secretary is also directed to establish procedures under which a manufacturer might apply to have a product added to the qualifying expenditure list.

Purchasers of newly constructed or reconstructed homes in connection with which renewable energy source equipment has been installed are eligible for the credit with respect to expenditures for both the equipment itself and for the labor costs attributable to the onsite preparation, assembly, and installation of such equipment. These costs are to include direct labor costs and indirect labor costs (such as the cost of construction supervisory personnel properly allocable to the onsite preparation, assembly, and installation of the equipment). The Secretary may require the taxpayer to supply a certification by the builder or contractor as to cost of the equipment and the labor costs attributable to the onsite preparation, assembly, and installation of such equipment.

In determining whether an item for which the credit is claimed is eligible, and in determining whether a particular item meets performance and quality standards, onsite inspections which are not already authorized and used by a governmental agency in the assessment and collection of income taxes are prohibited, except with the written consent of the resident claiming the credit.

Expenditures by joint occupants

If two or more individuals install qualifying renewable energy source property in connection with a dwelling used jointly by them as their principal residence, the amount of the credit for any calendar year is to be determined by treating all of the joint occupants as one taxpayer. Thus, a total of $10,000 of qualifying expenditures may be made for that residence, rather than $10,000 by each of the residents. The amount of the credit allowed to each occupant is to be apportioned according to the same ratio as the amount of qualifying expenditures made by that occupant bears to the total amount of qualifying expenditures made by all the occupants.

The fact that a joint occupant may be unable to claim his credit because his allowable credit does not equal the $10 minimum credit amount is to have no effect upon the computation of the amount of the allowable credit for the other joint occupants.

The maximum expenditure amount ($10,000) is to be reduced by the aggregate of prior years' expenditures on the residence by any of the joint occupants, which expenditures were taken into account in computing the credits for such years. This aggregate amount of prior years' expenditures is not broken down and is not applied in the current year to take account in any way of the specific expenditures of occupants in prior years. For example, assume A and B have together made prior year qualifying expenditures of $8,000 (A, $6,000 and B, $2,000) on their principal and jointly occupied residence. In the current year, each makes qualifying expenditures of $1,500, for a total of $3,000. Of the $2,000 of expenditures qualifying for the credits ($10,000 −$8,000), $1,000 will be allocated to A ($1,500/$3,000×$2,000) and $1,000 will be allocated to B (1,500/$3,000×$2,000). The fact that A had previously computed his credit in prior years with respect to $6,000 out of the total $8,000 of expenditures would not be relevant to the apportionment of expenditures for the current year.

Effect on tax basis of residence

In order to avoid a double tax benefit (allowance of a credit and also a reduced gain on a subsequent sale of the residence), the bill requires that any increase in basis on account of a qualified renewable energy source expenditure be reduced by the amount of the credit which is allowed with respect to the expenditure. The amount of allowed credit would include that part of the credit which was refunded to the taxpayer. For example assume a taxpayer made $1,500 of qualified expenditures which would normally increase the tax basis in his home by that amount. Assuming that the taxpayer was allowed the maximum credit allowable in this case, $450 (of which $200 was refunded to him), the taxpayer's basis in his residence would be increased by only $1,050 (the $1,500 of expenditures minus the $450 allowed credit).

Of course, the owner of a residence would not be entitled to an increase in tax basis with respect to qualifying expenditures of a lessee who uses the residence as his principal residence.

Effective date

The amendments made by this provision are to apply to taxable years ending on or after April 20, 1977, for expenditures made on or after that date and before January 1, 1986.

Revenue effect

These provisions are estimated to reduce receipts by $27 million for fiscal year 1978, $58 million for fiscal year 1979, and $186 million for fiscal year 1985.

Energy savings estimate for residential credits

It is estimated that as a result of the committee provisions for residential renewable energy source tax credits, oil imports will be reduced by 25,000 barrels per day in 1985.

B. TRANSPORTATION TAX PROVISIONS

1. Extension to 1985 of Existing Rate of Tax on Gasoline and Motor Fuels (sec. 1021 (a) and (c) of the bill and secs. 4041, 4081, 6412 and 6421 of the Code)

Present law

Under present law, a retailers excise tax of 4 cents a gallon is imposed on diesel and other special motor fuels sold for use (or used) in a highway vehicle (sec. 4041).[1] Also, a manufacturers excise tax of 4 cents a gallon is imposed on gasoline sold by the producer or importer (sec. 4081).[2] These taxes are scheduled to be reduced to 1½ cents a gallon on October 1, 1979 (as the Highway Trust Fund—to which the revenues now go—is scheduled to expire as of September 30, 1979).

Reasons for change

The committee believes that, because of the need to conserve energy and reduce gasoline consumption, it would be inappropriate to reduce the price of gasoline on October 1, 1979, by allowing the Federal excise tax on gasoline and other motor fuels to be reduced from 4 cents a gallon to 1½ cents a gallon. Thus, the committee decided to extend the present 4-cents-a-gallon tax rate for six years (until October 1, 1985) as a signal to motorists of the extent of the congressional concern for energy conservation.

Explanation of provision

The bill extends the current 4-cents-a-gallon excise tax on gasoline and other motor fuels for six years, or from September 30, 1979, to September 30, 1985 (after which time, the rate will be 1½ cents a gallon). The bill, however, does not extend the Highway Trust Fund, which is currently scheduled to expire as of September 30, 1979. The committee's bill does not address the question of the specific use of such motor fuel tax revenues after September 30, 1979, except that, until the use is otherwise specified in subsequent legislation, the revenues will go into the general fund of the Treasury.

The committee is aware that other congressional committees will be considering surface transportation authorization legislation during this Congress, and that recommendations will be made regarding the

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[1] The other special motor fuels are benzol, benzene, naphtha, liquified petroleum gas, casinghead and natural gasoline, or any other liquid (other than kerosene, gas oil, fuel oil, gasoline or diesel fuel). (See also discussion below, in section 3, of application of the tax on other special motor fuels in the case of nonhighway use, such as motorboat use.)

[2] Gasoline used for nonhighway purposes or by local transit systems is currently eligible for a refund or credit equal to 2 cents a gallon (sec. 6421). (See also changes made by this bill in the gasoline tax paid by motorboat users, by users for off-highway nonbusiness purposes, and by local transit systems, as well as the tax on other motor fuels used by school buses and local or intercity buses.)

Highway Trust Fund and the present trust fund taxes. The committee also will be giving consideration to these matters later in this Congress, and will decide at that time on the future use of the gasoline and other motor fuels tax revenues.

Effective date

The bill extends the present 4-cents-a-gallon excise taxes on gasoline and other motor fuels from September 30, 1979, through September 30, 1985.

Revenue effect

It is estimated that this provision will increase budget receipts by $3.3 billion in fiscal 1980, $3.4 billion in 1981, and $3.8 billion in fiscal 1985.

Energy savings estimate

This provision will result in a savings of oil consumption of about 28,000 barrels per day in 1980 and about 26,000 barrels per day in 1985.

2. Exemption From Excise Tax or Reduction of Rate for Certain Blended Gasoline (sec. 1021(b) of the bill and secs. 4041 and 4081 of the Code)

Present law

Under present law, motor fuel which is a blend of gasoline and methanol (wood alcohol) or gasoline and ethanol (grain alcohol) would ordinarily be subject to a 4-cent-per-gallon tax if used in a highway vehicle. This is the same rate of tax as would apply to ordinary gasoline used in highway vehicles.

Reasons for change

The committee considers it important to encourage the development of energy sources other than petroleum products. In particular, it is important to develop products which can reduce the use of petroleum products in automobile transportation.

Both methanol and ethanol can be mixed with gasoline in combinations of up to 15 percent methanol or ethanol to make a fuel which can be used by existing automobiles. Neither methanol nor ethanol are currently produced in sufficient quantities or at sufficiently low costs for gasoline-methanol or gasoline-ethanol combinations to be competitive with ordinary gasoline as an automobile fuel. Methanol, which can be made from coal, wood, or urban waste (as well as from natural gas), and ethanol, which can be made from grain or sugar cane, are currently more expensive to produce than ordinary gasoline, and large scale production of either would require very substantial capital investment.

Thus, the committee believes it is appropriate to encourage their production by providing gasahol, that is, gasoline-methanol and gasoline-ethanol blends, with a more favorable treatment under the Federal fuels excise tax than gasoline and petroleum-based fuels. The technology for the production of ethanol from agricultural products and for the production of methanol from forestry products seems to require greater subsidies than for the production of methanol from coal or from urban waste.

Consequently, the committee decided to exempt from Federal excise taxes on motor fuels gasahol blends containing at least 10 percent ethanol or methanol derived from agricultural or forestry products. It also decided to reduce the tax to 3 cents per gallon for gasahol blends of which at least 10 percent of the fuel by volume is methanol produced from nonagricultural and nonforestry products.

Explanation of provision

In general

The bill exempts from the Federal excise taxes on motor fuel gasoline-alcohol blends if such blends contain at least 10 percent ethanol or methanol (or a combination of ethanol and methanol) by volume and if such ethanol or methanol is produced from agricultural or forestry products.

If a gasoline-alcohol blend contains at least 10 percent ethanol or methanol (or a combination of ethanol and methanol) by volume and the ethanol or methanol is not produced from agricultural and forestry products or from natural gas or petroleum, the blend would be subject to Federal motor fuels excise taxes of 3 cents per gallon (rather than 4 cents per gallon).

In the case of ethanol which contains less than 5 percent by volume of a denaturant other than gasoline, the volume of the ethanol is to be treated as including the volume of the denaturant.

Relationship to taxes on alcohol

The committee intends that alcohol used in the production of gasahol not be subject to the Federal excise taxes on distilled spirits. However, no changes were made in these taxes because present law provides that the ethanol [1] potentially subject to tax can be withdrawn from the bonded premises tax-free if it is first denatured by adding 1 gallon of gasoline or 5 gallons of wood alcohol (methanol) for each 100 gallons of alcohol.[2] The requirement in existing law that denaturing occur before the ethanol is removed from the bonded premises is intended to guard against the diversion of the ethanol to uses which would be subject to tax.

Chapter 51 of the Internal Revenue Code sets forth a detailed regulatory scheme for distillery plants and persons involved in the production of alcohol. This regulatory scheme applies to the production of alcohol for industrial uses, as well as production for human consumption. The regulatory scheme requires the registration of a distillery and an investigation of the background of the individuals operating the distillery prior to its commencement of business. This scheme also requires approval of even the most minute details of plant construction and provides for continuing supervision by employees of the Bureau of Alcohol, Tobacco and Firearms.

The committee intends that producers of gasahol should be encouraged to begin commercial production of gasahol as soon as possible subject to the minimum amount of regulation needed to insure against violation of the alcohol taxes.

Consequently, the bill provides specific instructions to the Secretary of the Treasury to expedite, to the maximum extend possible, the applications of persons desiring to produce ethanol for use in gasahol. (and to the House Committee on Ways and Means) within 6 months after the date of enactment suggesting legislative amendments which could reduce the amount of regulation to which gasahol producers would be subject without undermining the basic goal of regulation of producers of alcohol—preventing the use of untaxed alcohol for human

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[1] Ethanol, but not methanol, is generally subject to a tax of $10.50 on each proof gallon when it is withdrawn from the distillery (or other bonded premises) unless certain exceptions, which are generally intended to insure that the alcohol is exported or is not used for human consumption, apply (secs. 5001, 5002, and 5214).

[2] Section 5214(a)(1)(C) of the Code provides that alcohol can be withdrawn from bonded premises free of tax for use as fuel after it has been denatured in an appropriate manner. The regulations state that approved manners of denaturing alcohol include adding 1 gallon of gasoline per 100 gallons of alcohol (27 CFR § 212.38 (1976)) or adding 5 gallons of wood alcohol per 100 gallons of alcohol (27 CFR § 212.16 (1976)).

consumption. It is intended that this report be based on a thorough investigation by the Bureau of Alcohol, Tobacco, and Firearms in conjunction with appropriate Treasury Department officials.

Effective date

These provisions apply to sales or use after January 1, 1978, and before October 1, 1985.

Revenue effect

It is estimated that this provision will reduce budget receipts by less than $5 million per fiscal year through 1983, by $9 million in 1984, and by $12 million in 1985.

Energy savings estimate

This provision is estimated to result in negligible energy savings.

3. Removal of Refund or Credit for Excise Taxes on Motor Fuels and Lubricating Oil for Nonbusiness, Off-Highway Use (secs. 1022 and 1023 of the bill, secs. 39, 4041(b), 6421, and 6424 of the Code, and sec. 201(b) of the Land and Water Conservation Fund Act of 1965)

Present law

Under present law, a 4-cents-a-gallon manufacturers excise tax is levied on the sale of gasoline by the producer or importer (sec. 4081). However, when the fuel is used in other than a highway vehicle which is registered, or is required to be registered, for highway use, the ultimate purchaser may obtain a refund of 2 cents a gallon on his purchase (sec. 6421) or credit against his income tax (sec. 39). Use of gasoline in a motorboat thus qualifies under present law for a credit or refund of 2 cents a gallon. This credit or refund is also available for nonbusiness off-highway use by such vehicles and equipment as minibikes, snowmobiles, power lawn mowers, chain saws and other yard equipment.

The 4-cents-a-gallon retailers excise tax on special motor fuels (sec. 4041(b))[1] applies only to fuels sold for use (or used) in a motor vehicle or motorboat. However, the rate of tax is only 2 cents a gallon if the purchaser is to use them in other than a highway vehicle which is registered, or required to be registered, for highway use. If special motor fuels are sold at the 4-cent rate, and used in a manner qualifying for the 2-cent rate, the purchaser is entitled to a 2-cent-a-gallon payment on such use (sec. 6427); the payment is by a refund or income tax credit in the same manner as the gasoline tax payment.

Diesel fuel also is taxed at 4 cents a gallon, but the tax does not affect motorboats or other nonhighway vehicles, as the fuel is taxed only when sold for use, or used, in a diesel-powered highway vehicle (sec. 4041(a)).[2]

Under present law, a manufacturer's excise tax of 6 cents a gallon is imposed on lubricating oil (other than cutting oils) (sec. 4091). However, if lubricating oil which is subject to tax is used otherwise than in a highway motor vehicle, the ultimate purchaser is eligible for a refund or income tax credit of the full 6 cents per gallon (secs. 39 and 6424).

The net proceeds from the fuel taxes collected from fuel used in motorboats are transferred to the Land and Water Conservation Fund[3] (after first having been appropriated to the Highway Trust Fund).

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[1] The fuels are benzol, benzene, naphtha, liquefied petroleum gas, casinghead and natural gasoline, and any other liquid fuel (other than kerosene, gas oil, fuel oil, gasoline, or diesel fuel).

[2] Diesel fuel is taxed at a rate of 2 cents a gallon if it is sold for use or used as a fuel in a diesel powered highway vehicle (1) which is not registered or required to be registered for highway use, or (2) which is owned by the United States and is not used on the highway.

[3] Moneys from the Land and Water Conservation Fund are used by the Federal Government for acquisition of recreation land (e.g., National Parks or other recreation areas) and for matching grants (on a 50/50 basis) to States for acquisition and/or development of recreation lands (e.g., State or local parks or other recreation areas). (16 U.S.C. 4601–5 and following.)

Reasons for change

The committee considers it to be in the interest of the national energy conservation policy to treat motorboat fuel use the same as highway fuel use. Thus, the committee believes it appropriate at this time to remove the present 2-cents-a-gallon refund or credit for motorboat use of gasoline and other special motor fuels.

Furthermore, the committee does not believe it to be in the interest of national energy conservation to allow a credit or refund of 2 cents a gallon for gasoline or of the entire 6-cents a gallon tax on lubricating oil where the gasoline or oil is used for nonbusiness, off-highway uses.

In addition, elimination of these excise tax refunds or credits for nonbusiness off-highway use of gasoline, other motor fuels and lubricating oil would simplify the filling out of the income tax return for nonbusiness taxpayers by eliminating one line from consideration, and it would result in loss of the credit for only about 340,000 returns on which it is currently claimed.

Moreover, since the user tax contribution from motorboats is increased by this provision, the committee concluded that the revenues from the 2-cents-a-gallon increase in the fuels tax on motorboat use should be transferred to the Land and Water Conservation Fund (as are the revenues from the present 2-cents-a-gallon tax) to be available for, among other things, the provision of increased funding of water recreational facilities used by motorboats.

Explanation of provision

The bill removes the current 2-cents-a-gallon reduction in the taxes on gasoline and special motor fuels (other than diesel fuel) for fuel used in a motorboat. Therefore, the taxes on motor fuels used in a motorboat (other than diesel fuel, which remains exempt from tax) would be 4 cents a gallon, the same as for motor fuels used in a highway vehicle.

The bill also removes the 2-cents-a-gallon credit or refund of the excise tax on gasoline used for nonbusiness, off-highway use. (Under present law, the excise tax on special motor fuels is not applicable to nonbusiness, off-highway use of fuel unless it is used in a motorboat or in certain motor vehicles which are not operated on the highway.)

In addition, the bill also removes the refund or credit of the 6-cents-a-gallon tax on lubricating oil which is used for nonbusiness, off-highway purposes.

The additional 2-cents-a-gallon fuels taxes on motorboat use will be transferred into the Land and Water Conservation Fund, to be available for expenditure for purposes under that fund.

Effective date

These provisions are effective on and after January 1, 1978.

Revenue effect

It is estimated that this provision will increase budget receipts by by $4 million per year beginning with fiscal year 1979. Almost all of these amounts would be transferred to the Land and Water Conservation Fund.

Energy savings estimate

This provision is estimated to result in negligible energy savings.

4. Repeal of Excise Tax on Buses and Bus Parts (secs. 1024 and 1025 of the bill and secs. 4061, 4063, 4221 and 6416(b)(2) of the Code)

Present law

Under present law, a 10-percent manufacturers excise tax is imposed on the sale of buses having a gross vehicle weight of more than 10,000 pounds (sec. 4061(a)).[1] However, present law provides for an exemption from this tax for "local transit buses"; that is, those "which are to be used predominantly by the purchaser in mass transportation service in urban areas" (sec. 4063(a)(6)).[2] The tax also does not apply to school buses sold to any person for "exclusive" use in transporting students and employees of schools operated by State or local governments or by tax-exempt educational organizations (sec. 4221(e)(5)).[3]

Present law also contains an 8-percent manufacturers excise tax on parts and accessories (other than tires and inner tubes, which are taxed separately under sec. 4071) of the type used on buses and trucks (sec. 4061(b)).[4] There are no exemptions from this tax for parts and accessories sold for use on local transit buses or privately-owned school buses.

The revenues from the excise taxes on buses and bus parts go into the Highway Trust Fund (through September 30, 1979).

Reasons for change

The committee considers it desirable to encourage the use of bus transportation because it is a more energy-efficient mode of transportation than use of private automobiles. In addition, the committee believes that the tax distinction between local transit buses and intercity buses (scheduled and charter) should be removed, as both types of bus transportation conserve energy as compared with private auto transportation (upon which there is no manufacturers excise tax for the purchase of either the passenger automobile or the related parts and accessories). Consequently, the committee decided that the excise taxes on buses and bus parts and accessories should be repealed.

Explanation of provision

The committee's bill repeals the 10-percent excise tax on all buses as well as the 8-percent tax on bus parts and accessories.

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[1] This tax is scheduled to be reduced to 5 percent for sales on or after October 1, 1979.

[2] This exemption applies to privately-owned local transit buses, since "public" transit buses are exempted under the provision exempting State and local governments from manufacturers excise taxes (sec. 4221(a)(4)).

[3] This exemption applies to persons purchasing school buses for contract operation to transport school students or employees; school buses sold directly to State and local governments and to tax-exempt educational organizations for their exclusive use are already exempted under the general manufacturers excise tax exemption provisions for State and local governments (sec. 4221(a)(4)) and for tax-exempt educational organizations (sec. 4221(a)(5)).

[4] This tax is also scheduled to be reduced to 5 percent on October 1, 1979.

Tax on buses

With respect to the 10-percent excise tax on buses, floor stocks refunds are provided in the case of tax-paid buses in dealers' inventories as of the day after the date of enactment. Also, consumer refunds are provided in the case of sales made on or after April 20, 1977, and on or before the date of enactment. The floor stocks refunds and consumer refunds are essentially similar to those generally provided on past occasions for repealed excise taxes, such as in the Revenue Act of 1971 (when the manufacturers excise tax was repealed for automobiles and light-duty trucks).

Floor stocks refunds.—Floor stocks refunds of the 10-percent tax paid by a manufacturer, producer, or importer are provided for buses held in dealers' inventories as of the day after the date of enactment of this Act if the bus has not been used and is intended for sale. The amount of tax is to be credited or refunded (without interest) to the manufacturer, producer, or importer, if certain conditions are met.

The claim for the credit or refund must be filed with the Secretary of the Treasury before the first day of the 10th calendar month beginning after the day after the date of enactment based upon a request from a dealer submitted to the manufacturer, producer, or importer before the first day of the 7th calendar month beginning after the day after the date of enactment. Further, reimbursement of the tax amount must be made to the dealer by the manufacturer, producer, or importer on or before the first day of the 10th month, or written consent must be obtained from the dealer regarding allowance of the credit or refund. No credit or refunds is to be allowed to a manufacturer, producer, or importer without such evidence of the dealer's inventory for which the credit or refund is claimed as may be required under Treasury regulations.

Consumer refunds.—The bill also provides for consumer refunds of the 10-percent tax for bus purchases made on or after April 20, 1977, and on or before the date of enactment. The amount of the tax is to be credited or refunded (without interest) to the manufacturer, producer, or importer: (1) if the taxpayer has evidence of the sale to the ultimate purchaser and of the reimbursement of the tax to the purchaser (as may be required by Treasury regulations); (2) if the claim for the credit or refund is filed before the first day of the 10th calendar month beginning after the day after the date of enactment based upon information supplied before the first day of the 7th calendar month beginning after the day after enactment by the person who sold the bus; and (3) if reimbursement of the tax has been made to the ultimate purchaser on or before the first day of such 10th calendar month.

Other provisions.—Any tax paid by reason of section 4218(a) (relating to use by the manufacturer or importer considered a sale) is to be treated as an overpayment of the tax if the tax is imposed on or after April 20, 1977. The term "dealer" includes a wholesaler, jobber, distributor, or retailer. A bus is considered as "held by a dealer" if the title has passed to the dealer (whether or not delivery has been made), and if, for purposes of consumption, the title (or possession) has not at any time been transferred to any person other than a dealer.

Tax on bus parts

The bill also repeals the 8-percent manufacturers excise tax on bus parts and accessories. Under regulations prescribed by the Secretary of the Treasury, the parts and accessories tax imposed by section 4061(b) is not to apply to any part or accessory which is "sold for use" by the purchaser on or in connection with a bus. It is contemplated that such parts and accessories would be sold tax-free by the manufacturer, producer, or importer for use on or in connection with a bus only if appropriate evidence of exemption is furnished by the purchaser. If the sale of the parts and accessories is made other than by the manufacturer, producer, or importer, the bill provides for a refund of the 8-percent tax where the part or accessory is "sold for use" by the purchaser on or in connection with a bus. Thus, parts and accessories that may be interchangeable between trucks and buses will continue to be subject to the parts tax if they are not "sold for use" with respect to buses.

There is no provision for floor stocks refunds or consumer refunds with respect to the repeal of the excise tax on bus parts and accessories, because the relatively small amount of tax per unit would not appear to cause a delay in consumer purchases, and because there would be considerable administrative burden in providing and processing such refunds.

Effective date

Tax on buses

The repeal of the 10-percent excise tax on buses is effective for sales by the manufacturer, producer, or importer on or after April 20, 1977. An article is to be considered as sold before April 20, 1977, if possession or right to possession passes to the purchaser before that time.

In the case of partial payments of tax in connection with leases, certain types of installment sales, conditional sales, or certain types of chattel mortgage arrangements, present law (sec. 4216(c)) provides that the manufacturers excise tax is to be paid upon each partial payment and is to be based on the tax rate in effect on the date each partial payment is due. To avoid windfall benefits to a manufacturer where the lease, installment sale, etc., took into account the 10-percent tax, the bill provides that no tax is due on partial payments made on or after April 20, 1977, if the lessor or vendor establishes that the amount of the payments payable on or after that date has been reduced by the amount of tax that would otherwise have been due with each partial payment on or after that date. If the lessor or seller does not establish that the payments have been so reduced, the tax reduction provided by the bill is not to apply to the article on which those partial payments are being made. In other words, for the tax reduction to be available in partial payment cases, the benefit of the repeal must be passed on to the lessee or purchaser.

Tax on bus parts

The repeal of the 8-percent excise tax on bus parts and accessories is effective for sales by the manufacturer, producer, or importer on or after the first day of the first calendar month beginning more than 10 days after the date of enactment.

Revenue effect

Tax on buses

It is estimated that the repeal of the 10-percent excise tax on buses will reduce budget receipts by $13 million for fiscal 1978 (which includes the floor stocks and consumer refunds) and $9 million per year thereafter.

These amounts would otherwise go into the Highway Trust Fund (through September 30, 1979).

Tax on bus parts

The repeal of the 8-percent excise tax on bus parts and accessories is estimated to reduce budget receipts by $3 million for fiscal year 1978 and each year thereafter.

These amounts would otherwise go into the Highway Trust Fund (through September 30, 1979).

Energy savings estimate

These provisions are estimated to result in negligible energy savings.

5. Removal of Excise Tax on Certain Items Used on or in Connection with Intercity, Local, or School Buses (sec. 1026 of the bill and secs. 4071, 4092, 4221(e), 6416(b), 6421(b)(1), 6424 and 6427 of the Code)

Present law

Presently, privately owned and operated buses use products that are subject to the manufacturers excise taxes on tires, tubes and tread rubber,[1] gasoline,[2] and lubricating oil,[3] as well as the retailers excise tax on diesel fuel and other special motor fuels.[4] Complete exemption is provided from these excise taxes for State and local governments (secs. 4041(g)(2) and 4221(a)(4)) and for tax-exempt educational organization (secs. 4041(g)(4) and 4221(a)(5)). A partial exemption (2-cents-a-gallon refund or credit) is available from the tax on gasoline and other motor fuels for use by a privately owned local transit system for the portion of its total fare revenue represented by "commuter fare revenue" (secs. 6421(b) and (d)(2) and 6427(b)).[5]

The revenues from these taxes paid with respect to highway use now go into the Highway Trust Fund (through September 30, 1979).

Reasons for change

Since bus transportation is more energy-efficient than private automobile transportation, the committee believes it desirable to encourage greater use of bus transportation. In addition, the committee considers it appropriate to make the excise tax treatment of private transit and school bus operations consistent with governmental and tax-exempt educational bus operations. Therefore, the committee decided to extend the present exemptions from the taxes on tires, tubes and tread rubber, gasoline and other motor fuels, and lubricating oil to privately owned intercity and local bus operations and private school bus operations not presently exempt from these taxes.

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[1] A tax of 10 cents a pound on highway tires and inner tubes and of 5 cents a pound on tread rubber for highway use (sec. 4071). (The taxes on highway tires and inner tubes are scheduled to be reduced to 5 cents a pound and 9 cents a pound, respectively, on October 1, 1979, while the tax on tread rubber expires on that date.)

[2] A tax of 4 cents a gallon (sec. 4081).

[3] A tax of 6 cents a gallon (sec. 4091).

[4] A tax of 4 cents a gallon (sec. 4041).

[5] The partial exemption is available only if at least 60 percent of the total passenger fare revenue derived during a calendar quarter from "scheduled common carrier public passenger land transportation service along regular routes" is from "commuter fare revenue." Commuter fare revenue is defined (sec. 6421(d)(2)) as fares derived from transportation of persons and attributable to (1) amounts paid which do not exceed 60 cents, (2) amounts paid for commuting or season tickets for single trips of less than 30 miles, or (3) amounts paid for commuting tickets for one month or less.

Explanation of provisions

The bill removes the excise taxes on highway tires, inner tubes and tread rubber, gasoline and other motor fuels, and lubricating oil for private intercity, local and school bus operations.

In the case of the excise taxes on highway tires, inner tubes and tread rubber, the bill provides an exemption for sales by a manufacturer, producer, or importer of such items "sold for use" by the purchaser on or in connection with an intercity, local, or school bus. It is contemplated that such tires, tubes and tread rubber would be sold tax-free only if appropriate evidence of exemption is furnished by the purchaser. Where the sale of such items is made other than by the manufacturer, producer, or importer, the bill provides for a refund (or credit) of the tax when the item is "sold for use" by the purchaser on or in connection with an intercity, local, or school bus.

An "intercity or local bus" means any bus which is used predominantly in furnishing (for compensation) passenger land transportation available to the general public if either (1) the transportation is scheduled and along regular routes, or (2) the passenger seating capacity of the bus is at least 20 adults (not including the driver).[6] Thus, under the first alternative portion of this definition, a bus which is used predominantly (that is, more than 50 percent) in providing (for compensation) scheduled transportation along regular routes (such as is provided by local transit systems or an intercity bus operation providing regularly scheduled service along regular routes) will qualify for the exemption from the taxes on tires, tubes, and tread rubber, regardless of the size of the bus involved. For nonscheduled (i.e., charter) operations (covered by the second alternative portion of the definition), the exemption is available only if the bus has a passenger seating capacity of at least 20 adults (not including the driver) and the transportation is available to the general public. The purpose of the "at least 20 passenger" requirement is to insure that, in situations where regularly scheduled service is not being furnished, vans and similar vehicles used for vanpooling or taxi service are not eligible for the exemption from these taxes (and the fuels taxes).

Charter service is to be considered "available to the general public" if the taxpayer offers this service to more than a limited number of persons or organizations. For example, if a bus operator normally provides charter operations through travel agencies, but his buses are available for chartering by the general public, the buses predominantly used in providing such service would be considered "intercity or local buses." However, if the bus operator is engaged in providing charter services to only one person, group, or organization, or a limited number of persons, with respect to a particular bus, such a bus would not qualify as an "intercity or local bus." The purpose of this limitation is to provide these exemptions only for buses which are used in a passenger transportation business available to the general public (for compensation) and not to buses used primarily as part of a nontransportation

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[6] The type of use which would qualify as "use in passenger land transportation available to the general public" includes not only mileage traveled with passengers (which otherwise meets the use qualification), but also use which is incident to such passenger transportation (such as "deadheading").

business or for the personal use of the operator, one family, one group, or organization, or contract use with a limited number of persons.

A "school bus" means any bus with respect to which "substantially all" (that is, at least 85 percent) of the use involves transporting students and employees of schools. If, in connection with the transportation of students or employees of schools, a bus is driven without passengers to or from a point to or from which students or employees of schools are transported (that is, so-called "deadheading"), this use shall be considered as a use which involves transporting students or employees of schools. A school is any educational organization which normally maintains a regular faculty and curriculum and normally has a regularly enrolled body of students in attendance at the place where the educational activities are regularly conducted. Thus, the exemption from these taxes applies to use by both tax-exempt and taxable schools. Also, it applies to a private contractor who operates a bus for tax-exempt or taxable schools.

The bill provides for the refund or credit of the taxes paid with respect to lubricating oil used in an intercity, local, or school bus. If the bus meets the "predominant use" or "substantially all the use" test, the tax on all the lubricating oil used in the bus is to be credited or refunded.

In addition, the bill provides for the refund or credit of the taxes paid on gasoline and other motor fuels but only to the extent these fuels are used in a bus engaged in furnishing (for compensation) passenger land transportation available to the general public or in school bus transportation operations. The allocation of fuel to these nontaxable uses may be determined on a mileage basis (for the same or comparable vehicles) or on an actual fuel use basis. Use in "passenger land transportation available to the general public" means the same type of use that would qualify in meeting the predominant use test for intercity or local buses, and use in school bus transportation operations means the same type of use that would qualify in meeting the "substantially all the use" test for school buses.

Effective date

These provisions are effective on the first day of the first calendar month which begins more than 10 days after the date of enactment of this Act.

Revenue effect

These provisions are estimated to reduce budget receipts by $13 million for fiscal year 1978 and each year thereafter. These revenues would otherwise go into the Highway Trust Fund (through September 30, 1979).

Energy savings estimate

It is estimated that the energy savings as a result of these provisions will be negligible.

6. Tax credit for vans used in van pooling (sec. 1027(a) of the bill and new sec. (46(c)(6) of the Code)

Present law

Under present law, an employer who purchases a van to transport individuals to and from work may claim the regular investment credit with respect to the purchase of the van.[1] Since vans designed for transportation of passengers normally are treated as having a useful life of about 4 years, the investment credit with respect to such vans is 3⅓ percent of the purchase price in the case of a van used exclusively for business purposes.

Reasons for change

A small but increasing number of employers have begun purchasing vans (or buses) to provide transportation for their employees to and from work. This "van pooling" is an energy efficient means of transportation in comparison to commutation to work by private automobile. Frequently, the employer can defray at least the operating expenses of the van by charging the employees for these expenses.

The purchase of a passenger van which would seat at least nine individuals is relatively expensive. These vans normally cost about $8,000 at the current time. The committee concluded that it was desirable to provide a greater incentive for the purchase of such vans for van pooling purposes than is provided under current law. Accordingly, the committee amendment provides a 20 percent credit for the purchase of a van by an employer to be used for van pooling purposes if the useful life of the van is at least 3 years.

Explanation of provision

The bill provides that, if an employer purchases a new van with a useful life of at least 3 years and a seating capacity of nine persons (including the driver) and substantially all the use of the van is for transporting his employees to and from work, the employer is entitled to the full 10 percent investment credit and the special 10 percent business energy investment credit.

To qualify for this treatment, substantially all the use of the van must be for the transporting of the taxpayer's employees to and from their places of employment, and the number of employees transported on a regular basis must be at least equal to one-half of the maximum number of persons (including the driver) that the van is designed to carry. This van pooling use may be on a for profit or nonprofit

[1] The investment credit is available only for property with respect to which a deduction for depreciation is allowable on the property. Consequently, if the van is used in part for business purposes and in part for personal use, the investment credit would be available only with respect to the proportionate part of the basis of the van which corresponds to the portion of the usage for business purposes.

basis in which the costs of such arrangements are primarily paid for by the individuals utilizing such arrangement or by the employer of such individuals.

If, prior to the expiration of 36 months from the time the van is placed in service, it ceases to be used for van pooling purposes, both the regular investment credit and the business energy investment credit shall be recaptured.

Use of a van for purposes other than van pooling shall not result in a recapture of the credit if substantially all (that is, at least 85 percent) of the use of the van on a mileage basis for at least 36 months after purchase is for van pooling.

Effective date

This provision applies to vans purchased after December 31, 1977 and before January 1, 1986.

Revenue effect

It is estimated that this provision will result in a decrease in budget receipts of less than $1 million annually.

Energy savings estimate

This provision will result in a negligible energy savings.

7. Exclusion from income of certain employer-furnished transportation (sec. 1027(b) of the bill and new sec. 124 of the Code)

Present law

Under present law, it is provided that, in the absence of provisions to the contrary, "gross income means all income from whatever source derived" (sec. 61). However, many specific statutory exceptions have been provided and there is considerable uncertainty about the taxation of certain noncash benefits furnished to employees.

Reasons for change

An increasing number of employers are providing their employees with transportation to and from work by van. The providing of such transportation either at no charge or below cost could be viewed as an item of gross income to the employee in an amount equal to the difference between the fair market value of the transportation and the amount charged the employee.

The furnishing of transportation to and from work by van or bus in "van pooling" results in the saving of energy, and the committee believes it desirable to encourage this activity by providing a clear rule that the value of such transportation in excess of its cost to the employee will not constitute income to the employee.

Explanation of provision

The bill provides that, in the case of a taxpayer who is an employee, gross income does not include the value in excess of the employee's cost of transportation to or from work furnished by an employer if such transportation is in a commuter van. The term "commuter van" means a vehicle capable of carrying 9 or more adult passengers (including the driver) and substantially all the use of which is for the purpose of transporting employees to and from their places of business. Also, for a vehicle to qualify as a commuter van, the number of employees transported on a regular basis must be at least equal to one-half of the maximum number of persons (including the driver) that the vehicle is designed to carry.

The definition of "employee" is very broad. In the case of a partnership, a partner who has earned income (within the meaning of section 401(c)(2)) from the partnership is treated as an employee and the partnership is treated as the employer. Similarly, an individual who owns the entire interest in a sole proprietorship shall be treated as an employee if the individual has earned income (within the meaning of section 401(c)(2)) and he shall also be treated as his own employer.

The exclusion does not apply to the value of transportation furnished under an arrangement which discriminates in favor of employees who are officers, shareholders, self-employed individuals, or highly compensated. This broad anti-discrimination provision

(patterned on the anti-discrimination rules of section 401(c)(4)) is intended to encourage employers to make the benefits of van pooling available to all employees on the same basis and to discourage the use of van pooling as a fringe benefit to limited classes such as officers, shareholders, and highly compensated individuals. However, in determining whether the classification is discriminatory, the employer may exclude from the calculations those employees who are members of a collective bargaining unit if there is evidence that benefits of the van pooling arrangement were the subject of good faith bargaining between representatives of that group and the employer.

No inference is intended as to whether gross income includes the value of transportation to and from work in other situations, such as where the transportation is furnished by car or limousine. It is anticipated that this issue may be examined when the committee reviews the taxation of fringe benefits.

Furthermore, no change in existing law is intended as to whether (or the extent to which) deductions are available to the employer for furnishing such transportation.

Effective date

This provision applies to transportation furnished after the January 1, 1978 and before January 1, 1986. However, no inference is intended as to transportation furnished during other periods.

Revenue effect

It is estimated that this provision will result in a decrease in budget receipts of less than $1 million annually.

Energy saving estimate

This provision is estimated to result in negligible energy savings.

8. Tax Credit for Electric Motor Vehicles (sec. 1028 of the bill and new sec. 44D of the Code)

Present law

Under present law, there is no special income tax credit available with respect to the purchase of an electric motor vehicle,[1] and there also is no other special tax incentive to aid in the development of electric motor vehicles.

Reasons for change

The committee believes that the development of electric motor vehicles should be encouraged as part of the overall program to reduce the use of petroleum. Presently, electric motor vehicles are characterized by very limited range and speed, in large part, because of the weight and storage capacity of their batteries. To assist in developing a larger market which would contribute to an improvement in the present level of performance of electric motor vehicles, the committee concluded that a tax credit for the purchase of these vehicles would be appropriate. Greater use of electric motor vehicles (principally as a second car for local trips) should reduce petroleum consumption as well as noise and air pollution. Since the batteries of these vehicles will generally be recharged during nonpeak load periods for local utilities companies, there may be some energy savings compared to the use of petroleum, without requiring any additional capital investment. In addition, since most electricity is now generated by the use of coal, there will be a substitution of the use of coal for petroleum to the extent that this part of the automobile sector is increased.

Explanation of provision

The bill provides a nonrefundable tax credit for individuals for 100 percent of the cost of a qualified electric motor vehicle, up to a maximum credit of $300.[2] This credit is available only if the individual acquires the qualified electric motor vehicle exclusively for his personal use or the personal use of a member of his family.[3] A qualified electric motor vehicle is a 4-wheeled vehicle manufactured primarily for use on public roads and powered by an electric motor which obtains

[1] A purchaser of an electric motor vehicle who uses the vehicle in his trade or business would, of course, be able to claim the investment credit and depreciation in the same manner as for other tangible personal property.

[2] In the case of joint acquisition by 2 or more individuals, the total credit available is not to exceed $300, and is to be allocated among the purchasers in proportion to their respective shares of the cost.

[3] Since the investment credit and accelerated depreciation are available for electric motor vehicles purchased for business purposes, the committee believes that no additional incentive is appropriate for vehicles purchased for business purposes.

If an individual is eligible to claim the investment credit with respect to any portion of the cost of an electric motor vehicle (because the vehicle is used in part for business purposes), the individual cannot claim any portion of the new credit for qualified electric motor vehicles.

current from rechargeable storage batteries or other portable sources of electric current. The original use of the vehicle must begin with the taxpayer or his family, i.e., the credit is not available for used electric cars or cars converted to electricity.

Effective date

The credit applies to qualified electric motor vehicles acquired on or after April 20, 1977, and before January 1, 1986.

Revenue effect

This provision is estimated to reduce budget receipts by less than $500,000 in year 1978 and by $10 million in fiscal year 1985.

Energy savings estimate

The energy savings under this provision are estimated to be negligible.

9. Intercity Bus Credit (sec. 1029 of the bill and new sec. 44E of the Code)

Present law

Present law provides no special tax incentives for taxpayers providing regularly scheduled intercity bus service.[1]

Reasons for change

The intercity bus network plays a vital role in the nation's total intercity passenger transportation process. Of the means of public transportation, the bus provides by far the most comprehensive service. Intercity bus service is available at approximately 16,000 locations as compared to only 670 serviced by air transportation and 500 by passenger trains. In many rural areas, intercity bus service is the only form of public intercity transportation accessible. The intercity bus lines in this country serve approximately 96 percent of communities with 2,500 to 5,000 residents and all those with over 5,000 residents. In addition, intercity bus transportation is utilized by low income groups and senior citizens to a much larger extent than other modes of intercity transportation. These groups in particular are adversely affected by increased energy costs.

Furthermore, intercity buses are the most fuel efficient form of intercity travel based on passenger miles per gallon of fuel consumed. Consequently, diversion of intercity travel from automobiles to buses can result in energy savings.[2]

The net operating revenues of the intercity bus companies have been substantially reduced in recent years and they have been unable to make desired purchases of new equipment and upgrade terminals to attract new customers. From 1972 to 1976, operating revenues of the largest 81 intercity bus operators increased by 28.5 percent over 1972 levels, but expenses over the same period increased 38.1 percent. Thus, net operating revenue (the difference between gross operating revenue and operating expenses) was cut in half.[3] The increased expenses are in large part attributable to increases in the costs of energy and equipment.

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[1] Of course, these taxpayers are eligible for such generally available investment incentives as the investment credit and accelerated depreciation.

[2] In particular, if persons can be encouraged to utilize excess capacity on intercity buses rather than driving their automobiles, all the fuel that would have been expended by their intercity automobile trips can be saved.

[3] In the bus industry, profitability is conventionally measured by the operating ratio—that is, the percent that operating expenses are of operating revenues. Prior to 1973, the intercity bus industry consistently had an operating ratio in the range of 85 to 90 percent. This left an operating profit margin of approximately 10 to 15 percent of revenues. However, the operating ratio reached 95.5 percent in 1976, leaving a margin between revenues and expenses of only 4.5 percent.

Consequently, the committee feels that the intercity bus industry should be given financial assistance in the form of tax incentives to enable it to improve its services, particularly on regularly scheduled routes. In particular, the committee feels that it is appropriate to assist the intercity bus companies by the use of a refundable tax credit which is based upon the number of passenger miles traveled along regularly scheduled routes by the taxpayer and the relative fuel efficiency of the taxpayer's operations. It also believes that a substantial portion of this credit should be required to be invested in terminals and equipment and that a substantial portion of the credit should be utilized to reduce fares, particularly in situations where buses are operating at less than full capacity. By attracting more people to utilize intercity bus transportation, the fare reductions would serve to increase bus efficiency on a passenger mile per gallon basis and might well divert some people from the use of their automobiles.

Explanation of provisions

In general

The bill provides a refundable tax credit for intercity bus operators based on the operator's bus passenger miles and the per passenger mile fuel efficiency of the taxpayer's intercity buses in comparison to the per passenger mile fuel efficiency of automobiles. It is designed so that a bus operator is required to use the credit (estimated to be $200 million for the industry) for fare reductions and investment in equipment and terminals (50 percent of the credit will be earmarked for fare reductions and the remaining 50 percent will be earmarked for investment in terminals and equipment).

Eligibility

This credit is available only to a common carrier which furnishes regularly scheduled intercity ground transportation by motor bus. Thus, it would not apply to a taxpayer which only has charter operations. In the case of a taxpayer with regularly scheduled operations and charter operations, the credit is computed by taking into account only the passenger miles furnished along regularly scheduled routes.[4]

Computation of credit

The credit is computed by multiplying a rate of 20 percent times a base. The base is the product of:

(1) the taxpayer's intercity bus passenger miles on regularly scheduled routes for the taxable year, as reported to the Interstate Commerce Commission ("ICC") or a State regulatory agency (or agencies), if the taxpayer is not subject to ICC regulation,

(2) an amount which reflects the difference between the fuel cost of an intercity auto passenger mile and the fuel cost of an intercity bus passenger mile for the taxpayer, and

(3) a fuel efficiency ratio (3.8), which is the ratio of passenger miles per gallon of intercity buses for 1976 to the passenger miles per gallon of intercity automobiles for 1976.

[4] Essentially, the credit is based only upon regularly scheduled operations because charter operations are normally characterized by operation at or near full bus capacity, whereas regularly scheduled operations are typically operated at substantially less than full capacity.

The passenger mile cost differential (the second factor in the base) between intercity automobile traffic and intercity bus traffic is the difference between two fractions. The numerator of the first fraction is the price per gallon of gasoline during the calendar year ending within or with the taxable year of the taxpayer, and the denominator is the average intercity passenger miles per gallon of an automobile for the most recently ended calendar year for which this information is available at the end of the taxable year. The numerator of the second fraction is the average cost of diesel fuel (the primary fuel used by intercity buses) for the calendar year ending within or with the taxpayer's taxable year, and the denominator is the company's passenger miles per gallon for the taxable year.

The fuel efficiency factor (the third factor in the base) is a constant which is the same for the entire industry. The constant (3.8) is the industry's intercity bus passenger miles per gallon for 1976 (125) divided by the average intercity automobile passenger miles per gallon (33).

Thus, the formula for computation of the credit is as follows:

$$\text{Credit} = \text{Intercity bus passenger miles} \times \left[\frac{\text{Cost of 1 gal. gasoline}}{\text{Auto passenger miles per gallon}} - \frac{\text{Cost of 1 gal. diesel fuel}}{\text{Bus passenger miles per gallon}}\right] \times 3.8 \times 20\%$$

Limitation based on operating expenses

Although the credit is refundable, it may not exceed an amount equal to the excess of:

(1) 17.65 percent of the taxpayer's total bus operating expenses (including those relating to regular route, charter and package express operations) over

(2) 50 percent of the taxpayer's net operating income (if any) from these bus operations, as reported to the ICC or a State regulatory agency (or agencies), if the taxpayer is not subject to ICC regulation.

Anti-flowthrough provision

The credit will not be allowed to a taxpayer if any portion of it is taken into account for ratemaking purposes by any Federal or State regulatory agency. The purpose of this provision is to provide additional funds to the intercity bus companies, and the committee has specified that these funds are to be used for specific purposes (one-half for fare reductions and one-half for certain types of investments). Consequently, taking this credit into account for rate making purposes, and thus flowing it through to customers other than in the manner prescribed in this provision, would defeat the basic purposes of the provision.

Recapture provisions

Requirement of use of 50 percent of credit for fare reductions.—The credit will be recaptured to the extent that 50 percent of the credit for a taxable year is not used for fare reduction during the taxable year or the following taxable year.

For purposes of this recapture provision, "fare reductions" are to be computed by multiplying the number of passengers who, during

the credit year, travelled on each route at a reduced fare by the amount that the fare for such route has been reduced. The base from which fares are to be computed for the purpose of determining whether a fare reduction has been made is the lowest fare actually being charged on a given route on August 1, 1977, not the highest fare for which prior approval had been given by the ICC (or, if no ICC approval is required, by a State regulatory body). The purpose for use of actual fares as a base is to give credit only for actual fare reductions, rather than credit for all amounts below a maximum approved rate.

If a fare reduction is offset in part or whole by a subsequent increase in fares, which was approved by the ICC (or, if no ICC approval is required, by a State regulatory body), the "fare reduction" per passenger would be the difference between (1) the base rate (in effect on August 1, 1977) plus the amount of the approved increase and (2) the fare actually charged.

In determining whether the recapture provision with respect to fare reductions has been satisfied, the taxpayer may use the fare reductions for the taxable year the credit is claimed (provided they have not been used for satisfaction of a prior year's credit) plus the fare reductions for the subsequent year. Thus, for example, if in 1978 a taxpayer is entitled to, and claims on his return a credit of $10 million, there would be a requirement that fare reductions of $5 million would have to be made. With respect to this requirement, the taxpayer would compute on his 1979 return the amount of fare reductions for 1978 (for example, $3 million) and then would look to 1979 fare reductions. If the 1979 fare reductions totalled only $1 million, there would be $1 million of the credit which would be recaptured ($5 million minus $3 million plus $1 million). This recapture of the credit would be reflected on the taxpayer's 1979 return. With respect to the taxpayer's credit for 1979 attributable to fare reductions, the taxpayer on his 1980 tax return would refer to its 1980 fare reductions to determine whether a portion of the credit was recapturable, since all of the 1979 fare reductions had been utilized in satisfying a portion of the 1978 credit.

Although there is a requirement that the amount of the credit be used for fare reductions on regularly scheduled routes, there is no restriction on what types of individuals must be granted the fare reduction. It is anticipated, however, that the bus companies will use these fare reductions for long-haul trips, off-peak hours, or other routes where there is excess capacity and where they feel that reduced fares are likely to stimulate the most increased ridership.

Investment in terminals and equipment.—A second recapture rule provides that, in general, recapture of the credit will occur to the extent that the taxpayer's qualifying investments in terminals and equipment in the taxable year and the three succeeding taxable years is less than 50 percent of the credit for the taxable year.[5] Qualifying investments in terminals and equipment are (1) 100 percent of amounts expended for new terminals or improvements of terminals and (2) 40 percent

[5] Of course, the fact that an investment in terminals or equipment is used to satisfy the investment requirements of this provision will not reduce the basis of the terminal or equipment for purposes of depreciation or the investment credit and will not limit the availability of the investment credit.

of the amounts expended for equipment. However, to the extent that the investment in equipment or a terminal is subsidized by a Federal, State, or local government (or an agency of such a government), it will not qualify.

Qualifying investments in terminals or equipment must be for property the original use of which begins with the taxpayer or for the rehabilitation of existing property. For purposes of this provision, expenditures for the rehabilitation of existing property are limited to amounts chargeable to a capital account and incurred for property or additions or improvements to property (or related facilities) with a useful life of 5 years or more, in connection with the rehabilitation of an existing building for use as a terminal or of existing equipment. An investment in land for terminals may be a qualifying investment in the year the land is actually used for a terminal.

The amounts of qualifying investments normally would be counted toward satisfying the investment requirement attributable to the credit for the taxable year. However, if the taxpayer elects, the amounts of qualifying investments in a taxable year shall be applied first to the credit allowed with respect to the third preceding taxable year, then to the credit allowed with respect to the second preceding taxable year, and so forth.

Recapture for dispositions of qualifying investments.—In general, if a taxpayer disposes of property within 60 months after the date on which the property or improvement is placed in service and all or a portion of the adjusted basis of the property or improvement was taken into account as a qualifying investment, the tax liability of the taxpayer for the taxable year in which the disposition occurs will be increased by an amount equal to the amount allowed as a qualifying investment with respect to the property. However, if the property (or improvement) is substantially or completely destroyed as a result of a casualty (described in section 165), or is compulsory or involuntarily converted (within the meaning of section 1033), no recapture of the qualifying investment will occur.

Advance refunds of one-half of credit

The committee wishes to encourage the bus companies to begin fare reductions as soon as possible. Since revenues would be reduced substantially during the year in which a fare reduction is implemented, the companies would experience cash flow problems if they had to wait until the end of the year to obtain the refundable credit. Even if the credit were reflected in their quarterly deposit of estimated taxes, they would be faced with a one quarter lag. Consequently, the committee bill provides that the bus company may obtain quarterly advances of the portion of its credit which is to be earmarked for fare reductions. Under this provision, a qualifying bus company may obtain quarterly advances equal to one-eighth of the credit which it estimates would be payable with respect to the taxable year.

To obtain this credit, the company must file, no earlier than 15 days before the start of each quarter of its taxable year and no later than 15 days after the start of each quarter, an application for credit. On this claim, the company will show, on the basis of the best estimates available as of the filing date, computations establishing the estimated

credit to which the company believes it will be entitled as of the end of the year. The Internal Revenue Service will be allowed 30 days from the date it receives the claim to make payment of one-eighth of the estimated total credit. If payment is not made within this time, interest will accrue on the unpaid balance at the general rate of interest for the underpayment of tax (see sec. 6621). No advance refunds will be issued pursuant to this provision unless the taxpayer states, under penalty of perjury, that a fare reduction program has begun during or prior to the quarter or will begin during such quarter.

If the amounts paid pursuant to this advance refund procedure with respect to a taxable year exceed 62.5 percent of the credit to which the company is entitled, any excess over such amount will be considered an underpayment of estimated tax and penalties will be applicable to this amount in the same manner as with respect to estimated tax.

As is the case with other credits, the portion of the credit which is not advanced to the company (generally, that part of the credit for the purchase of buses and construction of terminals) shall be reflected in the company's quarterly deposit of estimated taxes. However, since the portion of the credit which is refunded in advance is not to be counted as a credit reducing the tax liability for purposes of the corporation's estimated tax, a technical amendment is made to section 6655(e)(1)(B) to provide that the portion of such credit paid in advance is not treated as a reduction of tax for purposes of estimated taxes.

On the taxpayer's return for the taxable year, the entire amount of the credit is shown as such and any advance refund is treated as either reducing the amount of a refund to which the taxpayer is entitled on the return or increasing the balance of tax due, as the case may be.

Limitation on losses attributable to bus operations

If a taxpayer who is eligible to claim the intercity bus credit sustains a loss attributable to his bus operations for the taxable year, the loss is to be reduced by an amount equal to the lesser of the loss or the amount of the intercity bus credit allowed to the taxpayer. In determining the amount (if any) of the loss which the taxpayer has sustained, amounts of income and deduction shall be computed in the same manner as they are for Federal income tax purposes (rather than for purposes of reports to regulatory agencies). The purpose of this limitation is to prevent the offset of other income with a loss to the extent the loss has been reimbursed by the intercity bus credit.

Effective date

These provisions are to be effective for taxable years beginning after December 31, 1977, and before January 1, 1983.

Revenue effect

It is estimated this provision will reduce budget receipts by $120 million in fiscal year 1978, by $200 million per year in fiscal years 1979 through 1982, and by $80 million in fiscal year 1983.

Energy savings estimate

Since the bus industry over the past 10 years has been experiencing a decline in passenger miles traveled, a continuation of this trend could result in a substantial waste of energy by passenger diversion to less

energy-efficient automobiles. However, due to the structure of the credit, an accurate energy savings estimate cannot be made. One-half of the credit is intended for use in upgrading terminals and equipment and an estimate of the response to these improvements in the form of increased ridership cannot be made because noneconomic factors are involved. The committee believes that the current location and condition of many bus terminals has contributed to the decline in ridership the industry is experiencing. A purpose of the credit is to stop the present trend of disinvestment in bus equipment and facilities and the consequent curtailment of bus service. By renovating old terminals, building new terminals and relocating terminals presently situated in undesirable locations, bus traffic could become more attractive and the current decline in ridership could be reversed. If this reversal of the trend could present a shift to intercity automobile travel, additional energy savings would occur. The other one-half of the credit would significantly lower fares on routes now running at less than peak capacity and would result in a further increase in ridership with little increase in overall fuel consumption by buses. If the current decline in bus ridership could be avoided and a three percent shift from bus to automobile travel could be prevented, it is estimated that a savings of 25,000 barrels per day would result.

C. CHANGES IN BUSINESS INVESTMENT CREDIT TO ENCOURAGE CONSERVATION OF, OR CONVERSION FROM, OIL AND GAS OR TO ENCOURAGE NEW ENERGY TECHNOLOGY

(Secs. 1031, 1032, and 1033 of the bill and new secs. 44F and 46A of the Code

Present law

Investment tax credit

Under present law, an investment tax credit of 10 percent (which reverts to 7 percent after 1980) is allowed generally for tangible personal property which is placed in service in a trade or business. (The credit can be as high as 11½ percent for corporations with qualified employee stock ownership plans.) However, structural components of buildings, including insulation, storm windows and doors, solar energy equipment, etc., generally do not qualify for the credit. Otherwise eligible property placed in service in hotels and other businesses which cater to transients is eligible for the investment credit, but property placed in service in hotels and apartments which have predominantly permanent residents does not qualify for the credit.

The investment credit is also allowed for tangible property (other than buildings or their structural components) which is used in manufacturing, production, extraction, or as an integral part of furnishing transportation, communications, or electrical, gas, or other utility services, even though such tangible property may otherwise be considered real (and not personal) property under local law.

The extent to which the investment credit is available depends upon the estimated useful life used to depreciate or amortize the property for tax purposes. The determination of the useful life is made at the time the property is placed in service. No investment credit is allowed if the property has an estimated useful life of less than 3 years. Where the useful life is greater than 3 years but less than 5 years, the investment credit is allowed on one-third of the taxpayer's cost for the property; if the useful life of the property is greater than 5 years but less than 7 years, the credit is allowed on two-thirds of the cost, and the credit is allowed on the entire cost where the property has a useful life of 7 years or more. If the property on which the investment credit was claimed is later sold or otherwise ceases to be qualified property for the taxpayer before the end of its estimated useful life, the credit may be partially or entirely recaptured to reflect the taxpayer's reduced holding period.

Generally, the amount of the investment credit a taxpayer may apply against his income tax liability in any one year cannot exceed the first $25,000 of tax liability plus 50 percent of the tax liability in excess of $25,000. Special limitations have been provided for public

utility property, under which the 50 percent limit was increased to 100 percent for 1975 and 1976, and is 90 percent for 1977, after which it declines by 10 percentage points in each succeeding year until it returns to the generally applicable 50-percent limit in 1981. Similar increases in the tax liability limitation are available (under the Tax Reform Act of 1976) to railroads and airlines, which are allowed to apply their investment credits against 100 percent of their tax liability for 1977 and 1978, and the limitation is reduced by 10 percentage points in each subsequent year until it returns to 50 percent in 1983.

Investment tax credits are not refundable. However, credits which are not applied against tax liability in the year they are earned may be carried back for 3 taxable years and carried forward for 7 years. In applying credits against tax liability for a particular tax year, the first-in first-out method is generally required, under which the credits earned in prior tax years are applied first, then the credits earned in the current year or later years are used.

Industrial development bonds

Under present law, the interest income derived from obligations of a State or local government generally is exempt from Federal income tax. This rule does not extend to industrial development bonds whose proceeds are used by a taxpaying enterprise in its trade or business, except for those situations where the proceeds of the bonds are used by a taxpaying enterprise for specified exempt purposes. Exceptions have been provided where the proceeds are used to acquire or construct solid waste disposal facilities, and air or water pollution control facilities.

Reasons for change

The committee believes that the urgency of the energy problem requires a powerful measure designed specifically to reduce the consumption of oil and natural gas by industrial, utility, and institutional users. The committee believes that it has made available tax incentives to stimulate a rapid transition from heavy reliance on oil and gas. The alternative energy property tax credit would pay for 40 percent of the cost of equipment which uses sources of energy other than oil and gas and of associated pollution control, handling and preparation equipment. The credit would be available to businesses, state and local governments, and certain tax-exempt organizations. In conjunction with the existing investment credit and income tax depreciation deductions for the full cost of the property, the effective price of this equipment to businesses is lowered to about one-third of its nominal purchase price. The refundable feature of the credit will allow all businesses, irrespective of their income tax liability, to receive the full incentive effect. Because the committee believes that utilities' new facilities will not use oil or gas even in the absence of a tax credit, utilities would receive the credit only to the extent that they phase down or replace an existing oil- or gas-fired boiler.

The property eligible for the credit includes equipment which uses the following sources of energy: coal, biomass, hydroelectric, nuclear, geothermal, solar, wind, ocean thermal and tidal. By focusing this large incentive on users of energy, the committee believes that it can achieve a substantial reduction in business use of oil and natural gas and thus, in U.S. oil imports.

The committee also believes that it is essential to reduce the use of oil and gas in existing facilities and to provide an incentive to use energy-efficient processes. Thus it has provided an extra 10-percent refundable credit, which would also be available to certain tax-exempt organizations and governmental units, for certain items which result in the conservation of energy. In addition, a nonrefundable 10 percent credit is allowed for equipment used in cogeneration, solid waste recycling, the recovery of oil and gas from oil shale and geopressurized water deposits, and also for commuter vans and energy-saving equipment added to existing trucks.

1. Additional Credit for Investment in Certain Energy-Related Depreciable Property (secs. 1031 and 1033 of the bill and new sec. 44F of the Code)

Explanation of provisions

A. GENERAL PROVISION

This provision provides a 40-percent credit for certain conversion property, called alternative energy property, and a 10 percent credit is provided for certain conservation property, called specially defined energy property, during the period after April 19, 1977, and before January 1, 1986, for property acquired and placed in service during this period. If eligible property is constructed by the taxpayer, the credit will be available for construction completed after April 19, 1977, and only to the extent of costs incurred before January 1, 1986. If the taxpayer makes progress expenditures and elects to claim this credit for the progress expenditures, the credit is available only to the extent of progress expenditures made during this period. Property purchased by the taxpayer must be both acquired and placed in service during this period. The original use of the property must commence with the taxpayer, and the property must be an integral part of, or used in connection with, a building or other structure located in the United States.

The credit is refundable, so that the amount which the taxpayer is allowed is not limited by tax liability. Organizations described in Code section 501(c)(3) and electric utilities described in section 501(c)(12), which are exempt from Federal income tax, as well as State and local governments, are eligible to receive the credit. Any excess of the credit above tax liability may be claimed as as a refund.

B. RULES OF APPLICATION

For this credit the committee's bill provides rules generally similar to the regular investment credit provisions. (Eligibility for the special energy credit under this provision, however, does not affect the eligibility of the property for the regular investment credit under present law.) As a result, the rules for applying the regular investment credit, such as, the rules referring to leased property, will also generally apply to the alternative energy property investment credit. In the following areas, however, there are special rules for this additional credit:

Special rules for utilities.—In the case of a regulated public utility (as defined in section 7701(a)(33)) whose principal activity is the sale of electricity, a credit shall be allowed for a boiler only to the extent that a boiler, which was in existence on April 20, 1977, and used oil or natural gas as its primary fuel on that date, is phased down. A boiler shall be treated as phased down only where the boiler was used more than 2,000 hours in 1976 and will not be used more than 2,000 hours in any year following the year in which the new boiler is placed in service. The Secretary shall issue regulations necessary to prevent the avoidance of this restriction, for example, by phasing up another old boiler at the same time.

The determination of the extent to which an oil or gas boiler is phased down shall be on the basis of its capacity in terms of megawatts. For example, if a new boiler with a capacity of 80 megawatts is placed in service and a boiler with a capacity of 20 megawatts is phased down, 25 percent of the investment with regard to the new boiler shall be taken into account in computing the credit. Where an oil or gas boiler is converted into a boiler using an alternate substance, the phase down rule shall be considered satisfied, but the modified boiler shall not be treated as an eligible old boiler in the event it is subsequently phased down.

The bill allows utilities to treat qualified progress expenditures as qualifying investment for any calendar year where the utility certifies to the Secretary or his delegate that the eventual phase down of the old boiler will occur in the year following the year in which the new boiler is placed in service, provided the new boiler is to be placed in service within 3 years after the end of the first year for which the certification is effective. In addition, the taxpayer must agree to a reasonable extension of the period of limitations for assessing any additional tax which may be due in the event the phase-down does not in fact occur in accordance with the certification. In addition, where this provision is used, the credit for the year the equipment is placed in service shall be adjusted in accordance with the usual rules under section 46(c)(4).

Where the phased-down boiler was used more than 2,000 hours, the new boiler is to be treated as having been disposed of in the year in which that excess use occurs and the normal disposition rules applicable to this credit will apply. Where a utility runs a boiler solely to keep it in operating condition, it is not to be considered as having used the boiler for purposes of applying this provision.

The recapture provision for utilities will not apply in circumstances where the utility is prevented from using the replacement boiler by an act of God, a strike which prevents delivery of coal to the replacement facility, or damage by storm, fire or flood, etc., to the replacement facility. Therefore, the Secretary will prescribe regulations suspending applicability of the recapture provision during periods when the utility is unable to comply with the phase-down requirement because of such circumstances.

In addition, where a facility was in existence or under construction on April 20, 1977 and on that date (1) it was contemplated that the facility would include one or more boilers which would use oil or gas as its primary fuel or (2) the facility did include one or more such

boilers, and after April 20, 1977, the construction of such boiler or boilers is modified to use a primary fuel other than oil or gas, any boiler so modified will be eligible to be treated as alternative energy property.

These rules also apply in the case of any boiler leased to a regulated public utility, whether or not the lessor has elected to allow the utility to receive the credit.

Lodging limitation.—The lodging limitation of the regular investment credit (sec. 48(a)(3)) does not apply to additional credits for alternative energy property and specially defined energy property. As a result, the credit is available both for qualified property installed in connection with a lodging facility which provides accommodations to transients (for which the regular investment credit may be claimed for qualifying property under present law) and for property installed in connection with facilities (such as apartment houses) which predominantly provide long-term accommodations (for which the regular investment credit is generally not available under present law).

Structural component limitation.—The credit is to be available without regard to whether the equipment is a structural component of a building. Thus, for example, solar, geothermal and wind energy equipment could qualify for the credit even if integrally attached to a structure. Buildings, however, would be eligible for this credit only to the same extent they are eligible for regular investment credit.

Recapture.—If any qualifying property ceases to be used as alternative energy property and specially defined energy property before the end of one-half its useful life (as determined for purposes of depreciation under section 167 (or which would be so determined in the case of an exempt organization or governmental unit if it were taxable)) then it will be considered to be disposed of, and the entire credit will be recaptured.

Industrial development bonds.—Except for bioconversion property, equipment which is partially or entirely financed by industrial development bonds, whose interest is exempt from Federal income tax, receives a 20-percent, rather than 40-percent, credit. Bioconversion property, which would receive the 40-percent credit even if such bonds were a financing vehicle, is defined in Code section 103 (b)(4)(I) (added by section 1041 of this bill) as equipment for the conversion of agricultural and municipal wastes and other organic matter into either energy or into synethic gaseous, liquid or solid fuels.

Federal grants.—No credit is available for any equipment to the extent that such equipment is financed by any grant of Federal funds.

C. ALTERNATIVE ENERGY PROPERTY

Generally, the 40 percent refundable credit is allowed for investments in new property which either directly (for example, coal-fired boilers) or indirectly (for example, certain pollution control equipment) relate to the installation by industrial firms and electric utilities of equipment or facilities that will make possible shifts from oil and natural gas to other fuels.

Alternative energy property is defined as specific types of equipment whose fuel or feedstock is an alternate substance, that is, a substance other than crude oil, shale oil, refined petroleum products, natural gas, geopressurized methane, and natural gas liquids. Examples include coal and agricultural or municipal wastes. Equipment will not qualify for the credit unless it meets quality and performance standards which are in effect at the time the equipment is placed in service. Such standards would be set by the Secretary, in consultation with the Secretary of Energy and other appropriate agencies. Alternative energy property specifically includes the following types of property:

(1) *Boilers.*—A boiler which uses an alternate substance as its primary fuel (i.e., more than 50 percent) is the first type of alternative energy property. Equipment used to modify an existing boiler so that the primary fuel would be an alternate substance would also qualify as alternative energy property.

(2) *Burners.*—A burner for a combustor (other than a boiler) can also be treated as alternative energy property, if the primary fuel for the burner will be an alternate substance or a combination of such substances. The eligible investment includes equipment which is located on-site at the burner and which is necessary to bring the alternate substance to the burner. Among the burners within this category are burners for a lime kiln or cement kiln which use an alternate substance as a fuel.

(3) *Nuclear and hydroelectric equipment.*—Certain equipment used to produce power from nuclear and hydroelectric sources is eligible for the credit. In the case of nuclear power, the fuel, turbines and equipment beyond the turbine stage is not eligible; thus the eligible equipment is limited to the nuclear stream supply system. In the case of hydroelectric power, penstocks, turbines, generators, and other equipment up to, but not including, the electrical transmission stage are included in the category of eligible equipment. Dams are not to be considered eligible equipment.

(4) *Production of synthetic fuel.*—Equipment used to convert an alternate substance into a synthetic solid, liquid or gaseous fuel is included in the definition of alternative energy property. This includes coal gasification and liquefaction and the production of synthetic fuel from biomass. Only the equipment necessary to manufacture a marketable fuel would be eligible for the credit. Not included, however, is equipment which simply mixes an alternative substance with a liquid, for example, equipment which mixes coal and water to produce a slurry. Equipment used to produce coke or coke gas is also excluded.

(5) *Mixtures of oil or natural gas and an alternate substance.*—Alternative energy property includes equipment designed to modify equipment placed in service on or before April 20, 1977, which burns oil or natural gas, or uses oil or natural gas as a feedstock, so that this equipment uses coal, waste (such as biomass) or other alternative substances as a fuel or feedstock. This credit will be available where the use of an alternate fuel or feedstock is at least 25 percent of the total fuel or feedstock as a result of the modification. Quality investment in this category would include the costs of replacing or modifying existing combustors and burners to enable the facility to use this fuel mixture.

(6) *Coal used as feedstock.*—Alternative energy property includes equipment which uses coal or lignite as a feedstock to produce chemicals. Only the equipment necessary to manufacture a marketable product would be eligible for the credit. Equipment used to produce coke or coke gas is excluded.

(7) *Pollution control equipment.*—The alternative energy property credit is also available for pollution control equipment, such as scrubbers and electrostatic precipitators, which Federal, State or local governmental regulations require to be installed on or in connection with a boiler, a burner, equipment used in the production of synthetic fuel, equipment which uses coal as a feedstock, or equipment which uses a mixture of an alternate substance and gas or oil, which itself qualifies as alternative energy property. The credit, however, does not apply to any equipment which is installed on or in connection with property which, as of April 20, 1977, was using coal, and was required to be installed by Federal, State, or local governmental regulations in effect on April 20, 1977.

(8) *Handling and preparation equipment.*—Equipment used for the unloading, transfer, storage, reclaiming from storage, and preparation (including washing, crushing, drying, and weighing) at the point of use of a fuel or feedstock other than oil, gas, and their products qualifies as alternative energy property, if the fuel is to be used in certain specific types of alternative energy property, i.e., a boiler, a burner. equipment used in the production of energy from nuclear sources. equipment used in the production of synthetic fuel, equipment which uses coal as a feedstock, equipment which uses a mixture of an alternate substance and gas or oil, or pollution control equipment which itself qualifies for the credit. Eligible preparation equipment also includes equipment for shredding, chopping, pulverizing, or screening agricultural or forestry byproducts at the point of use in eligible equipment. No equipment for the transportation of fuel to the site of its use is covered by this provision. Thus, for example, coal slurry pipelines and railroad cars would not qualify for the additional tax credit.

(9) *Ocean and tidal equipment.*—Alternative energy property includes equipment necessary to convert ocean thermal energy and tidal power into useful forms of energy.

(10) *Solar and wind equipment.*—Equipment which uses solar or wind energy to provide heat, cooling, electricity, or hot water in connection with a building or structure is eligible for the credit.

Generally, a solar energy equipment system involves the transformation of sunlight into heat or electricity through the use of such devices as solar cells or other collectors, storage systems for electricity and for hot air or hot water (including rock beds), heat exchangers to utilize captured and stored energy, and related equipment, such as fans and thermostats. The credit for wind equipment similarly applies to the windmill or other devices to harness outdoor moving air to provide electricity and other forms of energy and includes storage and transfer systems to distribute this energy.

(11) *Geothermal equipment.*—Equipment used to produce, distribute, or use energy derived from a geothermal deposit would be considered alternative energy property. When geothermal energy is used to generate electricity, eligible equipment does not include any equip-

ment used to transmit electricity or any equipment beyond the electrical transmission stage, but turbines and generators would be included. A geothermal deposit is a reservoir consisting of natural heat which is stored in rocks or in an aqueous liquid or vapor, whether or not under pressure.

(12) *Plans and designs.*—Alternative energy property includes the costs of plans and designs for any equipment in the above categories.

D. SPECIALLY DEFINED ENERGY PROPERTY

This category of property qualifies for the refundable credit equal to 10 percent of the taxpayer's investment in new property. Organizations which are exempt from Federal income tax under Code section 501(c)(3) and electric utilities exempt under 501(c)(12), as well as State and local governments, are eligible to claim and receive payments equal to 10 percent of their basis in qualifying property.

Qualifying property includes specific items of equipment (described below) added to an existing operation in an existing agricultural, industrial, utility, or commercial facility. An existing building or facility is one for which 50 percent of the basis is attributable to construction, reconstruction or erection before April 20, 1977, or, in the case or a nuclear power plan, a construction permit was issued and construction began before April 20, 1977. An existing operation is one carried on in an existing facility as of April 20, 1977.

Equipment will not qualify for the credit unless it meets quality and performance standards which are in effect at the time the equipment is placed in service. Such standards would be set by the Secretary, in consultation with the Secretary of Energy and other appropriate agencies.

The following specified items of equipment are included in specially defined energy property:

(*1*) *recuperators*, which are configurations of equipment which consist in part of fixed heat transfer surfaces between two gas flows and which are used to recover energy, usually in the form of waste heat, from combustion exhaust gases in order to preheat incoming combustion air;

(*2*) *heat wheels*, which are items of equipment consisting, in part, of regenerators which rotate through two gas flows and which are used to recover energy, usually in the form of waste heat, from exhaust gases to preheat incoming gases;

(*3*) *regenerators*, which are devices used to recover energy by efficiently storing heat while exposed to high temperature gases and then releasing heat when exposed to low temperature gases;

(*4*) *heat exchangers*, which are equipment consisting in part, of fixed heat transfer surfaces separating two fluids which are used to recover energy, usually in the form of waste heat, from high temperature fluids of industrial proceses for transfer to low temperature fluids;

(*5*) *waste heat boilers*, which are boilers that use waste heat, usually in the form of combustion exhaust gases, as a primary energy source;

(*6*) *heat pipes*, which are devices that consist, in part, of sealed heat transfer chambers containing a working fluid which is alter-

natively vaporized and condensed as it travels from one end of the chamber to the other and are used to recover energy, usually in the form of waste heat, from high temperature fluids to heat low temperature fluids;

(*7*) *automatic energy control systems*, which are equipment used to control energy usage for environmental space conditioning or for manufacturing processes in ways which automatically minimize such energy usage;

(*8*) *turbulators*, which are small baffles placed in the upper passes of the firetubes of boilers to increase the rate of transfer of heat from combustion gases to the firetube surface;

(*9*) *preheaters*, which are equipment that consists, in part, of a fixed heat transfer surface separating two fluids and are used to recover energy, usually in the form of waste heat from either combustion exhaust gases or steam, to preheat incoming combustion air or boiler feedwater;

(*10*) *combustible gas recovery systems*, which are equipment used to recover unburned fuel from combustion exhaust gases; and

(*11*) *economizers*, which are configurations of equipment used to recover energy from combustion exhaust gases to preheat boiler feedwater; and

(*12*) *Industrial heat pumps*, which are devices, utilized in industrial or manufacturing processes, that use the compression and expansion of a gas in a system to extract heat from a gas or liquid and transfer it to another gas or liquid at a higher temperature. This does not include heat pumps used for the purposes of heating or cooling building space.

In addition to these types of property, the Secretary is authorized to specify other similar items of energy conservation equipment eligible for this credit, including modifications which are made to existing industrial processes (such as modifications to smelters or alumina electrolytic cells) the principal purpose of which is the reduction in the amount of energy consumed or heat wasted.

E. EXTENSION OF CREDIT TO CERTAIN EXEMPT ORGANIZATIONS AND TO STATE AND LOCAL GOVERNMENTS

The alternative energy property and specially defined energy property credits are available as payments to certain tax-exempt organizations and to governments of States and of any of their political subdivisions. The eligible tax-exempt organizations include those described in section 501(c)(3) of the Code. These include nonprofit, religious, charitable, scientific, and educational institutions. In addition, electric utilities described in section 501(c)(12) are also eligible for the credit. The amount of the payment shall be determined as if the organization were engaged in a trade or business and were subject to the income tax.

Effective date

The alternative energy property credit will be effective for qualifying property placed in service after April 19, 1977, to the extent of expenditures incurred after that date and before January 1, 1986.

Revenue effect

The decline in budget revenues from the additional credit for alternative energy property is estimated at $731 million in fiscal year 1978, $1.046 billion in 1979, $1.525 billion in 1980, $2.371 billion in 1981. $3.596 billion in 1982 and $5.230 billion in 1985.[1]

For specially defined energy property, the estimated revenue loss in fiscal years 1978 through 1982, respectively, is $303 million, $295 million, $312 million, $328 million, and $347 million. The revenue loss estimated in fiscal year 1985 is $407 million.

The revenue loss attributed to the additional credits for industrial heat pumps is estimated at $40 million in fiscal year 1978, $39 million in 1979, $45 million in 1980, $52 million in 1981, $60 million in 1982 and $91 million in 1985.

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[1] The Treasury Department agrees with these estimates under the assumption of no extraordinary increase in the prices of qualifying property. While difficult to forecast, investment tax credits of this magnitude could allow equipment manufacturers to increase prices and therefore increase the cost of this proposal.

2. Business Energy Property Credit (sec. 1032(a) of the bill and new sec. 46A of the Code)

Explanation of provisions

In order to increase energy conservation by industrial and commercial sectors of the economy, the bill provides a special investment tax credit that is in addition to the regular investment tax credit, for a limited period of time.

The business energy credit is available at a rate of 10 percent for certain types of property, called energy property, during the period after April 19, 1977, and before January 1, 1986. If eligible property is constructed by the taxpayer, the business energy credit will be available only for construction completed after April 19, 1977, and only to the extent of costs incurred during this period. Similarly, if the taxpayer makes progress expenditures and elects to claim this credit for the progress expenditures, the credit is available only to the extent of progress expenditures made during this period. Property purchased by the taxpayer must be both acquired and placed in service during this period.

Rules of general application

The committee's bill adds this business energy credit to the present law investment tax credit provisions. (Eligibility for the special energy credit under this provision, however, does not affect the eligibility of the property for the regular investment credit under present law.) The rules for applying the regular investment credit will also generally apply to the business energy investment credit. For example, business energy credits will be absorbed using the first in-first out (FIFO) rules which apply to the regular investment credit. Business energy credits may also be carried back for three years and carried forward for seven years, as is the case with the regular investment credit.

Several changes to the regular investment credit rules are made, however, for purposes of applying the business energy investment credit. First, the structural component limitation found in the regular investment credit provisions is not applicable in the case of energy property. This will enable such property to qualify for the special additional credit even though this property would otherwise be treated as a structural component of a building and ineligible for the regular investment credit. Buildings qualify only to the same extent as they do under the regular investment credit.

A second change to the generally applicable investment tax credit rules involves the elimination of the lodging limitation (sec. 48(a)(3)) for purposes of the business energy credit. As a result, the business energy credit is available both for energy property installed in connection with a lodging facility which provides accommodations to transients (for which the regular investment credit may be claimed

(80)

for qualifying property under present law) and for energy property installed in connection with facilities (such as apartment houses) which predominantly provide long-term accommodations (for which the regular investment credit is generally not available under present law).

The entire basis of eligible property will qualify for the business energy credit, rather than the rules under present investment credit provisions which allow only part of the taxpayer's basis to be considered qualifying property where the useful life of the property is between 3 and 6 years. If any qualifying property is disposed of by the taxpayer or otherwise ceases to be used as energy property before the end of one-half of its useful life (as determined for purposes of depreciation under section 167) the entire credit will be recaptured.

A special rule is also provided for energy property that is partially or entirely financed by industrial development bonds, whose interest is exempt from Federal income tax under present law. In this situation, the business energy credit will be 5 percent, instead of the 10 percent rate which is generally available.

For the purposes of the business energy credits, the term industrial includes agricultural to reflect the committee's intent that energy property used in connection with an agricultural operation or process also will qualify for the business energy property credit.

Energy property defined

In order to qualify as business energy property eligible for this special investment credit, the property must be either cogeneration equipment, recycling equipment, shale oil equipment, geopressurized methane gas equipment, and certain transportation equipment. These types of equipment are explained in detail below.

Except in the case of transportation equipment, to qualify as energy property, the property must be an integral part of, or used in connection with, a building or other structure located in the United States. Where the taxpayer is constructing the energy property, construction, reconstruction or erection must be completed after April 19, 1977. Similarly, property purchased by the taxpayer must be acquired after April 19, 1977, and its original use must be by the taxpayer and must begin after April 19, 1977. (As already noted, the credit is available only to the extent of costs incurred after this date and before January 1, 1986.

For purposes of determining the eligibility of cogeneration equipment for the energy investment credit, it is generally required that this property or equipment be used in connection with an existing facility.

Except in the case of nuclear facilities, a building or facility will be considered to be in existence, if it has been substantially completed before April 20, 1977; that is, at least 50 percent of the taxpayer's basis in the building or facility must be attributable to construction, reconstruction, or erection which occurred before April 20, 1977. In the case of nuclear powerplants, the facility will be considered an existing building or facility if a construction permit was issued and construction had actually begun by April 19, 1977.

Except for shale oil and geopressurized methane gas equipment, this credit will be available only if the equipment meets performance and quality standards (relating to energy savings) prescribed by the Secretary (after consultation with the Secretary of Energy) which are in effect at the time the property is acquired or construction is begun.

Cogeneration equipment

To qualify as energy property, cogeneration equipment must be installed in connection with an existing facility and must result in an expansion in the facility's cogenerating capacity (including the start of cogenerating activity). Under the bill, cogeneration equipment means property which produces steam, heat, or some other form of useful energy (other than electricity), for industrial, agricultural, commercial, or space heating purposes, and which also produces electricity.

In this context, cogeneration equipment includes the addition of equipment to produce or distribute steam, heat, or other energy from an existing electric generating facility and also the electrical generating equipment which is added to an existing industrial or commercial faciilty which presently produces steam or another form of energy other than electricity.

It is intended that cogeneration equipment include steam and heat distribution systems that are added to an existing electric generating facility. In addition, it covers a supplemental boiler and an electrical generating turbine which are added to an existing industrial or commercial boiler or other heat-producing source, where these additions are necessary in order to enable the facility to cogenerate. Where it is necessary to replace an existing boiler in order to enable an existing industrial or commercial facility to cogenerate, this replacement boiler will be covered only to the extent of additional capacity which is related to a cogenerating function.

Where a taxpayer has operational cogenerating capacity in place on April 20, 1977, the credit will be available only to the extent that additional or replacement cogeneration equipment increases the cogenerating capacity of the facility. For this purpose, the eligible investment is determined from either the incremental capacity (in terms of megawatts) to produce electricity or the incremental capacity to produce steam (in terms of pounds per hour) or other forms of heat.

Recycling

The second category of property which qualifies for the energy investment credit is equipment used to recycle solid waste. The credit here is limited to solid waste recycling equipment because equipment to recover and recycle waste heat and gases is included under the specially defined energy property category.

Equipment covered under this category must be used exclusively for one of two purposes, either to sort, prepare, and recycle solid waste to recover usable raw materials or a fuel, or to burn solid waste as a fuel to create heat, steam or other useful forms of energy. This would include, for example, equipment which separates recyclable solid waste from a mixture of waste materials. Equipment which functions predominantly to prepare solid waste materials would also be covered.

For example, processes which apply a thermal, mechanical or chemical treatment to waste to condition or prime the materials so they will respond properly to the recycling process are included. Equipment in the actual recycling function to recover usable recyclable materials is also included up to the point where a material has been created which can be used to the same extent as materials from one or other virgin substances to begin fabrication of an end product. This point, for example, would be the ingot stage in metal recycling, fibers in textiles, and newsprint or paperboard in the paper industry. In the case of recycling equipment used to create a fuel or burn solid waste as a fuel, equipment will be covered to the point where the fuel, steam or heat has been created. As a result, combustors and boilers and similar equipment will be covered, but steam and heat distribution systems between a combustor or boiler and the point of use will not be qualifying property.

It is intended that eligible property in this category will include both equipment to recycle post-consumer waste materials (for example, municipal waste and cans and bottles that have been used by the consumer and recovered) and also industrial fabricating waste materials such as trimmings from a metal stamping process. It is also intended that on-site loading and transportation equipment which is integrally related to the actual recycling equipment should also be eligible for the credit. This would include, for example, equipment to load solid waste into a sorting or preparation machine and also a conveyor belt system which transports the solid waste materials from separation equipment to another machine in the recycling process. Transportation equipment, such as trucks, which transfer solid wastes between geographically separated sites, e.g., between collection points and recycling plants, will not be recycling equipment.

It should be emphasized that equipment will be eligible as recycling property only if it is used to process predominantly solid waste materials; the credit is not available where the equipment is used to process more than a nominal amount of virgin materials. For these purposes, a nominal amount is interpreted to mean not more than 10 percent virgin materials. If more than 10 percent virgin materials are used in a recycling facility during the course of any taxable year, the property will cease to be qualifying energy property. If this event occurs during the first one-half of the useful life of the equipment, this special tax credit will be recaptured in its entirety.

The credit for recycling equipment is available where used in connection with either a new or existing facility and industrial or commercial process. However, in order to prevent windfall benefits to taxpayers who are already engaged in recycling and who wish to replace their existing equipment in order to obtain this special investment credit, the committee intends that the credit be available only to the extent that the equipment results in an increase in the taxpayer's recycling capacity.

Oil shale equipment

This category of eligible property covers equipment which is used to extract oil from oil shale rock. In general such equipment would qualify if used after the mining stage for oil shale and up through the retorting process. Eligible equipment would include that involved

in either surface, or *in situ*, processing, including, in the case of *in situ* processing, equipment used to create the underground cavity. On-site water supply and treatment equipment and handling equipment for spent shale would similarly be eligible property.

Geopressurized methane gas equipment

This type of equipment will be used to treat a saline water and dissolved gas combination that is extracted from a geopressurized aquifer, in order to recover the dissolved methane gas. The eligible property is the equipment that is required to separate the methane gas from the saline water and to remove other impurities from the gas up to the point where the gas may be introduced into a pipeline system.

Transportation equipment

This category of equipment includes two types of property. First, this property includes commuter vans, defined in section 1027 of the bill, which are vehicles capable of carrying nine or more passengers, including the driver, which are owned by an employer and for substantially all the use of which is to transport employees to and from the employer's place of business. In addition, equipment which is added to existing trucks, which are engaged primarily in the commercial transportation of property, in order to conserve fuel is treated as energy property. Existing is defined, for this purpose, to mean placed in service before April 20, 1977. In addition, the Secretary is authorized to prescribe performance and quality standards for this qualifying property.

Effective date

These provisions are effective for qualifying property placed in service after April 19, 1977, to the extent of expenditures after that date.

Revenue effect

The revenue loss from the additional credit for cogeneration and recycling equipment is estimated at $60 million in fiscal year 1978, $72 million in 1979, $107 million in 1980, $149 million in 1981 and $197 million in 1982. In fiscal year 1985, the revenue loss is estimated at $379 million.

The estimated revenue loss from the extra credits for transportation equipment are $25 million, $20 million and $10 million in fiscal years 1978, 1979, and 1980, respectively.

3. Investment Tax Credit for Busines Insulation Property (sec. 1032(b) of the bill and new sec. 48(a)(10) of the Code)

Business insulation property which is a structural component of a building would be eligible for the regular investment tax credit, if placed in service during the period from April 20, 1977 through December 31, 1985. The provision applies to business insulation property that presently is not eligible for the investment tax credit. The criteria that are employed ordinarily to determine whether property is eligible for the credit would apply to this property; for example, the property must have a useful life of at least 3 years, and partial credits are allowed for useful lives of 3 through 6 years.

Business insulation property is defined as property which is specifically and primarily designed to reduce the heat loss of gain of an existing commercial or industrial building or facility in or on which the insulation property is installed. In addition, such insulation must be new property, have a useful life of at least three years, and meet performance and quality standards prescribed in regulations by the Secretary of the Treasury after consultation with the Secretary of Energy. This regulatory authority is to be applied prospectively only, and thus, these standards will not apply to insulation property purchased prior to the promulgation of such standards.

Qualifying property includes not only insulation, but a variety of other items designed to reduce heat loss or gain, including double glazing, heat-absorbing or heat-reflective glazed windows and doors and heat-absorbing and heat-reflective window and door materials, storm doors and windows, and weatherstripping.

To be qualified, business insulation property must be added on or in a building or facility which was in existence and placed in service before April 20, 1977. Expenditures for such insulation are to be treated as made when the installation of the insulation is completed. Accordingly, the time of payment of accrual of such expenditures is not to be taken into account in determining whether such expenditures qualify for the credit.

Effective date

This provision is effective for qualifying property placed in service after April 19, 1977, to the extent of expenditures after that date and before January 1, 1986.

Revenue effect

The decline in revenues as a result of the investment credit for business insulation property is estimated at $103 million in fiscal year 1978, $101 million in 1979, $107 million in 1980, $113 million in 1981, $119 million in 1982 and $141 million in 1985.

Energy savings estimate

It is estimated that as a result of the additional investment credits to encourage conservation of, or conversion from, oil and gas or to encourage new energy technology, oil imports will be reduced in 1985 by 1,508,000 barrels per day.

D. TAX INCENTIVES FOR ALTERNATIVE ENERGY SOURCES

1. Industrial Development Bonds for Coal Gasification and Liquefaction Facilities and for Bioconversion Facilities (sec. 1041 of the bill and sec. 103 of the Code)

Present law

Under present law, interest earned on obligations of a State or local government generally is exempt from Federal income tax. This rule does not extend to industrial development bonds, the proceeds of which are used by a taxpaying enterprise in its trade or business, except where the proceeds of the bonds are used for specified exempt purposes, and except for certain small issues.

Coal gasification and liquefaction facilities

Although the use of facilities for the local furnishing of gas is one specified exempt purpose for industrial development bonds (sec. 103 (b) (4) (E)), many bond issues for coal gasification facilities cannot qualify for the exemption under current Treasury Department regulations (§ 1.103–8(f) (2) (iii) (*d*)), which interpret the term "local furnishing" to mean, in general, furnishing gas to no more than two contiguous counties (or political equivalents). This bars exempt status for bonds issued for facilities serving a larger area.

In addition, the statute does not designate the provision of liquid fuel produced from coal liquefaction as an exempt purpose.

Bioconversion facilities

Present law (sec. 103(b) (4) (E)) also provides an exemption for interest earned on industrial development bonds whose proceeds are to be used to provide waste disposal facilities. However, Treasury regulations (§ 1.103–8(f) (2) (ii) (*c*)) provide that a waste disposal facility qualifies under this provision only if at least 65 percent of the total materials introduced into the facility's recycling process are valueless. (Certain bioconversion facilities also may not qualify as exempt purposes because of the two-contiguous-county regulation described above.) Generally, no exemption is provided under present law for interest income from industrial development bonds for bioconversion facilities for the conversion of organic matter into energy or into synthetic fuels.

Reasons for change

The statutory and regulatory limitations on the qualification of certain coal gasification and liquefaction facilities and certain bioconversion facilities as exempt activities under the tax provisions for industrial development bonds have hampered the development of these facilities. Because facilities for coal gasification and liquefaction and facilities for bioconversion may produce significant amounts of energy,

the Committee decided to amend the industrial development bond provisions to permit these facilities to qualify as exempt activities.

Explanation of provisions

Coal gasification and liquefaction facilities

The committee bill extends the exemption from taxation for interest earned on certain industrial development bonds to interest earned on bonds issued to provide facilities for the production of a synthetic gaseous or liquid fuel by coal gasification and liquefaction processes, respectively. Under the bill, the new exemption is not restricted to facilities for furnishing the products of coal gasification and liquefaction to two contiguous counties. This restriction, however, remains effective for natural gas facilities.

The facilities which may qualify for the exemption include:

(1) facilities which directly perform the coal gasification or liquefaction process;

(2) facilities for the on-site transportation, handling, storage, or treatment of coal and other raw materials, supplies, or materials in the process preparatory to the coal gasification or liquefaction process;

(3) facilities for the on-site economic recovery, recycling, handling, storage, treatment, or utilization of byproduct materials or energy generated by the coal gasification or liquefaction process;

(4) facilities for the on-site handling or transportation, or the increasing of the British thermal unit (Btu) content per unit of volume, of synthetic gaseous or liquid fuels produced by the coal gasification or liquefaction process; and

(5) other on-site facilities to the extent that such facilities are functionally related, and subordinate to, any of the above described facilities.

For purposes of this provision, the term "synthetic gaseous or liquid fuel" is defined to mean any gaseous or liquid product of a coal gasification or liquefaction process which can be used as a substitute for natural gas or oil regardless of its chemical composition or British thermal unit content.

Bioconversion facilities

The committee bill provides a new statutory exemption from Federal income taxation for interest earned on industrial development bonds which are issued to provide bioconversion facilities for the conversion of municipal and agricultural (including forestry) wastes and sion of municipal and agricultural (including forestry) wastes and other organic matter into energy or into synthetic gaseous, liquid, or solid fuels. Facilities which qualify under this provision are not subject to the rule (described above) that at least 65 percent of the materials introduced into the conversion processes must be worthless. For purposes of this provision, bioconversion facilities include machinery for handling, storing, processing (including equipment for sorting, shredding, and pulverizing wastes and agricultural byproducts), and treating the organic materials used in the particular bioconversion facility. In addition, because the new category of exempt bioconversion activity is not limited to the local furnishing of energy or fuels, the two-contiguous-county rule does not apply.

Effective date

These provisions apply with respect to obligations issued after December 31, 1977.

Revenue effect

These amendments are expected to reduce revenues by a negligible amount in fiscal 1978, by $3 million in fiscal 1979, and by $77 million in fiscal 1985.

2. Geothermal Tax Provisions (secs. 1042 and 1043 of the bill and secs. 57, 263, 465, 613, 614 and 1254 of the Code)

Present law

Percentage depletion

Under present law, it is unsettled whether the production of geothermal steam and associated geothermal resources qualifies for either a percentage depletion deduction or the intangible drilling cost deduction. In *Reich* v. *Commissioner*, 454 F. 2d 1157 (9th Cir. 1972), aff'g, 52 T.C. 700 (1969), the Ninth Circuit held that the production of geothermal steam entitled the taxpayers to both deductions to the extent that such deductions were available for gas wells.[1] Nevertheless, the Internal Revenue Service apparently is not following the *Reich* decision in cases arising outside of the Ninth Circuit.

Except in the case of certain small producers, the Tax Reduction Act of 1975 generally eliminated the depletion allowance for oil and gas. That Act, however, did not affect the issue of whether geothermal resources qualify for percentage depletion. As a result, the 22-percent depletion deduction allowable to gas wells immediately prior to the Tax Reduction Act of 1975 still is available for geothermal energy if courts decide, as did the *Reich* court, that certain geothermal wells are gas wells and that the other requirements for depletion are met (sec. 613A(b)(1)(C)).

Intangible drilling costs

Deduction.—Even if the *Reich* decision is not followed, under present law, expenditures incurred in connection with the exploratory phase of geothermal energy which result in dry holes are deductible at the time when the well (or leasehold) is abandoned. Moreover, to the extent that these costs result in new processes or technology, it is possible under present law that these costs would be considered research and experimental expenditures subject to the election to be deducted currently or to be amortized over a 60-month period. For example, in Revenue Ruling 74–67, 1974–1 C.B. 63, the Internal Revenue Service held that certain costs of developing a method for the hydraulic mining of hard minerals, including a portion of the cost of drilling wells, were deductible as research and experimental expenditures. However, under present law, the costs of determining the exist-

[1] In the *Reich* case, the Tax Court held that the product of the taxpayers' geothermal steam wells was a gas, and that the taxpayers as a result were entitled to expense currently their intangible drilling costs (sec. 263(c) of the Code). The court held further that the taxpayers were entitled to the then 27½ percent depletion deduction allowance for their product because (1) their product was steam, not inexhaustible earth heat, (2) the particular geothermal wells in question were exhaustible, (3) steam is a gas, and (4) the exclusion from the right to depletion of "water" in section 613(b)(7) of the Code does not exclude steam from the depletion allowance.

ence, location, extent, or quality of any oil, gas, or other mineral deposit are not deductible as research and experimental expenditures, and must be capitalized.

Application of minimum tax.—To the extent that geothermal wells are determined to be gas wells, as they were by the *Reich* court, the minimum tax, the recapture provisions and the at risk rules which the Tax Reform Act of 1976 applied to oil and gas wells would apply to geothermal wells. Under the Tax Reform Act of 1976, the deduction for intangible drilling costs on oil and gas wells is treated as a tax preference item for purposes of the minimum tax to the extent that it exceeds the amortization which would have been allowed on the basis of a 10-year life or cost depletion. In the Tax Reduction and Simplification Act of 1977, the Congress provided that for taxable years beginning only in 1977 intangible drilling and development costs (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. However, this rule would not apply for future years unless there is further Congressional action. These rules would apply to the extent that a geothermal deposit was determined to be a gas well.

Recapture.—The Tax Reform Act of 1976 also provided for the recapture of certain intangible drilling and development costs upon the disposition of oil and gas properties. The amount subject to recapture is the amount deducted for intangible drilling and development costs reduced by the amount which would have been deductible had those intangible costs been capitalized and deducted through cost depletion. The amount recaptured is to be treated as ordinary income; it cannot exceed the gain realized or the difference between the fair market value of the property transferred over the basis in the property. The recapture rule generally applies regardless of any other Code provision which otherwise would provide for nonrecognition and the rule applies on a property-by-property basis.

At risk limitation

In addition, the Tax Reform Act of 1976 provided that the amount of any loss (otherwise allowable for the year) which may be deducted in connection with exploring for, or exploiting, oil and gas resources cannot exceed the aggregate amount with respect to which the taxpayer is at risk with respect to the property at the close of the taxable year (i.e., generally the amount of an otherwise allowable loss for the year cannot exceed the taxpayer's basis reduced by any nonrecourse borrowing to which the property is subject). The at risk limitation applies to all taxpayers except corporations which are not subchapter S corporations or personal holding companies.

Reasons for change

To encourage the exploration for, and the drilling and development of, geothermal wells and to accord geothermal resources uniform tax treatment, the Committee decided to provide for all geothermal resources incentives similar to those provided for oil and gas.

Explanation of provisions

Percentage depletion

The committee bill provides an allowance for percentage depletion for all geothermal deposits regardless of whether or not the geothermal resource would qualify for depletion under present law and regardless of whether or not the resource in fact is renewable, so long as the deposit is located within the U.S. or its possessions. The percentage is 22 percent for production in the years 1978 through 1980, 20 percent for the year 1981, 18 percent for the year 1982, 16 percent for the year 1983, and 15 percent for the years 1984 and thereafter. For purposes of these rules, a geothermal deposit means a geothermal reservoir of natural heat which is stored in rocks or in an aqueous liquid or vapor (whether or not under pressure). (H.R. 8444, the House-passed energy bill, provides a 10-percent depletion allowance.) Under the committee bill, the amount of the allowance is not limited to the taxpayer's adjusted cost basis in that property. (The House-passed bill provided such a limitation.)

Generally, the percentage depletion allowed with respect to geothermal deposits is to be governed by the same rules which apply to percentage depletion for other minerals under section 613. (Of course, if cost depletion is greater than percentage depletion with respect to a particular property containing geothermal deposits, the depletion allowance will be computed under the cost depletion method.)

The percentages allowed under the committee bill are the same percentages allowed for independent oil and gas producers under section 613A of the Code. However, in order to encourage this relatively undeveloped resource, the committee bill exempts geothermal deposits from the limitations and the restrictions in section 613A. Therefore, percentage depletion for geothermal deposits is available to all producers, including major producers who are not eligible for percentage depletion with respect to their oil and gas production. Also, percentage depletion is allowable for all of the taxpayer's geothermal deposits. (It is not limited to a certain number of barrels per day, or the Btu equivalent in the form of geothermal energy.) Further, the 65 percent of taxable income limitation, imposed on percentage depletion in the case of oil and natural gas, does not apply to percentage depletion for geothermal deposits. However, the usual rules (under sec. 613) for determining the taxpayer's gross income from the property are to apply, including those for allocating the income among resources where different resources are recovered.

Intangible drilling costs

Deduction.—The committee bill provides taxpayers with the option to deduct currently, rather than to capitalize, intangible drilling and development costs related to the exploration for, and the development of, geothermal deposits located in the U.S. or its possessions. Geothermal deposits are defined by the bill to mean geothermal reservoirs consisting of natural heat which is stored in rocks or in an aqueous liquid or vapor (whether or not under pressure). The election to

capitalize or to deduct intangible drilling costs must be made prior to the expiration of the time for filing claims for credit or refund of any overpayment of tax imposed with regard to the taxpayer's first taxable year to which the provision is effective and for which intangible drilling costs are paid or incurred. Prior to the expiration of this period, but not thereafter, the election may be changed or revoked. A taxpayer having properties containing geothermal deposits and other properties containing oil and natural gas (or geopressurized methane) may make different elections for properties containing different kinds of natural resources, but must make one election for all properties containing the same type of resource (in accordance with regulations to be prescribed by the Secretary).

Application of minimum tax.—The committee bill also provides that the excess of the intangible drilling and development costs over the amount of those costs which would have been amortizable on the basis of a 10-year life or under cost depletion and which further exceed the taxpayer's income from the production of geothermal resources constitutes a tax preference item for purposes of the minimum tax on individuals. To ascertain the amount of the intangible drilling and development costs over the amount amortizable, which is subject to the minimum tax, the taxpayer's income from oil and gas properties and geopressurized methane gas properties is to be determined separately from the calculation of income from geothermal properties. Moreover, the committee bill also provides that the excess of the allowable depletion deduction, with respect to each geothermal property, over the adjusted basis of that property at the end of the taxable year, is to be treated as an item of tax preference subject to the minimum tax.

Recapture.—The committee bill also provides that gain on the disposition of geothermal properties will be subject to recapture (i.e., treated as ordinary income rather than capital gain) to the extent that the amount of the intangible drilling cost deductions exceed the amount which would have been allowable had the costs been capitalized and deducted through cost depletion.

At risk limitation

The committee bill provides that the amount of any loss (otherwise allowable for the year) which may be deducted in connection with exploring for, or exploiting, geothermal deposits cannot exceed the aggregate amount with respect to which the taxpayer is at risk at the close of the taxable year, as determined under existing law (sec. 465). For purposes of the at risk rules, developing geothermal deposits is to be treated as a separate activity (distinguished, for example, from oil or gas activities, or the development of geopressurized methane). The at risk limitation applies to all taxpayers other than corporations which are not subchapter S corporations or personal holding companies.

Effective date

The provisions relating to the deduction for intangible drilling costs, to the minimum tax, to recapture, and to the at risk rules apply with respect to wells commenced on or after April 20, 1977, in taxable years ending on or after that date.

The provision relating to the provision for a 22-percent depletion allowance applies to taxable years ending after December 31, 1977.

Revenue effect

The revenue loss from permitting the expensing of intangible drilling costs for geothermal discovery and development is estimated to be $5 million in fiscal 1978, $12 million in fiscal 1979, and $36 million by fiscal 1985.

The revenue loss attributable to the provision of a percentage depletion allowance at a 22-percent rate for all geothermal resources is estimated to be negligible for fiscal years 1978–1980, and $14 million for fiscal 1985.

Energy savings estimate

It is estimated that the additional energy that would be made available due to the provision for the expensing of intangible drilling cost for geothermal discovery and development the 22-percentage depletion allowance, and the additional investment tax credit available in section 1031 of the bill would reduce oil imports in 1985 by 50,000 barrels per day.

3. Geopressurized Methane Gas (secs. 1042 and 1043 of the bill and secs. 44G, 57, 263, 465, 613, 614, 617 and 1254 of the Code)

Present law

Geopressurized methane gas essentially is natural gas dissolved in water, and contained in a geopressurized aquifer,[1] up to and including 1,000 standard cubic feet per barrel of fluid for approximately the first 100 million cubic feet of production.[2]

Percentage depletion

Current law is unsettled as to the appropriate depletion rate for geopressurized methane gas. As a gas, it could be argued that an independent producer of geopressurized methane is entitled to claim the depletion rate set forth in sec. 613A(c)(5). Alternatively, as a geothermal resource, geopressurized methane could be entitled to a 22-percent depletion rate for all years without the independent producer requirements (under sec. 613A(b)(1)(*c*)) if it was determined to be a geothermal deposit which was a gas well. In addition, it could be argued that geopressurized methane gas is encompassed within the provision for miscellaneous minerals (sec. 613(b)(7)) and, therefore, entitled to a 14-percent depletion rate.

While it is difficult to determine precisely which depletion rate applies to geopressurized methane, generally, except in the case of certain independent producers, the Tax Reduction Act of 1975 eliminated the depletion allowance for oil and gas. However, percentage depletion was retained for the independent producer [3] for average daily production up to a specified level.

The exemption for oil was 2,000 barrels a day in 1975 and is being reduced 200 barrels per day a year for 5 years from 1976 through 1980 when the permanent exemption will be 1,000 barrels a day. For 1977,

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[1] A geopressurized aquifer is a sandstone formation filled with saline water and dissolved gas, including methane, at a static formation pressure in excess of .6 psi per foot of depth. These features generally distinguish geopressurized methane gas from natural gas which is produced along with some water.

[2] It is estimated that this quantity should be reached in approximately the first three months of geopressurized methane production. After the first 100 million cubic feet of production, the amount of methane per barrel of water may increase above 1,000 standard cubic feet due to separation of the methane and water in formation.

[3] Under the Tax Reduction Act of 1975, the percentage depletion deduction generally was restricted to independent producers and was eliminated for major oil companies, by denying the deduction to an "integrated" operation, that is to a taxpayer (1) who sells oil or natural gas or their products through a retail outlet which he or a related person owns, or (2) who sells oil or natural gas or their products to any person who is contractually obligated to the taxpayer to market or distribute the latter's oil or gas, etc., under the taxpayer's trademark or trade name, etc., or who leases a retail outlet from or is controlled by the taxpayer. The retailer restriction does not apply to cases where gross receipts for sales of oil, gas, etc., from all retail outlets do not exceed $5 million annually. (Code section 613A.) In addition a taxpayer is considered a refiner of crude oil if the taxpayer's refinery run exceeds 50,000 barrels on any day.

the percentage is 22 percent and the number of barrels is 1,600 per day. Gas wells are allowed percentage depletion for an equivalent average daily production level, but if the taxpayer elects percentage depletion for natural gas, he must reduce his maximum allowable exemption for oil by the Btu-equivalent of the exempt gas. In addition, the depletion rate for the independent producer will remain at 22 percent through 1980, after which it will be phased down to a permanent level of 15 percent beginning in 1984. The excess of the allowable depletion deduction, with respect to each property, over the adjusted basis of that property at the end of the taxable year, is treated as an item of tax preference subject to the minimum tax. The depletion deduction resulting from the independent producer exemption may not exceed 65 percent of the taxpayer's net income from all sources (computed without regard to the depletion deduction, net operating loss carrybacks and captial loss carrybacks).

Exploratory costs

Under present law, expenditures incurred in connection with the exploration phase of geopressurized methane which results in dry holes are deductible at the time when the well (or leasehold) is abandoned. Moreover, to the extent that these expenditures result in new processes or technology, it is possible under present law that these costs would be considered to be research and experimental expenditures subject to the election to be deducted currently or to be amortized over a 60-month period. For example, in Revenue Ruling 74-67, 1974-1 C.B. 63, the Internal Revenue Service held that certain costs of developing a method for the hydraulic mining of hard minerals, including a portion of the cost of drilling wells, were deductible as research and experimental expenditures. However, under present law the costs of determining the existence, location, extent, or quality of any oil, gas, or other mineral deposit (generally referred to as geological and geophysical expenses, or "G&G") are not deductible as research and experimental expenditures, and must be capitalized.

Intangible drilling costs

Application of the minimum tax.—Under present law, the operator of an oil or gas well may elect to deduct intangible drilling and development costs as an expense rather than capitalize the costs and recover them through depletion and depreciation deductions. Generally, intangible drilling and development costs are defined as those expenditures made by the owner of the operating interest or wages, fuel, repairs, hauling, supplies, etc., incurred in preparing a drill site, drilling and cleaning a well, and constructing assets which are necessary in drilling the well and preparing it for production (such as derricks, pipelines, and tanks). Under the Tax Reform Act of 1976, the deduction for intangible drilling costs 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 is 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 intangible drilling and development costs (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. However, this rule would not apply for future years unless there is further Congressional action. These rules would apply to the extent that a geopressurized methane deposit was determined to be a gas well.

Recapture.—The Tax Reform Act of 1976 also provided for the recapture of certain intangible drilling and development costs upon the disposition of oil and gas properties. The amount subject to recapture is the amount deducted for intangible drilling and development costs reduced by the amount which would have been deductible had those intangible costs been capitalized and deducted through cost depletion. The amount recaptured is to be treated as ordinary income; it cannot exceed the gain realized or the difference between the fair market value of the property transferred over the basis in the property. The recapture rule generally applies regardless of any other provision of the Code which otherwise would provide for nonrecognition and applies on a property-by-property basis.

At risk limitations

In addition, the Tax Reform Act of 1976 provided that the amount of any loss (otherwise allowable for the year) which may be deducted in connection with exploring for, or exploiting, oil and gas resources, cannot exceed the aggregate amount with respect to which the taxpayer is at risk with respect to the property at the close of the taxable year (i.e., generally the amount of an otherwise allowable loss for the year cannot exceed the taxpayer's basis reduced by any nonrecourse borrowing to which the property is subject). The at risk limitation applies to all taxpayers except corporations which are not subchapter S corporations or personal holding companies.

Reasons for change

To encourage the exploration for, and the drilling and development of, geopressurized methane gas, the Committee decided both to clarify the treatment of this resource, and to provide various incentives, similar to those provided for other resources, for its production.

Explanation of provisions

Definition

The committee bill requires the Secretary of the Treasury, after consultation with the Secretary of Energy, to issue an appropriate definition of geopressurized methane gas. This provision is necessary so that the geopressurized methane gas can be distinguished from more conventional gaseous substances, for example, natural gas contained in water, or natural gas which contains some fluids. Generally, the committee bill applies the rules which are applicable to oil and gas to geopressurized methane gas.

Percentage depletion

The committee bill provides a 10-percent allowance for percentage depletion for geopressurized methane gas located in the U.S. or its possessions, without regard to the application of section 613A. This allowance would apply only to the gas at the wellhead produced from

a geopressurized methane gas well, and would not extend to the brine which is produced from the well along with the gas. No depletion allowance is to be allowed with respect to geopressurized brine which is produced from the well together with the gas, and which thereafter is reintroduced into the ground. (However, under appropriate circumstances the brine may qualify for the depletion allowance applicable for geothermal resources generally.) In other respects, the computation of percentage depletion is to be comparable to the computation (under sec. 613) with respect to natural gas sold under fixed contracts and regulated natural gas (which are exempted from the limitations of sec. 613A). Thus, gross income is determined in accordance with the rules for oil and gas wells, and the production of geopressurized methane gas is not considered to be mining. Furthermore, the excess of the allowable depletion deduction, with respect to each geopressurized methane gas property, over the adjusted basis of that property at the end of the taxable year, is to be treated as an item of tax preference subject to the minimum tax. Moreover, the allowance for depletion may not exceed 50 percent of the taxable income from each property, computed without the allowance for depletion. Where more than one resource is produced from the same well, the usual allocation rules are to apply.

Geological and geophysical costs

The committee bill would provide taxpayers with the option to deduct currently, rather than requiring the capitalization of, geological and geophysical (G&G) costs incurred only in the exploration for geopressurized methane located in the U.S. or its possessions. These costs are subject to recapture through the deduction for depletion in the taxable year in which the property becomes productive, or if the taxpayer receives or accrues a bonus or royalty with respect to the property. Generally, G&G costs also are subject to recapture upon disposition of the property. These rules are similar to those applicable to mine exploratory expenses. These costs generally would include such items as aerial photography, geological mapping, airborne magnetometer surveys, gravity meter surveys, and seismograph surveys. G&G costs, however, do not include any exploratory or developmental drilling expenses, nor do they include any expenditures for the acquisition or improvement of depreciable property. The election to deduct G&G costs is to be made in accordance with regulations and substantiation requirements prescribed by the Secretary.

Due to the difficulty of, and expenses involved in, locating commercially exploitable quantities of geopressurized methane gas, the Committee decided to provide an incentive for the production of this energy source which is inapplicable in the case of any other resource. Under present law, G&G costs are capitalized and become part of the taxpayer's basis.

The Committee recognizes, however, that because G&G costs will be deductible currently only when they are incurred in exploring for geopressurized methane gas that various timing and identification problems are likely to arise, especially since G&G equipment and methodologies generally are interchangeable between resources. Nevertheless, there are several factors which might be used to indicate

whether a taxpayer incurred G&G costs exploring for geopressurized methane gas. For example, if a taxpayer has secured a permit from the appropriate state agency to drill for geopressurized methane gas at the time when the G&G costs were incurred with regard to the drilling site, this would be a strong indication that the costs actually were incurred in exploring for geopressurized methane gas. Conversely, an oil or natural gas drilling permit would tend to indicate that the G&G costs should be capitalized. Where a taxpayer has not secured a drilling permit for geopressurized methane gas at the time when the costs are incurred, but subsequently obtains such a permit for the property, this would tend to support a claim for current deductibility of G&G costs, unless the taxpayer also secured drilling permits for other minerals. Similarly, if the taxpayer had a mineral interest in the property which did not include geopressurized methane gas, this would tend to indicate that the G&G costs should be capitalized.

The Committee anticipates that the Secretary of the Treasury will promulgate regulations which will contain other factors which might be used to distinguish deductible from capitalized G&G costs.

Intangible drilling costs

Deduction.—The committee bill provides taxpayers with the option to deduct currently rather than to capitalize intangible drilling and development costs related to the exploration for, and the development of, geopressurized methane gas located in the U.S. or its possessions. Geopressurized methane gas is to be defined by the Secretary of the Treasury.

The election to capitalize or to deduct intangible drilling costs must be made prior to the expiration of the time for filing claims for credit or refund of any overpayment of tax imposed with regard to the taxpayer's first taxable year to which the amendment is effective and for which intangible drilling costs are paid or incurred. Prior to the expiration of this period, but not thereafter, the election may be changed or revoked. A taxpayer having properties containing geopressurized methane gas and other properties containing oil and natural gas, or geothermal deposits may make different elections for properties containing different kinds of natural resources, but must make one election for all properties as to the same type of resource.

Application of the minimum tax.—The committee bill also provides that the excess of the intangible drilling and development costs over the amount of those costs which would have been amortizable on the basis of a 10-year life or cost depletion and which further exceed the taxpayer's income from the production of geopressurized methane gas constitutes a tax preference item for purposes of the minimum tax on individuals. To determine the amount of the intangible drilling and development costs over the amount amortizable, which is subject to the minimum tax, the taxpayer's income from oil, gas, and geothermal properties is to be determined separately from the calculation of income from geopressurized methane gas properties.

In addition, the minimum tax is to apply to the excess of the allowable depletion deduction, with respect to each geopressurized methane gas property, over the adjusted basis of that property at the end of the taxable year.

Recapture.—The committee bill also provides that gain on the disposition of geopressurized methane gas properties will be subject to recapture (i.e., treated as ordinary income rather than capital gain) to the extent that the amount of the intangible drilling cost deductions exceed the amount which would have been allowable had the costs been capitalized and deducted through cost depletion.

At risk limitation

The committee bill provides further that the amount of any loss (otherwise allowable for the year) which may be deducted in connection with exploring for, or exploiting, geopressurized methane gas properties cannot exceed the aggregate amount with respect to which the taxpayer is at risk at the close of the taxable year, as determined under existing law (sec. 465). For purposes of the at risk rules, developing geopressurized methane gas is to be treated as a separate activity (distinguished, for example, from oil and gas activities, or the development of geothermal deposits). The at risk limitation applies to all taxpayers other than corporations which are not subchapter S corporations or personal holding companies.

Effective date

The provisions relating to the deduction for intangible drilling costs, to the minimum tax, to recapture, and to the at risk rules apply with respect to wells commenced on or after April 20, 1977, in taxable years ending on or after that date.

The section relating to the provision for a 10-percent depletion allowance applies to taxable years ending after December 31, 1977.

The provision relating to the deduction for G&G costs applies to taxable years ending after December 31, 1977.

Revenue effect

The provision of a 10-percent depletion allowance for geopressurized methane will have no revenue effect for fiscal years 1978 and 1979, but will result in revenue losses of approximately $14 million in fiscal year 1985.

The revenue loss attributable to the option to deduct intangible drilling costs will be approximately $9 million in fiscal year 1978, $16 million in fiscal year 1979, and $23 million in fiscal year 1985.

4. Credit for Production of Oil and Gas from Nonconventional Sources (sec. 1044 of the bill and sec. 44G of the Code)

Present law

Present law contains no special provisions for oil or gas production from nonconventional sources. However, oil shale is entitled to a 15 percent depletion allowance applied to the value of the shale oil after retorting (heating) but before the hydrogenation process (sec. 613 (b)(2)(B) of the Code).[1] Taxpayers engaged in oil shale production are entitled to all applicable business tax incentives, including the investment credit under the provisions' general rules.

The proper depletion rate for geopressurized methane gas is unsettled under current law. Natural gas produced from tight rock formations is entitled to percentage depletion at a rate of 22 percent under section 613A. Taxpayers engaged in the business of producing such gas are subject to all the rules generally applicable to income from conventional gas wells, and would be entitled to the same business tax incentives allowed to gas producers under present law.

Reasons for change

Oil shale

Oil shale is a major but underdeveloped fossil energy resource in the United States. Total U.S. oil shale resources have been estimated to contain 2,400 billion barrels of oil. Oil shales [2] are underground sedimentary layers of finely grained rock which is rich in organic matter. The oil which can be extracted from this shale requires only minimal additional refining in order to make it equivalent to conventional crude petroleum. However, the cost of producing shale oil exceeds the cost of producing conventional oil by drilling. The Committee believes that commercial production of shale oil should be encouraged and that tax incentives rewarding actual production would best motivate the development of this resource.

Geopressurized methane gas

Geopressurized methane gas is located in extensive deep (1 to 4 miles) zones of pressurized water with widely varying salinity in which the pressure exceeds the corresponding pressure of the water at that depth. The geopressured fluids of the Gulf Coast have a very large energy potential particularly with respect to geopressurized methane gas. Other geopressured sections of the Gulf Coast and other

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[1] However, shale used or sold for use in the manufacture of sewer pipe or brick and shale used or sold for use as sintered or burned lightweight aggregates is entitled to a seven and one-half percent rate of depletion under section 613(b)(5). Shale which is not used for the purposes specified in section 613(b)(5) or which does not constitute oil shale is entitled to a five percent rate of depletion under section 613(b)(6)(A).

[2] Shale is a rock that is formed by the consolidation of clay, mud, or silt, has a finely stratified or laminated structure, and is composed of minerals essentially unaltered since deposition.

regions of the country probably have at least three times more potential energy than the evaluated part, but the recoverable fraction may be considerably less because of lower average porosity and permeability which make it harder for the methane to be extracted. Much of the geopressured resource was considered by the U.S. Geological Survey to be recoverable at one to two times 1975 prices.

Tight rock formations

Significant deposits of natural gas are located in tight rock formations such as the Devonian shales in the Appalachians, coal seam methane deposits, and Western tight rock formations. The low permeability of these rock formations makes extraction of the gas from the rock more difficult and expensive than the extraction of gas by ordinary drilling methods from conventional gas deposits.

The Committee believes providing a tax incentive for the production of oil and gas from nonconventional sources, such as oil shale, geopressurized methane gas and tight rock formations would encourage the development of these energy resources.

Explanation of provisions

Shale oil

The committee bill allows a taxpayer a $3 credit against his tax liability for each barrel of shale oil which is produced from the taxpayer's property during the taxable year. Shale oil is the liquid oil obtained from the oil shale after the retorting (heating) process, but before hydrogenation, refining, or any other process subsequent to retorting.

Geopressurized methane gas and tight rock formation gas

The bill allows a taxpayer a 50-cent credit against his tax liability for a taxable year for each thousand cubic feet of gas produced during the txable year from all tight rock formation property in which the taxpayer has an interest and which is attributable to the taxpayer. The same credit applies for each thousand cubic feet of geopressurized methane gas, which is produced during the taxable year from all geopressurized methane gas property (within the meaning of section 465(c)(2)(F)) in which the taxpayer has an economic interest but only to the extent that such production is attributable to the taxpayer.

Who is entitled to the credit

Under the bill, a taxpayer is entitled to the credit for nonconventional oil or gas production, if and to the extent that he has an ownership interest in the oil shale or the gas property. The bill establishes a ratio for determining the production attributable to a taxpayer for oil or gas produced from any property during a taxable year. The production attributable to a taxpayer for a taxable year is to be equal to an amount bearing the same ratio to the total production from the property during the year as the amount of the taxpayer's gross income from the property for the taxable year (under section 613(a)) on account of such production bears to the aggregate gross income from the property for the year (within the meaning of section 613(a)) of all parties having an interest in such property. By placing in the denominator of the fraction established by this ratio the aggregate gross income of all parties, including, for example the "gross income"

of Federal, State or local governments from the property, the full 100 percent of the production from the property is taken into account.

The production credits allowed by this bill apply only with respect to oil and gas produced from a property located in, or offshore of, the United States (within the meaning of paragraph (1) of section 638) or in, or offshore of, a possession of the United States.

Definitions

After consultation with the Secretary of Energy, the Secretary of Treasury is to establish by regulation standard scientific definitions of shale oil, geopressurized methane gas and tight rock formations.

The terms "oil shale property" and "tight rock formation property" means any property with respect to which the taxpayer is claiming a production credit allowed by the bill. The bill applies the present law definition in section 614 of the Code to the term "property" for purposes of the production credits, so that generally the term means each separate interest owned by the taxpayer in each oil shale deposit or tight rock formation gas deposit in each separate tract or parcel of land. (Geopressurized methane gas wells are included within the section 614 definition of property under another section of the committee bill.)

The term "barrel" is defined to mean 42 United States gallons. Credits for fractions of a barrel or fractions of a thousand cubic feet are to be determined on a proportional basis.

Application with other credits

The credit for production of oil and gas from nonconventional sources may be claimed only after a taxpayer's income tax liability has been reduced by the sum of all the nonrefundable tax credits allowed under sections 32 through 45 of the Code, but before any reduction in liability on account of the refundable tax credits: section 31 (relating to the credit on tax withheld on wages); section 39 (relating to the credit for certain uses of gasoline, special fuels, and lubricating oil); section 43 (relating to the earned income credit); section 44C (relating to the home insulation credit); section 44E (relating to the intercity bus credit); and section 44F (relating to the energy investment credit).

Effective date

The production credits to apply to taxable years beginning after December 31, 1977.

Revenue effect

The credit for shale oil production will reduce revenues about $4 million in fiscal 1978, $19 million in fiscal 1979, and $327 million in fiscal 1985. The credit for geopressurized methane gas production will have no impact on revenues in fiscal years 1978 and 1979; it will reduce revenues by $52 million in fiscal 1985. The credit for tight rock formation gas production will not affect revenues in fiscal years 1978 and 1979; it will reduce revenues by $194 million in fiscal 1985.

Energy savings estimate

By 1985, this amendment is expected to result in shale oil production 200,000 barrels per day, geopressurized methane and tight rock gas production which will reduce oil imports by 45,000 barrels of oil per day in 1985.

5. Percentage Depletion for Peat (sec. 1042 of the bill and sec. 613(b) of the Code.)

Present law

Under present law, taxpayers may claim a five-percent depletion deduction for natural deposits of peat.[1] Peat is a dark brown or black residuum produced by the partial decomposition and disintegration of mosses, sedges, trees, and other plants which grow in marshes and similar wet places.[2] Moss which has not yet disintegrated into peat is not entitled to percentage depletion.[3]

Reasons for change

The Committee believes that a program encouraging conversion to fuels other than oil and gas, particularly coal, should provide incentives for the use of all safe major fuel sources indigenous to the United States. The Committee decided that increasing the depletion rate for peat which is used as fuel or fuel source, to the same percentage allowed coal and lignite would promote the production and use of peat, the nation's second most abundant fuel.

Explanation of provision

The bill increases the percentage depletion rate for peat from deposits in the United States which is used directly as a fuel or otherwise to produce energy from five percent to 10 percent. Peat which is used for other purposes, primarily agricultural, remains entitled to depletion at the present five percent rate.

Effective date

The increase in percentage depletion for peat used directly or indirectly for fuel is to apply to taxable years ending after December 31, 1977.

Revenue effect

This provision is expected to reduce revenues by less than $1 million annually.

Energy saving estimate

This provision is expected to have a negligible impact on energy savings.

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[1] Section 613(b)(6)(A) of the Code.
[2] Rev. Rul. 57-336, 1957-2 C.B. 325.
[3] Section 613(b)(7)(A) of the Code.

E. ADDITIONAL INCENTIVES FOR THE PRODUCTION AND CONSERVATION OF ENERGY, FOR CONVERSION TO ALTERNATIVE ENERGY SOURCES, AND FOR DEALING WITH ENERGY-RELATED PROBLEMS; ENERGY TRUST FUND

(Sec. 1054 of the Bill)

The House energy bill (title II of H.R. 8444) contains several new taxes designed to reduce demand for oil and gas, including a wellhead tax on crude oil, a tax on business use of oil and natural gas and a tax on fuel-efficient automobiles. The Committee voted not to adopt any of these taxes. The Committee believes that the nation's energy program should achieve a balance between encouraging energy conservation and encouraging additional energy production, rather than simply emphasizing conservation.

The Committee believes that, if new taxes are to be imposed by this legislation, they should be accompanied by incentives for energy production, which is not the case in the House bill, and more effective incentives for energy conservation and for conversion from conventional oil and gas to alternative sources of energy. Also, they should be accompanied by measures to deal with any adverse and undesirable consequences, such as inequities, which may result from the energy situation. Thus, the committee bill includes a provision which is intended to give the conferees flexibility to make the appropriate amendments should the House conferees insist on the enactment of some of the House-passed taxes, amendments which might not otherwise be within the scope of the conference.

Additional taxes and tax incentives

The committee bill states that no taxes imposed by this bill shall go into effect unless they are accompanied by tax and other incentives for increased energy production, energy conservation, and conversion from conventional oil and gas to alternative sources of energy. Also, they may be accompanied by measures to ameliorate any adverse effects, such as inequities, resulting from the energy crisis and from energy legislation.

The Committee intends that the concept of tax incentives for increased energy production, conservation or conversion be interpreted broadly. Tax and other incentives for greater production would include, for example, modifications of the crude oil equalization tax in the House bill to transfer a portion of the revenue raised by the tax to oil producers. This could be done in several different ways: (1) shifting the tax from purchasers of crude oil to oil producers and royalty holders, allowing the ceiling price of regulated crude oil to rise by the amount of the tax and exempting a portion of each producer's oil pro-

duction from the tax; (2) providing a refundable tax credit to oil producers and royalty holders equal to part or all of the crude oil equalization tax on a portion of their oil; or (3) should the existing oil price controls to expire before October 1, 1981, which could occur anytime after April 30, 1979, at the President's discretion, by modifying the House bill's crude oil equalization tax, which applies only to controlled oil, so that it applies to a portion of the deregulated oil.

Other production incentives would include exemptions from the crude oil equalization tax for small refiners or modifications of the crude oil entitlements program to aid small refiners. This could include treating as separate entities refineries which are owned or controlled by a small refiner and which serve different marketing areas.

The Committee intends that the concept of modification of the House-passed taxes to mitigate adverse effects of the energy crisis should also be interpreted very broadly. Such changes could include exemptions from the energy taxes (including credits against the taxes and refunds of the taxes), modifications of exemptions or rebates contained in the House bill (such as the heating oil rebate), provisions to relieve the burden on natural gas users whose gas supplies are curtailed, and excess profits or windfall profits taxes on industries whose profits rise unduly as a result of the energy situation.

Energy trust fund

The committee bill also establishes an Energy Production, Conservation, and Conversion Trust Fund, and appropriates to the Trust Fund the net revenues from any new taxes added by the bill as enacted (not including revenues from the extension of any existing taxes). The Trust Fund is to consist of two accounts—the Energy Financing Program Account and the Energy-Efficient Transit Account—which are to be separately managed and administered as if each such account constitutes a separate trust fund. Amounts in each account shall be available, as provided by appropriations acts, for the purposes specified in the bill.

In the case of the Energy Financing Program Account, amounts may be used solely for purposes of providing financial assistance (including, but not limited to, loan guarantees, price guarantees, and loans) to business concerns for projects involving energy development, production, transportation, transmission, distribution, or conservation, but only if such projects could not receive sufficient funding upon commercially reasonable terms or conditions from other sources to make such project commercially feasible. To avoid duplication of effort, financial assistance would not be available for any project which would be eligible to receive grants or other aid from the Department of Energy. In the case of the Energy-Efficient Transit Account, amounts may be used solely for purposes of energy-efficient transit, including (but not limited to) research and demonstration projects and grants to States for energy-efficient transit purposes or for regional transportation programs.

F. LIMITATION OF PRESIDENT'S AUTHORITY TO ADJUST OIL IMPORTS

(Sec. 1055 of the Bill)

Present law

The Trade Expansion Act of 1962.[1] delegates to the President discretionary authority to adjust imports to the extent which he deems necessary so that they will not threaten to impair the national security (sec. 232(b)). Adjustments to limit imports may take the form of either quantitative restrictions, called quotas, or monetary exactions, usually called tariffs, duties, or import license fees.[2]

In determining whether any imports threaten to impair the national security, the Trade Expansion Act of 1962 specifically requires the President, without excluding other relevant factors, to consider:

(1) domestic production needed for projected national defense requirements;

(2) the capacity of domestic industries to meet projected national defense requirements;

(3) existing and anticipated availabilities of the human resources, products, raw materials, and other supplies and services essential to the national defense;

(4) the requirements of growth of industries, supplies and services essential to the national defense, including the investment, exploration, and development necessary to assure such growth; and

(5) the importation of goods in terms of their quantities, availabilities, character, and use as those affect industries essential to the national defense and the capacity of the United States to meet national security requirements.

In administering actions taken under this authority, the President must also recognize the close relation of the U.S. economic welfare to national security, and must consider the impact of foreign competition on the economic welfare of individual domestic industries. In addition, any substantial unemployment, decrease in government revenues, loss of skills or investment, or other serious effects resulting from the displacement of any domestic products by excessive imports are to be considered, without excluding other factors, in determining whether such weakening of the United States' internal economy may impair the national security.

Currently, specific import license fees of 21 cents and 63 cents are imposed on each barrel of imported crude petroleum or petroleum

[1] Public Law 87–794 (as amended).

[2] In *Federal Energy Administration v. Algonquin SNG, Inc.*, 426 U.S. 548 (1976), the Supreme Court upheld as proper under section 232(b) of the Trade Expansion Act of 1962 Presidential action changing the adjustment of oil imports through quotas to adjustment through the imposition of monetary exactions called import license fees.

(106)

products, respectively. Statutory import duties of 5 or 10 cents per barrel, depending on the gravity of the oil, are also imposed. However, these duties reduce the amount of the import license fees.

The Trade Act of 1974 delegates to the President discretionary authority to modify duties on imports under certain circumstances. Title I of the Act authorizes the President to increase or impose U.S. import duties pursuant to trade agreements with foreign countries if he determines that such duties are unduly burdening U.S. foreign trade and interfering with the development of mutually beneficial trade agreements between the United States and foreign countries.

Title V of the Trade Act of 1974 authorizes the President to allow duty free imports of eligible articles, including imports of petroleum and petroleum products, from designated developing countries. In determining whether to grant such treatment, the President must consider the effect of such action in furthering the economic development of the developing country; the extent of any comparable action by other major developed countries; and the impact of such action on U.S. producers of products which are like, or which are directly competitive with, the imported products.

Reasons for change

The Committee believes that the Congress bears the ultimate responsibility for the regulation of foreign imports. Although the Committee recognizes that sudden or severe situations, such as war, require delegation of authority over import adjustments to the President in order that any necessary changes in quotas or duties be made swiftly, the Congress should itself determine any adjustments of imports critical to the national economy, particularly imports of petroleum or petroleum products. In recognition of Congress' reponsibility and in order to avoid any unilateral presidential action with regard to imports which might be designed to affect domestic oil prices, the Committee decided to modify the broad delegation of import authority granted to the President under the Trade Expansion Act of 1962 by limiting his authority over crude oil imports to times of war or actual hostilities. The Committee also limited the President's authority under the Trade Act of 1974.

However, the Committee also recognizes that the need for a strong domestic refining industry occasionally might require swift adjustments of imports of foreign refined petroleum products. The Committee decided to grant the President special authority to adjust imports of refined petroleum products if such products threaten to impair the national security.

The Committee believes it necessary to maintain a competitive domestic refining industry. It is concerned that a crude oil tax together with the cost of environmental and safety requirements could have a serious adverse impact on this industry. Furthermore, the Committee recognizes that the U.S. refining industry must rely heavily on imported crude petroleum, unless domestic supplies increase significantly, if they are to operate at capacity. The industry could be severely injured if import duties on crude oil were increased significantly and suddenly, for example, by the President under the discretionary authority delegated to him under the Trade Expansion Act of 1962. Because the scope of that presidential authority has not been clearly de-

fined and because the Committee considers maintenance of the domestic refining industry important to the national security, the Committee decided expressly to require the President to recognize the relationship between this industry and the national security in making any import adjustments.

Explanation of provision

The committee bill nullifies any presidential adjustment of imports of petroleum and petroleum products under authority granted him under the Trade Expansion Act of 1962 (sec. 232(b)).

An exception to the restrictions on presidential discretion is made for military or defense emergencies involving actual hostilities. The President will continue to have the full discretion which he has under present law to adjust imports of petroleum and petroleum products during a period in which the Congress declares war, the United States Armed Forces are introduced into hostilities pursuant to statutory authorization, a national emergency is created by attack upon the United States, or the United States Armed Forces are introduced into hostilities under circumstances which require a report by the President under the War Powers Resolution (sec. 4(a)). Any adjustment which the President makes affecting import duties under these circumstances will automatically end on the sixtieth day after the cessation of hostilities.

A second exception to the restrictions on presidential authority pertains to adjustments of imports of refined petroleum products. The committee bill provides that upon a request for an investigation of the effects of imported refined petroleum products on the national security by any interested party or the head of a Federal department or agency, or on his own initiative, the Secretary of the Treasury must report his findings and recommendations to the President within 6 months from the date of the request or the beginning of the investigation.

If the Secretary finds in his investigation that imports of refined petroleum products threaten to impair the national security, he must relate this determination to the President. The President then shall decide whether any action is needed. The bill authorizes the President to take such action as he deems necessary, including the imposition or adjustment of tariffs, fees, or quotas on imported refined petroleum products for as long as he believes required so that such imports do not threaten the national security.

In deciding whether imports of refined petroleum products should be adjusted, the bill requires the President to consider all the relevant factors which he must take into account under the statute in exercising his present law authority over imports under the Trade Expansion Act of 1962.

In adjusting imports of foreign refined petroleum products, the amendment specifically requires the Secretary of the Treasury and the President to recognize the close relation between national security and a modern domestic refining industry which is competitive with foreign refineries. They also must consider the economic welfare and capital investment needs of the industry. The impact of excessive imports of refined petroleum products, such as substantial unemployment, decrease in government revenues, loss of skills or investment, or other

adverse effects must be weighed, without at the same time disregarding any other relevant factors which must be considered under this provision in making any adjustment, such as the possible effects of any proposed action on the economy, on regional needs, or on consumers.

The provision further restricts the authority to adjust import duties, including duties on petroleum and petroleum products, granted the President by the Trade Act of 1974. The provision bars any increase in or imposition of U.S. import duties on petroleum or petroleum products as part of any trade agreement between the United States and a foreign country. The provision also provides that the President may not designate either petroleum or refined petroleum products imported from a developing country as eligible articles for preferential duty-free import treatment.

Effective date

The limitations on the President's authority to adjust imports of petroleum or petroleum products are effective after October 14, 1977.

G. OTHER PROVISIONS

1. Intangible Drilling Costs of Oil and Gas Wells (sec. 1051 of the bill and sec. 57 of the Code)

Present law

Under present law, the operator of an oil or gas well may elect to deduct intangible drilling and development costs as an expense rather than capitalize the costs and recover them through depletion and depreciation deductions. Generally, intangible drilling and development costs are defined as those expenditures made by the owner of the operating interest for wages, fuel, repairs, hauling, supplies, etc., incurred in preparing a drill site, drilling and cleaning a well, and constructing assets which are necessary in drilling the well and preparing it for production (such as derricks, pipelines, and tanks). Under the Tax Reform Act of 1976, the deduction for intangible drilling costs 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 is 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 intangible drilling and development costs (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. However, this rule would not apply for future years unless there is further Congressional action.

Reasons for change

The classification of certain intangible drilling expenses as a tax preference item under the minimum tax in order to curtail the use of oil and gas tax shelters resulted in a disincentive for increased exploration by individuals in the business of exploring for oil and gas and developing oil and gas properties. This disincentive has a significant impact, particularly on independent producers, who do most of the exploratory drilling for new oil in the United States.

The Committee believes that by applying the preference only where intangible drilling costs exceed oil and gas production income the preference will not constitute a major disincentive to those individuals in the oil and gas business, but will continue to limit the ability of outside investors to reduce the income tax paid on their wage and salary income through the use of tax shelters.

Explanation of provision

The committee bill extends for all future years the minimum tax provision on intangible drilling costs of individuals currently applicable for 1977. As a result, intangible drilling cost deductions for oil or gas wells would be included in the minimum tax base of indi-

viduals only to the extent that intangible drilling and development costs, over the amount of those costs amortizable on the basis of a 10-year life or under cost depletion, exceed the taxpayer's income from oil and gas properties. Income from oil and gas properties is to be determined first with reference to the rules for determining gross income from oil and gas properties for purposes of percentage depletion (sec. 613(a) of the Code, without regard to the limitations under sec. 613A). Net income from oil and gas properties is gross income from oil and gas properties reduced by the amount of deductions properly attributable to that gross income (and deductions attributable to oil and gas properties with no gross income), except that no reduction is to be made for those intangible drilling costs subject to the minimum tax (i.e., those incurred on successful wells).

Effective date

These provisions are to be effective upon enactment and apply to taxable years ending after December 31, 1977.

Revenue effect

The provision limiting the minimum tax on intangible drilling costs for oil and gas to the amount in excess of net related income is estimated to reduce budget receipts by $32 million in fiscal 1979, $37 million in fiscal 1980, and $74 million in 1985.

Energy savings estimate

There is no estimate of the increase in the supply of oil, gas, or geothermal energy which would result from the enactment of this provision.

2. Rerefined Lubricating Oil (sec. 1052 of the bill and sec. 4093 of the Code)

Present law

Present law imposes a manufactures excise tax of 6-cents-per-gallon on lubricating oil (other than cutting oils) sold in the United States by the manufacturer or producer (sec. 4091). Also, a manufacturer of lubricating oil is liable for the tax if he uses the oil himself rather than selling it (unless the oil is used in manufacturing a product which is subject to a manufacturers excise tax). The net revenues from the tax (after refunds or credits for nonhighway use) go into the Highway Trust Fund (through September 30, 1979).

Cleaning, renovating, or refining used oil is not considered to be manufacturing, so the sale of recycled or rerefined oil by a refiner is not subject to the excise tax. However, where new lubricating oil is mixed with waste or rerefined oil, this does constitute manufacturing, and the excise tax is imposed on the portion of the mixture which consists of new lubricating oil.

Although present law taxes most sales of lubricating oil, present law also allows a tax refund or credit where lubricating oil is used for any purpose other than lubricating a highway motor vehicle. No refund is available where the oil, including rerefined oil, was exempt from tax in the first place. However, present law also denies the exemption where part of the oil was exempt from tax. As a result, when new oil and rerefined oil are blended, a tax is imposed on the new oil portion of the blend, but no refund or tax credit is available. Thus the tax laws provide a disincentive to the use of new or recycled oil.

In nontax areas, Congress has recently acted to encourage the use of recycled oil. Under section 383 of the Energy Policy and Conservation Act (Public Law 94–163), various Federal agencies are instructed to encourage the recycling of used oil, and to promote the use of the oil so processed or rerefined. The purpose of this mandate is to reduce the consumption of new oil by using recycled oil where appropriate, and to reduce environmental hazards and wasteful practices associated with the disposition of used oil. Recycled oil is to be tested to determine the uses for which it is substantially equivalent in performance to new oil; existing Federal rules pertaining to the labeling of recycled oil are to be changed so that recycled oil which is substantially equivalent to new oil will not be labeled to connote that it is less than equivalent to new oil for a particular purpose. In addition, the Act instructs Federal officials to revise procurement practices to encourage the procurement of recycled oil for military and nonmilitary uses wherever such recycled oil is available at prices competitive with new oil produced for the same use.

Reasons for change

To encourage the conservation and use of previously used oil, as well as to promote the disposition of spent additives in an environmentally acceptable manner, the committee bill removes the excise tax disincentive to the use of rerefined oil.

Explanation of provision

The bill exempts the sale of lubricating oil from the 6-cents-per-gallon manufacturer's excise tax where the lubricating oil is sold for use in mixing with 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 with regard to the portion of the new oil that does not exceed 55 percent of the mixture.

Effective date

This provision is effective for sales on or after the first day of the first calendar month beginning more than 10 days after the enactment of this Act.

Revenue effect

The exemption from the 6-cents-per-gallon excise tax for lubricating oil mixed with waste or rerefined oil will reduce revenues by about $3 million per year. These revenues would otherwise go into the Highway Trust Fund (through September 30, 1979).

Energy savings estimate

It is estimated that this provision will result in negligible energy savings.

3. Annual Report on Energy and Revenue Effects of the Bill (sec. 1053 of the bill)

To assist the Congress in assessing the need for future legislation and developing subsequent programs, the Committee decided that an evaluation of the revenue impact and energy saving effectiveness of the provisions of this bill is necessary.

The provision requires the President to submit an annual report to the Congress every August after 1977. The report is to provide estimates of the amount of revenue increases or decreases resulting from each of the provisions of this bill and an evaluation of the extent to which each of the provisions has resulted in increased energy conservation and production.

The provision also requires that the President provide such other information as he determines is relevant for an evaluation of the provisions of the bill. The Committee expects the President to include in his report the petroleum (or natural gas) savings resulting from each provision and the extent to which shifts from petroleum and natural gas to other materials has occurred as a result of each provision.

(114)

4. Reconciliation of Revenue Effect of Bill with Budget Resolution (secs. 1056 and 1057 of the bill)

The Second Concurrent Resolution on the Budget for Fiscal Year 1978 includes a revenue floor of $397 billion. The resolution states that this is consistent with total tax reductions for fiscal year 1978 of $1.1 billion.

The committee wants the energy bill which ultimately emerges from the House-Senate conference to be consistent with the Second Concurrent Resolution on the Budget for Fiscal Year 1978. Because it is not clear to what extent the final version of the bill will contain the large tax increases passed by the House, the committee could not be sure how large a package of tax incentives would be consistent with the budget resolution and precisely what the effective dates of those inventives would have to be.

To ensure that the energy bill is consistent with the second budget resolution, the committee included a provision requiring the Secretary of the Treasury to adjust the effective dates of the tax reductions in the bill in such a way that budget receipts for fiscal year 1978 are not lower than $397 billion—the revenue floor in the second concurrent budget resolution. Any such postponement of an effective date must be to a date no later than October 1, 1978.

Also, the committee bill includes a provision expressing the sense of the Senate that, to the extent practicable, the net tax reduction from this bill for fiscal year 1978 be no greater than $972 million, which is the revenue loss from the House energy bill (title II of H.R. 8444).

(115)

The following sections of the report have been omitted:

VI—Costs of Carrying Out the Bill and Vote of the Committee in Reporting H.R. 5263, as Amended (pages 116-117)

VII—Regulatory Impact of the Bill and Other Matters to be Discussed under Senate Rules (pages 118-122)

VIII—Changes in Existing Law (page 123)

IX-XIII—Additional, Supplemental, and Dissenting Views (pages 125-147)

95TH CONGRESS 2d Session } SENATE { REPORT No. 95-1324

(Numerals at top of page indicate official report page numbers)

ENERGY TAX ACT OF 1978

OCTOBER 11, 1978.—Ordered to be printed

Mr. LONG, from the committee of conference, submitted the following

CONFERENCE REPORT

[To accompany H.R. 5263]

The committee of conference on the disagreeing votes of the two Houses on the amendments of the Senate to the bill (H.R. 5263) to suspend until the close of June 30, 1980, the duty on certain bicycle parts, having met, after full and free conference, have agreed to recommend and do recommend to their respective Houses as follows:

That the House recede from its disagreement to the amendment of the Senate to the text of the bill and agree to the same with an amendment as follows:

In lieu of the matter proposed to be inserted by the Senate amendment insert the following:

The table of contents and the text of the law as amended (pages 1-37) omitted

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JOINT EXPLANATORY STATEMENT OF THE COMMITTEE OF CONFERENCE

The managers on the part of the House and the Senate at the conference on the disagreeing votes of the two Houses on the amendment of the Senate to the bill (H.R. 5263) to suspend until the close of June 30, 1980, the duty on certain bicycle parts, submit the following joint statement to the House and the Senate in explanation of the effect of the action (other than action of a technical nature) agreed upon by the managers and recommended in the accompanying conference report.

General Explanation

House bill

The House bill suspends the duty on certain bicycle parts until June 30, 1980.

Senate amendment

The Senate amendment strikes out all of the House bill after the enacting clause and inserts two titles. Title I contains certain tax and other provisions related to energy and is in reality the Senate position on the matters decided in this conference. In order to bring the House energy tax provisions into conference, the Senate added a title II which is the text of title II of H.R. 8444 (the National Energy Act) as passed by the House.

Conference agreement

The conference agreement does not include any provision relating to the duty on bicycle parts. In order to explain the action agreed upon by the conference, in the remainder of this statement, title I of the Senate amendment will be referred to as the "Senate amendment" and title II of the Senate amendment (embodying the text of title II of H.R. 8444 as passed by the House) will be referred to as the "House bill."

A. RESIDENTIAL ENERGY CREDITS

1. Residential Insulation and Other Energy-Conserving Component Credit

House bill

Under present law, no special tax credit or deduction is allowed for the installation of insulation or other energy-conserving components in or on a taxpayer's residence.

The House bill provides a nonrefundable income tax credit for insulation and other energy-conserving component expenditures for installations in or on the principal residence of the taxpayer. The credit is 20 percent of the first $2,000 of qualifying expenditures, for a maximum credit of $400. The credit would be applied against the taxpayer's liability, and no carryover is provided to the extent the credit exceeds the amount of tax liability.

The credit would be available only with respect to principal residences the construction of which was substantially completed before April 20, 1977. Owners and renters would be eligible for the credit; moreover, an individual who owns stock in a cooperative housing association or who is a member of a condominium management association would be eligible for the credit.

The credit would apply to qualifying insulation and other energy-conserving components. Insulation is defined as any item specifically and primarily designed to reduce, when installed in or on a dwelling or water heater, the heat loss or gain of the dwelling or water heater.

The term "other energy-conserving component" means any item (other than insulation) which is:

(1) a furnace replacement burner designed to achieve a reduction in the amount of fuel consumed as a result of increased combustion efficiency;

(2) a device for modifying flue openings designed to increase the efficiency of operation of the heating system;

(3) an electrical or mechanical furnace ignition system which replaces a gas pilot light;

(4) a storm or thermal window or door for the exterior of the dwelling;

(5) a clock thermostat;

(6) caulking or weatherstripping of an exterior door or window; or

(7) an item of a kind which the Secretary of the Treasury specifies by regulations as increasing the energy efficiency of the dwelling.

The House bill applies to taxable years ending on or after April 20, 1977, for expenditures made on or after that date and before January 1, 1985.

Senate amendment

The Senate amendment is generally the same as the House bill except in the following material respects: (1) the credit would be refundable; (2) the termination date of the credit would be one year

later than the House bill (December 31, 1985); (3) individuals whose residences are the subjects of weatherization grants under the nontax energy provisions would not be entitled to the credit, (4) the amount of any loan made under the nontax energy provisions would be reduced by the amount of the credit allowed; and (5) additional energy-conserving components qualifying for the credit would include replacement furnaces, automatic energy-saving thermostats (as well as the clock thermostats included in the House bill), heat pumps, energy usage display meters, replacement fluorescent light systems, evaporative cooling devices, hydrogen-fueled residential equipment, and wood or peat-fueled residential equipment.

Conference agreement

The conference agreement follows the House bill with the following changes. First, the credit is to be 15 percent of the first $2,000 of qualifying expenditures, for a maximum credit of $300. Second, the credit is to be available for expenditures made on or after April 20, 1977, and before January 1, 1986. Third, a credit carryover is provided to the extent that the credit exceeds the taxpayer's tax liability; the carryover is to extend for two years beyond the termination date of the credit, i.e., through taxable years ending before January 1, 1988. Fourth, a credit relating to qualifying expenditures made during 1977 is to be claimed (along with any credit relating to 1978 qualifying expenditures) only on the taxpayer's 1978 tax return and, subject to the carryover provision, only against the taxpayer's 1978 tax liability. Fifth, the credit would be available for automatic energy-saving thermostats (as well as clock thermostats) and energy usage display meters. Sixth, the credit is applicable to replacement burners on either oil-fired furnaces or boilers.

2. Residential Renewable Energy Source Equipment Credit

House bill

Under present law, no special tax credit or deduction is allowed for solar, wind, or geothermal energy equipment installed in connection with a residence.

The House bill provides a nonrefundable income tax credit for qualifying solar and wind energy equipment expenditures for installations in connection with the principal residence of the taxpayer. The credit would be 30 percent of the first $1,500 of qualifying expenditures and 20 percent of the next $8,500 of qualifying expenditures, for a maximum credit of $2,150. The credit would be applied against the taxpayer's tax liability, and no carryover would be provided to the extent it exceeds the amount of tax liability.

The credit would be available with respect to existing, newly constructed and reconstructed principal residences. Owners and renters would be eligible for the credit; moreover, an individual who owns stock in a cooperative housing association or who is a member of a condominium management association would be eligible for the credit.

The House bill applies to taxable years ending on or after April 20, 1977, for expenditures made on or after that date and before January 1, 1985.

Senate amendment

The Senate amendment is generally the same as the House bill except in the following material respects: (1) the credit would be refundable; (2) the credit would be 30 percent of the first $2,000 and 20 percent for the next $8,000 of qualifying expenditures, for a maximum credit of $2,200; (3) the termination date of the credit would be one year later than the House bill (December 31, 1985); (4) the amount of any loan made under the nontax energy provisions would be reduced by the amount of the credit allowed; (5) the credit would apply to "passive" as well as "active" solar systems;[1] (6) the credit would apply to leased (as well as purchased) solar energy equipment; (7) the credit would apply to equipment using solar energy in the production ot electricity; (8) the credit wou d apply to equipment using wind energy for transportation (as well as residential) purposes; (9) the credit would apply to equipment using geothermal energy; (10) the Secretary of Treasury, under regulations, may add to the list of qualifying property equipment items which rely on "renewable energy resources;" and (11) in determining whether an item is eligible for the credit, onsite inspections which are not already authorized in the assessment and collection of income taxes would be prohibited unless the resident claiming the credit consents to the inspection.

Conference agreement

The conference agreement follows the Senate amendment, deleting, however, items (1), (4), (6), (7), (8) and (11) listed above under the Senate amendment section. In addition, certain other changes are made. First, the credit is to be nonrefundable, and, instead, a credit carryover is provided to the extent that the credit exceeds the taxpayer's tax liability; the carryover is to extend for two years beyond the termination date of the credit, i.e., through taxable years ending before January 1, 1988. Second, a credit relating to qualifying expenditures made during 1977 is to be claimed (along with any credit relating to 1978 qualifying expenditures) only on the taxpayer's 1978 tax return and, subject to the carryover provision, only against the taxpayer's 1978 tax liability.

[1] An "active solar system" is based on the use of mechanically forced energy transfer, such as the use of fans to circulate solar generated energy. "Passive solar systems" are based on the use of conductive, convective, or radiant energy transfer, such as the use of portions of a residential structure which serve as solar furnaces so as to add heat to the residence. However, expenditures for labor, materials and components which will serve a significant structural function in the dwelling (e.g., extra-thick walls) would not be eligible for the credit.

B. TRANSPORTATION TAX PROVISIONS

3. Gas Guzzler Tax and Use of Proceeds

House bill

A gas guzzler tax would be imposed on a manufacturer on the sale or initial lease of automobiles whose fuel economy fails to meet certain fuel efficiency standards. The fuel efficiency standards below which an automobile will be taxed would generally start from 3 to 5.5 miles (depending on the year involved) below the fleetwide average standards of the Energy Production and Conservation Act ("EPCA").

The tax would apply to 1979 and later model year automobiles weighing 6,000 pounds or less. The tax would not apply to trucks with a cargo capacity of 1,000 pounds or more or to vehicles which are equipped with 4-wheel drive and other significant features designed to equip them for off-highway operation.

Tax rates range from $339 to $553 in 1979, $245 to $1,216 in 1981, $345 to $2,134 in 1983, $371 to $2,638 in 1984, and $397 to $3,856 in 1985 and later years.

The exemption from the manufacturers excise taxes generally provided for State and local governments and nonprofit educational institutions would not be available in the case of the gas guzzler tax. Also, the Secretary of the Treasury would not have the authority to waive the gas guzzler tax in the case of sales or leases to the United States.

Purchasers of vehicles subject to the tax would have to reduce the basis of the vehicles by the amount of the tax.

Proceeds of the gas guzzler tax would be placed in a trust fund to be used for the purpose of reducing the national debt.

Senate amendment

No provision.

Conference agreement

The conference agreement generally follows the House bill with several modifications.

First, under the conference agreement, no tax is imposed on 1979 model year automobiles. Second, the mileage standards, and generally the tax rates, applicable to each model year from 1979 through 1985 are deferred one year under the conference agreement. Thus, the mileage standards which the House bill would apply to model year 1979 are applied to model year 1980; the standards that the House bill would apply to model year 1980 are applied to model year 1981, etc. Beginning with model year 1983, the fuel efficiency standards below which a passenger automobile will be subject to tax are reduced one mile per gallon. Under the conference agreement, the fuel efficiency standards below which a passenger automobile will be subject to tax will generally start from 4 to 6.5 miles per gallon (depending on the year involved) below the fleetwide average standards of EPCA.

The rates of tax are rounded to the nearest $50, and the lowest two rates of tax for the 1980 model year and the lowest rate of tax for the 1981 and 1982 model years are reduced. Thus, the tax rates for model year 1980 passenger automobiles would range from $200 (for a passenger automobile with a mileage rating of at least 14, but less than 15, miles per gallon) to $550 (for a passenger automobile with a mileage rating of less than 13 miles per gallon). For the 1986 model year and later model years, the tax rates would range from $500 (for a passenger automobile with a mileage rating of at least 22.5, but less than 23.5, miles per gallon) to $3,850 (for a passenger automobile with a mileage rating of less than 12.5 miles per gallon).

The conference agreement also narrows the group of vehicles which are subject to the tax. As under the House bill, the automobiles to which this tax applies generally include any 4-wheeled vehicle propelled by fuel (1) which is manufactured primarily for use on public streets, roads and highways (except any vehicle operated exclusively on a rail or rails), and (2) which is rated at no more than 6,000 pounds gross vehicle weight.

However, the conference agreement excludes from the application of the tax any vehicle which is treated as a nonpassenger automobile under the rules which were prescribed by the Secretary of Transportation for purposes of section 501 of the Motor Vehicle Information and Cost Savings Act (15 U.S.C. 2001) and which were in effect on the date of the enactment of this provision.[1] Thus, even if these rules are later changed, a vehicle which is described as a nonpassenger automobile under the rules currently in effect would not be subject to the gas guzzler tax. Also, as in the House bill, vehicles which are equipped with 4-wheel drive and other significant features designed to equip them for off-highway operation would not be subject to the gas guzzler tax.

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[1] These rules provide as follows:

§ 523.5 Nonpassenger automobile.

(a) A nonpassenger automobile is an automobile either designed for off-highway operation, as described in paragraph (b) of this section, or designed to perform at least one of the following functions:

(1) Transport more than 10 persons;

(2) Provide temporary living quarters;

(3) Transport property on an open bed;

(4) Provide greater cargo-carrying than passenger-carrying volume; or

(5) Permit expanded use of the automobile for cargo-carrying purposes or other nonpassenger-carrying purposes through the removal of seats by means installed for that purpose by the automobile's manufacturer or with simple tools, such as screwdrivers and wrenches, so as to create a flat, floor level surface extending from the forwardmost point of installation of those seats to the rear of the automobile's interior.

(b) An automobile capable of off-highway operation is an automobile—

(1) (i) That has 4-wheel drive; or

(ii) Is rated at more than 6,000 pounds gross vehicle weight; and

(2) That has at least four of the following characteristics (see Figure 1) calculated when the automobile is at curb weight, on a level surface, with the front wheels parallel to the automobile's longitudinal centerline, and the tires inflated to the manufacturer's recommended pressure—

(i) Approach angle of not less than 28 degrees.

(ii) Breakover angle of not less than 14 degrees.

(iii) Departure angle of not less than 20 degrees.

(iv) Running clearance of not less than 8 inches.

(v) Front and rear axle clearances of not less than 7 inches each.

(49 C.F.R. § 523.5.)

Another modification exempts emergency vehicles from the gas guzzler tax. This exemption covers any vehicles sold for use and used (1) as an ambulance or combinat on ambulance-hearse, (2) by the United States or by a State or local government for police or other law enforcement purposes, or (3) for other emergency uses prescribed by the Treasury Department by regulations. The first category of this exception, which applies to ambulances and combination ambulance-hearses regardless of ownership, does not include vehicles used solely as hearses (since they do not require acceleration for emergency use). The second category exempts vehicles used by the United States or by a State or local government for police or other law enforcement purposes. It does not include vehicles used by private law enforcement organizations. The third category, which exempts vehicles used for other emergency uses prescribed by Treasury Department regulations, is intended to give the Treasury Department the discretion to add vehicles used for emergency purposes. This could include, for example, vehicles used by the chief of a fire department if substantially all of the use of the vehicle is for fire department purposes. In promulgating regulations under this provision, the Treasury Department is intended to have the discretion to make distinctions based on ownership of the vehicle and the amount of use for emergency purposes, as well as on the nature of the purposes.

Another modification of the House bill provides special rules foı small manufacturers. These rules, which are generally patterned on the special rules for small manufacturers in EPCA, provide that a small manufacturer (that is, a manufacturer of less than 10,000 automobiles per year) may apply to the Secretary of the Treasury for special treatment with respect to all of the automobiles manufactured by the manufacturer during a model year (or with respect to a model type). The term "manufacturer" for this purpose does not include an importer; however, a manufacturer who manufactures some or all vehicles abroad is eligible to apply for this treatment.

If the Secretary determines that it is not feasible for the manufacturer to meet the tax-free fuel economy level for the model year with respect to all of its automobiles, or a particular model type, the Secretary can provide by regulation an alternate rate schedule for such model year automobiles or model type. The alternate rate schedule, which is to be determined by the Secretary only after consultation with the Secretary of Energy, the Secretary of Transportation, and other appropriate Federal officers, is to be based on the maximum fuel economy level which the manufacturer can meet for the model year for all the manufacturers automobiles or a particular model type, as the case may be. In determining an alternate rate schedule, the Secretary may vary the rates of tax, the mileage standards, or both.

The conference agreement omits the House bill provision which would require placement of the gas guzzler tax proceeds in a trust fund to be used for the purpose of reducing the national debt.

4. Repeal of Personal Deduction for State and Local Taxes on Gasoline

House bill

The House bill repeals the deduction for State and local taxes imposed with respect to gasoline, diesel fuel, and other motor fuels which

are purchased by a taxpayer for nonbusiness use after December 31, 1977.

Senate amendment

No provision.

Conference agreement

The conference agreement does not include this provision.

5. Extension of Current Rate of Federal Taxes on Gasoline and Other Motor Fuels

House bill

Under present law, a retailers excise tax of 4 cents a gallon is imposed on diesel and other special motor fuels sold for use (or used) in a highway vehicle. Also, a manufacturers excise tax of 4 cents a gallon is imposed on gasoline sold by the producer or importer. These taxes are scheduled to be reduced to 1½ cents a gallon on October 1, 1979 (as the Highway Trust Fund—to which the revenues now go—is scheduled to expire as of September 30, 1979).

The bill extends the current 4-cents-a-gallon excise taxes on gasoline, diesel fuel, and other motor fuel (which are scheduled to drop to 1½ cents per gallon on October 1, 1979) for 6 years—that is until September 30, 1985.

Senate amendment

The Senate amendment contains a provision which is the same as this provision in the House bill.

Conference agreement

The conference agreement does not include these provisions of both the House bill and the Senate amendment because the excise taxes on gasoline and other motor fuels would be extended by other legislation (H.R. 11733) which has been approved by both the House and the Senate. This other legislation also deals with extension of the Highway Trust Fund and of the current rates of other highway-related excise taxes.

6. Exemption From Motor Fuels Excise Taxes for Certain Alcohol Fuels

House bill

No provision.

Senate amendment

Gasohol (i.e., fuel which is a blend of gasoline, or other motor fuel, and alcohol) that is at least 10 percent alcohol (including ethanol, methanol or other alcohol) made from agricultural or forestry products would be exempted from the Federal excise taxes on motor fuels on or after January 1, 1978, and before October 1, 1985.

Gasohol that is at least 10 percent alcohol made from other products (such as urban wastes), but not from petroleum, natural gas, or coal, is also exempted from the Federal excise taxes on fuels for this period. The Secretary of Energy is directed to make annual reports to Congress from 1979 through 1985 on the use of alcohol in fuels.

Also, the Secretary is directed to expedite the applications for permits to distill ethanol for use in the production of gasohol and to report

to the Senate Finance Committee and the House Ways and Means Committee on a simplified manner of regulating the distilling operations of gasohol producers who distill ethanol.

Conference agreement

The conference agreement generally follows the Senate bill; however, under the conference agreement, the exemption would apply only to sales of fuel after December 31, 1978, and before October 1, 1984,[1] and the Secretary of Energy is directed to make annual reports on the use of alcohol in fuels only from 1980 through 1984.

7. Exemption From Agricultural Set Aside Requirements for Acreage Used for Commodities for Production of Alcohol Fuels

House bill

No provision.

Senate amendment

The amendment authorizes the Secretary of Agriculture to use any set-aside acreage (that is, acreage that would otherwise be withheld from production) for the production of any agricultural or forestry product that is to be used or sold for primary use in the manufacture of alcohol fuels.

Conference agreement

The conference agreement does not include this provision of the Senate amendment. However, it is the intent of the conferees that, in determining the need for acreage set-aside programs for particular commodities and the extent of the acreage set-aside programs (under sections 105A and 107A of the Agricultural Act of 1949, as added by sections 402 and 502 of the Food and Agriculture Act of 1977), the Secretary of Agriculture take into account the demand for these commodities by producers of alcohol fuels (including fuels which consist of gasoline-alcohol blends) and other fuels.

Reducing the amount of acreage set aside for purposes of the set-aside program by the amount of acreage needed to provide commodities for use in alcohol fuels and other fuels will have the same general effect as allowing set-aside acreage to be used to provide raw materials for alcohol fuels—it will allow the use of "surplus" agricultural land to produce fuel crops. In addition, this approach will alleviate the need to trace production from set-aside acreage to use in alcohol fuels.

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[1] The conference agreement follows the Senate bill in providing that, if a mixture of gasoline and alcohol has been sold tax-free by the producer under the provisions added by this section and if a person later separates the gasoline from the mixture of gasoline and alcohol, such person shall be treated as the producer of the gasoline. Generally, such treatment means that a tax would be imposed on the sale or use by the producer of such separated gasoline. Similarly, if a mixture of special motor fuel and alcohol has bene sold tax-free (under new sec. 4041(k) and a person later separates the special motor fuel from the mixture of special motor fuel and alcohol, the separation will be treated as a sale of the special motor fuel which will be subject to the normal rules relating to the imposition of tax on such motor fuels (sec. 4041(b)). These provisions will apply to any separation of the gasoline (or special motor fuel from the mixture of gasoline (or other motor fuel) and alcohol regardless of the manner in which the separation is accomplished.

Since the conferees understand that the Secretary of Agriculture is required to take into account all sources of demand for agricultural commodities in determining the need for, and the extent of, set-aside programs for agricultural commodities, no statutory changes appear necessary to achieve the result intended by the conferees.

8. Removal of Refund or Credit for Excise Taxes on Motor Fuels and Lubricating Oil for Nonbusiness, Offhighway Uses

House bill

As of October 1, 1977, the current law 2-cent reduction (or credit or refund) of the Federal excise taxes on gasoline or special motor fuels used for nonhighway purposes would not be available if the gasoline or special motor fuel is used in a motorboat.

Senate amendment

As of January 1, 1978, the Senate amendment repeals the 2-cents-a-gallon reduction (through refund, credit, or exemption) of the excise taxes on gasoline and special motor fuels, and the refund (or credit) of the 6-cents-a-gallon tax on lubricating oil, with respect to gasoline, special fuels, and lubricating oil used (1) for nonbusiness, off-highway purposes (such as lawnmowers, snowmobiles, etc.) and (2) in motorboats (whether or not such use is business use).

However, the 2-cents-a-gallon reduction in the tax on gasoline is to continue to apply to gasoline used in a commercial fishing vessel for business use.

Conference agreement

The conference agreement generally follows the Senate amendment, but the provisions apply only to fuels used after December 31, 1978.

However, the provision relating to the availability of the 2-cents-a-gallon refund of the gasoline tax for commercial fishing vessels is replaced by appropriate cross references to 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 (sec. 4041(g)(1) and sec. 4221 (a)(3) and (d)(3)). 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 used as supplies for such vessels (sec. 6416(a) and (b)(2)(B)). The Internal Revenue Service has ruled that fishing vessels are employed in the fisheries or whaling business when used (1) exclusively for the purpose of catching shrimp and other types of aquatic life for sale commercially as bait or (2) on specific trips exclusively for catching fish all of which are to be sold commercially (Rev. Rul. 65–134, 1965–1 C.B. 492). These cross references make it clear that no change is intended with respect to these exemptions for commercial fishing vessels.

9. Repeal of Excise Tax on Buses

House bill

The House bill would repeal the 10-percent manufacturers excise tax imposed on the sale of buses having a gross vehicle weight of more than 10,000 pounds effective for sales on or after April 20, 1977.

Senate amendment

The Senate amendment contains a provision which is identical to this provision in the House bill.

Conference agreement

The conference agreement follows this provision of the House bill and the Senate amendment.

10. Repeal of Excise Tax on Bus Parts

House bill

The House bill would repeal the 8-percent manufacturers excise tax on bus parts and accessories for sales on or after the first day of the first calendar month beginning more than 10 days after the date of enactment.

Senate amendment

The Senate amendment contains a provision which is the same as this provision in the House bill.

Conference agreement

The conference agreement follows this provision of the House bill and the Senate amendment.

11. Removal of Excise Tax on Certain Items Used on or in Connection With Intercity, Local, or School Buses

House bill

Presently, privately owned and operated buses are subject to the manufacturers excise taxes on tires, tubes, tread rubber, gasoline, and lubricating oil, as well as the retailers excise taxes on diesel fuel and other special motor fuels. Complete exemption is provided from these excise taxes for State and local governments and for tax-exempt educational organizations. A partial exemption (2-cents-a-gallon refund or credit) is available from the tax on gasoline and other motor fuels for use by a privately owned local transit system for the portion of its total fare revenue represented by "commuter fare revenue."

The House bill 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, effective on the first day of the first calendar month which begins more than 10 days after the date of enactment.

Senate amendment

The Senate amendment contains provisions which are the same as the provisions of the House bill.

Conference agreement

The conference agreement follows the provisions of the House bill and the Senate amendment.

12. Tax Credit for Certain Commuter Vehicles

House bill

No provision.

Senate amendment

Under the Senate amendment, if an employer purchases a new van with a useful life of at least 3 years, seating nine or more persons (including the driver), and substantially all the use of the van is for transporting employees to and from work, the employer is entitled to the full 10-percent investment credit and the additional 10-percent business energy investment credit. These credits are available for vehicles purchased after April 19, 1977 and before January 1, 1986 and placed in service by the taxpayer before January 1, 1986.

Conference agreement

The conference agreement generally follows the Senate bill in allowing the full 10-percent investment tax credit for certain vehicles used in van pooling, but it does not allow the additional 10-percent business energy credit for any of these vehicles. The full credit would apply only to vehicles acquired by the taxpayer after the date of enactment and placed in service prior to January 1, 1986.

Several changes are made in the definition of eligible vehicles. The eligible vehicles are redesignated as "commuter highway vehicles," the passenger seating capacity of which is at least 8 adults (not including the driver) and at least 80 percent of the mileage use of which is for vanpooling. Generally, use for vanpooling means use for the purpose of transporting the taxpayer's employees between their residences and their places of employment on trips during which the number of employees transported for this purpose is at least one-half of the adult seating capacity of the vehicle (not including the driver). The mileage use which qualifies as vanpooling use includes not only mileage travelled on trips which transport the required number of employees, but also use which is incident to such trips (such as "deadheading").

This revised definition is intended (*inter alia*) to make it clear that a bus, as well as a van, may qualify for the full investment credit under this provision.

In determining whether employees are transported from their homes to their places of employment, it is not necessary that the employees be picked up at, and transported to, their homes. It is sufficient to meet this requirement if the employees are transported to and from some central pickup point (or points) or intermediate location between the employees' residences and places of employment.

Under the normal investment credit rules, as applied to this provision, the credit will be recaptured if the commuter highway vehicle is disposed of within 3 years after it is placed in service. The conference agreement adds a recapture rule which provides, in effect, that recapture will occur if the full investment credit is claimed under this provision with respect to a vehicle, and within the first 36 months of the operation of the vehicle, the vehicle ceases to be a commuter highway vehicle. In applying the 80 percent of mileage use test to determine whether a vehicle ceases to be a commuter highway vehicle, the test shall be applied on the basis of the entire portion of the 36 month period which falls within the taxable year. If recapture results from a change in use from vanpooling to other business use, the amount of credit which will be recaptured will be two-thirds of the investment credit claimed (assuming the vehicle has a useful life of 3 or 4 years).

If recapture results from a change from a vanpooling use to a personal use, the entire amount of the investment credit will be recaptured.

13. Exclusion From Income of Certain Employer-Furnished Transportation

House bill

No provision.

Senate amendment

In the case of a taxpayer who is an employee, gross income would not include the value in excess of the employee's cost of transportation to or from work furnished by an employer if such transportation is in a communter van.

This provision applies to transportation furnished after January 1, 1977, and before January 1, 1986. (No inference is intended concerning the taxability of transportation furnished during other periods.)

Conference agreement

The conference agreement generally follows the Senate amendment. However, certain changes are made concerning the transportation to which this provision applies.

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 (sec. 401(a)(4)), and (2) the transportation must be by a commuter highway 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).

Furthermore, the exclusion does not apply unless the plan under which the transportation is furnished provides that the value of any transportation is furnished in addition to, and not in lieu of, any compensation otherwise payable to the employee and provides such means of verification as the Secretary of the Treasury prescribes by regulation. Also, the provision does not apply to self-employed individuals (such as partner or proprietors) or former employees even though such individuals or former employees are treated as employees for certain other purposes under section 401(c)(1).

The plan under which transportation must be furnished must be reduced to writing prior to the furnishing of transportation under the plan, except that transportation under the plan will be considered qualified for the exclusion if it is reduced to writing no later than July 1, 1979. Thus, the plan will relate back to transportation furnished for the first half of 1979 if the plan is reduced to writing on or before July 1, 1979. There is no requirement that the plan be submitted to the Internal Revenue Service for prior or subsequent approval.

For years beginning prior to the issuance of final regulations, the employer will have been considered to have met the requirement that the plan provides means of verification as the Secretary prescribes by regulation if the plan provides for means of verification which are reasonable under the circumstances.

The managers wish to make it clear that no inference is intended as to whether gross income includes the value of transportation to and from

work in other situations, such as where the transportation is furnished by a car or limousine. Also, no inference is intended as to the inclusion in income of other types of "fringe benefits."

14. Tax Credit for Electric or Hydrogen Motor Vehicles

House bill

A nonrefundable tax credit (i.e., the credit cannot exceed the taxpayer's tax liability) would be provided for the first $300 of the purchase price of a new 4-wheeled electric motor vehicle (manufactured primarily for use on public roads) purchased by an individual for personal use on or after April 20, 1977, and before January 1, 1983. This credit applies only to new vehicles, not to used vehicles or vehicles converted to electricity.

Senate amendment

Under the Senate amendment, the credit is generally the same as the House bill except that it applies to vehicles purchased on or after April 20, 1977, and before January 1, 1986. However, the credit applies to electric motor vehicles even if they do not have 4 wheels (although they must be manufactured primarily for use on the public roads).

In addition, under the Senate amendment, this credit applies to new motor vehicles powered by hydrogen fuel systems and to the cost of converting gasoline powered vehicles to the use of hydrogen.

Conference agreement

The conference agreement does note the provisions of the House bill and the Senate amendment.

15. Alcohol Fuels Research and Demonstration Project

House bill

No provision.

Senate amendment

The Secretary of Energy is required to select a Federal agency to operate 1 000 of its passenger vehicles on alcohol fuel as a test or demonstration project; 900 of the passenger vehicles would be run on alcohol blended with gasoline, and 100 would operate on straight alcohol. This project is to be operated for a period of up to 3 years, and reports (including economic, technological, and environmental information) are to be made by the Secretary of Energy to Congress for each fiscal year through the fiscal year ending September 30, 1981.

For the fiscal years ending September 30, 1979, September 30, 1980, and September 30, 1981, there are authorized to be appropriated sums not to exceed $3 million in the aggregate for the 3 years as may be needed to carry out this project.

Conference agreement

The conference agreement does not include this provision.

C. CRUDE OIL EQUALIZATION TAX AND REBATES; ENERGY TRUST FUND

16. Crude Oil Equalization Tax

House bill

An excise tax would be imposed on the first purchase (generally by the refiner) of price controlled, domestically produced crude oil. The tax would increase the cost of all crude oil to the world price by 1980. The termination date of the tax would be September 30, 1981.

The tax would be imposed in three stages. In 1978, a tax would be imposed on lower tier oil (old oil under current regulations) equal to one-half of the gap between the ceiling prices of lower tier and upper tier oil for each classification of crude oil. In 1979, the tax would be raised to equal the entire gap. In 1980 and for the duration of the tax, the tax would equal the difference between the wellhead prices of uncontrolled and controlled crude oil of the same classification. As a result, the price of controlled oil plus the tax would be raised to the world price of oil in 1980.

Exemptions from the tax are provided for crude oil used as feedstock to produce natural gas liquids and for crude oil and its products used to extract natural gas or crude oil. Presidential authority is granted to suspend increases in the tax subject to veto by either House.

The crude oil tax is applicable to first purchases of crude oil after December 31, 1977, and before October 1, 1981.

Senate amendment

No provision.

Conference agreement

The conference agreement does not include this provision.

17. Natural Gas Liquids Equalization Tax

House bill

The tax would be imposed in three stages based upon the difference (the price gap) between the controlled price of the liquid and the wholesale price for No. 2 distillate fuel oil in the region, adjusted for differences in Btu content. The tax would equal one-third of the price gap in 1978, two-thirds of the gap in 1979, and equal to the entire gap in 1980 and later years.

The tax would be imposed on the use or sale for use, and the retailer (or user) would be liable for payment of the tax. Exemptions from the tax would be provided for natural gas liquids used in a residence, hospital, church, or school and for agricultural uses.

The natural gas liquids tax is applicable to sales to end users of natural gas liquids after December 31, 1977, and before October 1, 1981.

Senate amendment

No provision.

Conference agreement

The conference agreement does not include this provision.

18. Heating Oil Refund and Other Home Heating Tax Credits

House bill

The House bill provides a refund of the crude oil equalization tax to the retailer of heating oil for oil used in a residence, hospital, church, or school if the retailer passes on the refund to the user. The heating oil refund is effective for sales after December 31, 1977, and before October 1, 1981.

Senate amendment

The Senate amendment provides a refundable income tax credit equal to 25 percent of the initial $600 of expenditures on home heating oil and propane, phased out as adjusted gross income rises from $15,000 to $30,000. The amendment also provides a refundable tax credit up to $150 for the increase in home electric heating and cooling costs from one year to the next to the extent they result from increased prices for imported residual fuel oil, phased out as adjusted gross income rises from $15,000 to $30,000.

The heating oil credit is effective for taxable years beginning after December 31, 1977, and ending before January 1, 1983. The electric heating and cooling credit is effective for taxable years ending after December 31, 1977.

Conference agreement

The conference agreement does not include either the House or Senate provision.

19. Equalization Tax Rebates

House bill

The House bill rebates net proceeds from the crude oil equalization taxes for 1978 only. The rebate is a fixed amount per taxpayer, with a double rebate for single heads of households. (It is estimated to be $22 per taxpayer.) The rebate, generally, would be provided as a nonrefundable tax credit for all taxpayers. Those persons who do not receive a credit for income tax purposes would receive a direct payment as part of their regular social security, SSI, railroad retirement or AFDC payments. Persons not receiving their rebate under these methods could file a claim with the Treasury (called the "roundup payment").

Senate amendment

The Senate amendment provides generally that no new tax should be imposed under the bill unless the bill also provides adequate tax incentives for increased production and conservation of energy and for conversion to alternate sources of energy, and also contains tax mechanisms for mitigating undesirable consequences arising out of the energy crisis.

Conference agreement

The conference agreement does not include any rebate provision.

20. Energy Cost Credit for the Elderly

House bill

No provision.

Senate amendment

The Senate amendment provides a refundable tax credit of $75 for any taxpayer who maintains a household which includes someone age 65 or over, phased out between adjusted gross incomes of $7,500 and $12,500. The elderly credit would be effective for taxable years beginning after December 31, 1977, and ending before January 1, 1986.

Conference agreement

The conference agreement does not include this provision.

21. Small Refiners Study

House bill

The House bill provides that the Treasury Department will make a study of the effect of the imposition of the crude oil equalization tax and the entitlements program on small refiners. The results of the study are to be given to Congress within 90 days of enactment.

Senate amendment

No provision.

Conference agreement

The conference agreement does not include this provision.

22. Oil Pricing Amendments for Stripper Wells

House bill

No provision.

Senate amendment

Under present law oil from stripper wells is exempt from price controls. Stripper wells are those from properties on which the average daily production per well is less than 10 barrels. The definition of stripper oil is amended to include water and other injection wells in computing the average daily production per well.

Conference agreement

The conference agreement does not include this provision.

23. Energy Production, Conservation, and Conversion Trust Fund

House bill

No provision.

Senate amendment

The Senate amendment establishes an Energy Production, Conservation, and Conversion Trust Fund. It appropriates to the Trust Fund a portion of the net revenues not refunded to consumers and not otherwise rebated, from any new taxes (not including extended existing taxes) added by the bill as enacted. The Trust Fund consists

of two separately managed and administered accounts: (1) the Energy Financing Program Account, to encourage conservation of energy, conversion to energy sources other than oil and gas and domestic production of energy (other than conventional production of oil and natural gas), and (2) the Energy-Efficient Transportation Account, to encourage energy-efficient forms of transportation. Any expenditures from either Trust Fund account would require authorization and appropriation acts.

Conference agreement

The conference agreement does not include this provision.

24. Payments to States

House bill

No provision.

Senate amendment

If there is a crude oil equalization tax, the Senate amendment authorizes an appropriation of up to $400 million in each of the fiscal years 1978, 1979, 1980 and 1981 for payments to States for repair of Federal-aid highways.

Conference agreement

The conference agreement does not include this provision.

D. TAX ON BUSINESS USE OF OIL AND NATURAL GAS; CREDITS AGAINST THE TAX

25. Excise Tax on Business Use of Oil and Gas and Credits Against Oil and Gas Use Tax

House bill

A tax would be imposed on the use of oil and natural gas as fuel in a trade or business. Three levels of tax would be imposed: Tier 1 would generally apply to process uses, Tier 2 would apply to boilers, turbines, and other internal combustion engines, and Tier 3 would apply to electric utilities, industrial cogenerators, and industrial producers of electricity using boilers with a total rating of at least 100 megawatts per plant.

The tax on Tier 1 oil would start at $.30 per barrel in 1979 and would rise gradually to $1.00 per barrel for use in 1981 and thereafter. The tax on Tier 2 oil would start at $.30 per barrel and would rise gradually to $3.00 per barrel for use in 1985 and thereafter. Tier 3 oil would be exempt through 1982 and would be taxed at $1.50 per barrel in 1983 and thereafter. Beginning in 1981, the tax rates would be adjusted annually for inflation that occurs after 1979.

With respect to the industrial use of natural gas in Tier 1 and Tier 2 categories, the tax would be determined on a variable tax basis by subtracting a cost differential, which would be reduced annually from $1.35 to $.30 for Tier 1 and from $1.05 to zero for Tier 2 by 1985, from the user acquisition price per million Btu of gas from the natural gas target price per million Btu for the region in which the gas is used. The basis for determining the natural gas target price is the average regional price of all No. 2 grade distillate oil sold during the preceding calendar year in the region, adjusted for differences in energy (Btu) content between such oil and natural gas.

Tier 3 gas would be exempt through 1982 and would be taxed at $.55 per million Btu in 1983. The rate would rise gradually to $.75 for use in 1985 and thereafter. The tax would not exceed the amount necessary to make the firm's cost of gas (including the tax) equal to the cost of residual oil (including the tax) in the region where the gas is used.

The following uses of oil and gas would be exempt from the tax:

(1) Industrial process use would be exempt from the tax when the use of fuels other than oil or natural gas would materially and adversely affect the manufacturing process or the quality of the manufactured goods, or when the use of such alternate fuels would not be economically and environmentally feasible.

(2) An exemption from the tax would be provided to nonindustrial uses of oil and natural gas in residential facilities, in transportation (including pipelines), on a farm for farming purposes, in nonmanufacturing commercial buildings, and in the exploration, development and production of crude oil and natural gas.

(3) Oil and natural gas would be exempt from taxation if used in a facility that was in existence or under construction on April 20, 1977, and which is precluded from using coal by State air pollution regulations in effect on that date or by Federal air pollution regulations. State regulations in effect after that date would also be grounds for exemption if such regulations were necessary to meet a requirement of Federal law. A regulation of a local agency having jurisdiction over a facility under an approved State Implementation Plan also would be the basis for an exemption.

In addition to oil or natural gas employed in exempt uses, firms would also be able to exempt from taxation the Btu content of 50,000 barrels of oil per year (i.e., 300 billion Btu). In cases of a regional competitive disadvantage, the Secretary of the Treasury may provide additional exempt amounts for individual plants, and he is required to publish the identification of taxpayers and plants which receive additions to their exempt amounts.

The Secretary of the Treasury would establish a procedure for reclassifying uses to a category which is taxed at a lower rate or which is exempt from tax. Reclassification would depend on the extent to which reduction in oil and natural gas use could be achieved as a result of the tax.

The President could suspend the tax for a period up to one year, if he believes it would have an adverse economic effect. A suspension plan would have to be submitted to Congress, and it would be subject to a veto by either House before the end of 15 days.

A taxpayer could elect a credit against the use tax of $1 for each dollar of qualified investment, up to 100 percent of the taxpayer's oil and natural gas use taxes, made after April 20, 1977. If the amount of investment is in excess of the amount of use taxes for the year, a carryforward is permitted against use taxes in future years and a carryforward to 1981 is provided for use taxes incurred in 1979 and 1980.

Utilities would be allowed to carry forward qualifying investment expenditures for offset against use tax liabilities that would be incurred beginning in 1983. Utilities would be allowed a credit to the extent that old oil and gas boilers are replaced or phased down for peakload or standby use (1500 hours or less a calendar year).

Where a phased-down old boiler is used between 1500 and 2000 hours in a calendar year, a penalty equal to the use tax would be imposed. Taxes paid in such cases would not be available for offset by qualified investment expenditures. Where old boilers would be used more than 2000 hours in a calendar year, there would be a recapture of credits against tax.

The taxpayer who elected to apply the credit against the user tax would receive the regular investment tax credit on his qualified energy investment expenditures only to the extent that a credit against the use tax was not claimed for the same investment outlay.

The credit would not be available after 1990, except for qualified property on which construction had begun.

Qualified energy investment which could be a credit against the use tax includes the cost of alternative energy property (as defined below in the section on Business Credits) placed in service during the year or, if the taxpayer elects, the progress expenditures made for that property during the year.

Senate amendment

The Senate amendment provides for an excise tax on business use of oil and natural gas in existing coal-capable facilities and in new electric powerplants and major fuel burning installations. The tax would apply only to units capable of consuming at least 100 million Btu/hour or a combination of units at the same site capable of consuming at least 250 million Btu/hour.

The tax rate for oil used in new industrial and utility facilities would be $6.00 per barrel beginning in 1979. For existing installations, the tax would start at $.60 per barrel in 1979 and would rise gradually to $6.00 per barrel for use in 1985 and thereafter. The tax rates would be adjusted for inflation in the same manner as in the House bill.

The tax on industrial and utility use of gas would be the same as the Tier 2 tax in the House bill, except that the target price includes the oil users tax and the target price for gas is the full Btu equivalent for a comparable facility using oil (instead of a phase-in).

In addition to the exempt uses provided in the House bill, the Senate amendment exempts all process uses and the environmental exemption applies to all facilities and takes all State regulations into account. The Senate amendment also provides that any combustor qualifying for an exception or exemption from the requirement of using coal under any law or regulation is exempt from the tax.

The amendment also provides that the Secretary shall grant temporary exceptions for up to five years where alternate fuel transportation, pollution control equipment, or other necessary equipment is not available. In addition, the Secretary is to suspend the tax if he determines that the taxpayer is proceeding as expeditiously as possible to convert from the use of oil or gas.

Use in Hawaii is exempt under the Senate amendment.

The credit against the oil and gas user tax is generally the same as the House bill except that the credit is allowed only for the conversion of existing coal-capable facilities. In addition, the firm is eligible both for the investment credit and the user tax credit, and there are no special rules governing the eligibility of utilities for the credit.

The property which qualifies for the credit is generally the same as the House bill except that it includes equipment to convert an alternate substance to synthetic liquid fuel, but does not include nuclear, geothermal and hydroelectric equipment and does not include equipment for modifying existing boilers so that an alternate substance is at least 25 percent of the fuel.

Conference agreement

The conference agreement does not include this provision.

E. BUSINESS ENERGY TAX CREDITS

26. Additional investment tax credit for alternative energy property

House bill

The bill provides for an additional 10-percent investment credit which is not available to taxpayers who claim credit against the user tax. The credit is limited to 100 percent of tax liability, and this additional credit rate is 5 percent for property financed with tax-exempt industrial development bonds. Utilities will receive the credit for new boilers only to the extent that an existing oil- or gas-fired boiler is phased down to less than 1,500 hours of use per year. The credit is available only to persons engaged in a trade or business, and the credit is recaptured according to the rules for the regular investment credit.

Qualifying property includes equipment which uses a fuel or feedstock other than oil or gas or their products, i.e., an alternate substance. Equipment must be new and must be used in connection with a building or structure located in the United States and is eligible even if considered a structural component or used in connection with lodging facilities.

Alternative energy property includes:

(1) Boilers;

(2) Burners for combustors other than boilers;

(3) Nuclear and hydroelectric power equipment, not including turbines or generators;

(4)(a) Geothermal power equipment, not including turbines or generators;

(b) Geothermal equipment to provide heating, cooling and electricity used in connection with an existing building and an existing commercial or industrial process;

(5) Equipment for producing synthetic gas;

(6)(a) Equipment for modifying existing equipment so that an alternate substance is at least 25 percent of the fuel or feedstock;

(b) Equipment for modifying an existing boiler in an existing electric generating facility so that an alternate substance is at least 25 percent of the fuel; the rate of credit depends on fuel savings percentage;

(7) Pollution control equipment required by Federal, State, and local regulations to be installed in connection with equipment in categories (1), (2), (5), and (6);

(8) Equipment used to handle, store, and prepare an alternate substance, at the point of use as a fuel or feedstock, for use in equipment in categories (1), (2), (3), (4)(a), (5), (6) and (7); facilities to manufacture coke are excluded;

(9) Equipment which uses solar and wind energy to provide heat, cooling or electricity in connection with an existing building and existing industrial or commercial process, and

(10) Plans and designs for equipment in the above categories.

The credit is available for investments after April 19, 1977, and before January 1, 1983.

Senate amendment

The Senate amendment follows the House bill with several modifications. The Senate amendment provides a refundable, additional 15-percent investment tax credit. The credit rate is 7.5 percent for property financed with tax-exempt industrial development bonds. Bioconversion property financed with industrial developments bonds, however, would receive the 15 percent credit. Utilities would receive credit for new boilers only to the extent that an exist ng oil-or gas-fired boiler is phased down to less than 2,000 hours of use per year. The credit is available to persons engaged in a trade or business, to educational, religious, charitable and scientific organizations (tax-exempt under Code sec. 501(c)(3)), to electric utility cooperatives (tax-exempt under Code sec. 501(c)(12)), and to State and local governments. The credit is recaptured if property is disposed or if converted to nonqualifying use before one-half its useful life has elapsed. Investment qualifying for the credit is reduced to the extent that equipment is financed with Federal grants.

Alternative energy property is generally the same as the equipment included in the House bill, except that the equipment must meet performance standards prescribed by the Secretary. The Senate also added the following equipment to the list of eligible property:

(1) Dams, turbines and generators used in hydroelectric power facilities;

(2) Geothermal equipment to produce, distribute, or use geothermal energy but only, in the case of electrical generation, equipment up to the electr cal transmission stage; there is no existing building or industrial process requirement;

(3) Equipment for producing a synthetic gaseous, liquid or solid fuel, for producing chemicals from coal or lignite, and for producing coke or coke gas;

(4) Handling equipment but not equipment used in conjunction with hydroelectric or geothermal equ pment; handling equipment at facilities that process coal into coke or its byproducts would be eligible;

(5) Solar and wind energy equipment installed in connection with a new structure;

(6) Equipment to convert ocean thermal energy or tidal power into useful forms of energy, and

(7) Equipment used in construction of, and in research and development on, electric highway motor vehicles.

These provisions would be effective for investments after April 19, 1977, and before January 1, 1986.

Conference agreement

The conference agreement follows the House bill with the following modifications.

The eligible equipment inncludes the Senate provision of equipment for producing synthetic liquid, gaseous or solid fuel, but not coke or coke gas, and equipment which uses coal (including lignite) as a feed-

stock for the manufacture of chemicals or other products, except coke or coke gas. Geothermal equipment is defined as in the Senate bill.

Hydroelectric and nuclear equipment, structures and dams are excluded.

Solar and wind energy equipment are included, as defined in the Senate amendment, and are eligible for a refundable credit. The definition of solar equipment does not include so-called "passive solar" equipment.

The additional investment credit for alternative energy property is not available to the tax-exempt organizations that were included in the Senate amendment: State and local governments and organizations exempt under sections 501(c)(3) and (12). In addition, the credit is not available to public utility property, as defined in section 46(f)(5): property used predominantly in the trade or business of the furnishing or sale of:

(i) electrical energy, water, or sewage disposal services,

(ii) gas through a local distribution system,

(iii) telephone service, telegraph service by means of domestic telegraph operations or other communication services, or

(iv) steam through a local distribution system or the transportation of gas or steam by pipeline.

The additional credits, except those for solar and wind energy equipment, are not refundable, but may be used to offset 100 percent of tax liability. The rules for applying the limitations based on tax liability to the use of the investment credit in combination with the energy credits provided in the conference agreement will operate under the following stacking order. A taxpayer first will apply the credits attributable to section 38 property (not including the energy credits provided in this agreement) against tax liability to the extent allowed under current law. The first-in-first-out rule of section 46(a) will continue to apply with respect to the stacking of credits within the limitation. Next, a taxpayer will apply the credits attributable to the application of the energy percentage to energy property to the remaining tax liability, up to 100 percent of that tax liability. Finally, if the energy credits exceed tax liability and any of the excess is attributable to solar and wind energy credit, these latter amounts will be treated as an overpayment of tax i.e., as if the amounts were allowed by section 39.

The credits are available for eligible property acquired and placed in service after September 30, 1978, and before January 2, 1983, to the extent of basis attributable to this period.

27. Specially Defined Energy Property Tax Credit

House bill

An additional 10-percent investment credit is provided for this category of energy property. The credit is limited to 50 percent of tax liability. Qualifying property is required to be new depreciable property, with a useful life of at least 3 years, used in connection with a structure located in the United States. All categories of qualifying property must satisfy performance and quality standards prescribed by the Secretary. The recapture rules under the regular investment credit

also apply to this credit. The credit is reduced to 5 percent for property financed by industrial development bonds.

Eligible property includes: (1) a recuperator, (2) a heat wheel, (3) a regenerator, (4) a heat exchanger, (5) a waste heat boiler, (6) a heat pipe, (7) an automatic energy control system, (8) a turbulator, (9) a preheater, (10) a combustible gas recovery system, (11) an economizer, or (12) any other property of a kind specified by the Secretary by regulations, the principal purpose of which is reducing the amount of energy consumed in any existing industrial or commercial process and which is installed in connection with an existing industrial or commercial facility.

The additional credit applies to investments in qualifying property after April 19, 1977, and before January 1, 1983.

Senate amendment

The Senate made available the same 10-percent credit as the House bill, but amended the House bill in several other respects.

The credit is refundable, under the same terms applicable to alternative energy property (No. 27 above).

The list of eligible property was expanded to include industrial heat pumps; energy efficient replacement electric motors; fuel cells, gas turbines and external combustion engines with demonstrated fuel efficiency; fluorescent replacement lighting systems; and silicone controlled rectifier units.

In addition, the Secretary's administrative authority has been extended to equipment that reduces the amount of heat wasted, and equipment in this category of energy property may be installed in connection with utility and agricultural facilities.

This credit applies to investments in qualifying property after April 19, 1977, and before January 1, 1986.

Conference agreement

The conference agreement generally follows the House bill, but the credit may be applied against 100 percent of tax liability as in the Senate amendment. The Secretary is authorized to specify other similar items of energy conservation equipment eligible for this credit, including modifications which are made to existing industrial processes, the principal purpose of which is the reduction in the amount of energy consumed or heat wasted. The conferees expect the Secretary to consult with Department of Energy and the Bureau of Standards in determining additional items to be eligible as specially defined energy property. The credit will be available for qualifying property placed in service after September 30, 1978, and before January 1, 1983, and for qualified expenditures incurred during this period.

28. Energy Property Tax Credit

House bill

The additional nonrefundable 10-percent investment credit is available for two additional types of energy property:

(1) Cogeneration property for the production of steam, heat or other forms of useful energy and also electric energy; and

(2) Recycling equipment which is used exclusively in the recycling of solid waste or to sort and prepare solid waste for recycling.

This credit is limited to 50 percent of tax liability and the additional credit is reduced to 5 percent if the property is financed in whole or in part with industrial development bonds.

The credit applies to qualifying property placed in service after April 19, 1977, and before January 1, 1983.

Senate amendment

Under the Senate amendment, the credit is an additional 10 percent, applicable up to 100 percent of tax liability. Eligible property includes:

(1) Cogeneration property defined as in the House bill plus cogeneration for agricultural purposes, and water purification and desalination.

(2) Recycling equipment defined as in the House bill, but the exclusive use requirement is modified to permit use of up to 10 percent virgin materials; in addition, eligible equipment includes recycling equipment to the point where a marketable product has been produced, e.g., newsprint, paperboard, metal ingots, or textile fibers.

(3) Shale oil equipment which is used to mine, extract or produce oil from oil-bearing shale rock;

(4) Transportation equipment which includes commuter vans and equipment designed to reduce energy consumption when added to existing motor vehicles and commercial carriers;

(5) Equipment used to produce natural gas from geopressured brine;

(6) On-site electrical heat processing equipment which is replacement equipment and which uses electricity produced with an alternate substance; and

(7) Electric motor vehicles, primarily for use on public streets, roads and highways, when purchased for use in a trade or business.

The credit applies to eligible equipment placed in service after April 19, 1977, and before January 1, 1986.

Conference agreement

The conference agreement provides that the additional 10 percent credit will be available to be applied against 100 percent of tax liability. Eligible property includes (1) recycling equipment defined as in the Senate bill, except that in the iron and steel industry, the credit is limited to equipment used before the solid waste is reduced to a molten state, (2) shale oil equipment, as in the Senate amendment, and (3) equipment to produce natural gas from geopressured brine, as in the Senate amendment. For the latter equipment, the rules of the Federal Energy Regulatory Commission will be applied to determine which well qualifies as a well producing natural gas from geopressured brine under the terms of the definition in the Natural Gas Pricing Act, but the Secretary of the Treasury will determine whether the equipment used in connection with that well is eligible for the credit.

The additional credit will be available for eligible equipment acquired or placed in service after September 30, 1978, and before January 1, 1983, and for qualified expenditures in this period.

29. Investment Tax Credit for Business Insulation

House bill

The House bill makes all types of business insulation eligible for the existing investment credit where added to existing buildings. This includes structural insulation, insulation glass, storm doors, weather-

stripping and similar items which satisfy performance and quality standards prescribed by the Secretary.

This credit applies to qualifying property placed in service after April 19, 1977, and before January 1, 1983.

Senate amendment

The Senate amendment is the same as the House bill.

Conference agreement

The conference agreement does not include this provision.

30. Denial of Investment Tax Credit and Accelerated Depreciation for Certain Property

House bill

Oil and natural gas fueled boilers and other combustors would generally be ineligible for the investment tax credit and accelerated methods of depreciation, unless either the use of coal was precluded by air pollution regulations or the taxpayer's use of oil or gas was exempt under the use tax provisions of the bill. Portable air conditioners and space heaters would also be ineligible to receive the investment credit.

This provision applies to property placed in service after June 20, 1977, except for property under a binding contract on that date.

Senate amendment

No provision.

Conference agreement

The conference agreement generally follows the House provision, modified to apply only to portable air conditioners, portable space heaters and boilers fueled by oil or gas. Other combustors fueled by oil or natural gas will not be subject to the investment tax credit and accelerated depreciation denial rules under the conference agreement. In addition, the conference agreement includes the range of exempt uses under the House bill, which generally exempt from the provision those uses which are not part of manufacturing, production or mining. For example, an oil or gas fueled steam and electrical generation facility will be considered an exempt use where the products (such as steam or electricity) of the facility are provided for use by a group of exempt activities (such as a group of offices or hospitals) and the furnishing of electricity is not subject to rate regulation. In addition, the exempt uses are extended to include combined cycle electric plants.

The provision applies to property placed in service after September 30, 1978, except for property for which a binding contract was in effect on that date.

31. Depreciation Allowance for Early Retirement or Replacement of Oil or Gas Boilers

House bill

Special treatment is provided for depreciation of a natural gas or oil-fueled boiler or other combustor which is retired or replaced before the end of its originally determined useful life. The taxpayers will be authorized to redetermine the useful life of an oil or natural gas-fueled combustor and use this shortened useful life to depreciate the

remaining basis in the property (net of any salvage value). If this treatment is elected, the taxpayer may use only the straight-line method for depreciation of the remaining basis. In order to qualify for this treatment, the taxpayer must establish to the satisfaction of the Secretary that there is a reasonable foundation for the conclusion that the combustor will in fact be retired or replaced at the end of the shortened useful life. The taxpayer will be eligible to use this treatment beginning with the taxable year in which the Secretary approves the application of the taxpayer to redetermine the useful life of the combustor under this provision. Recapture of excess depreciation deductions (with interest) is required where the retirement or replacement does not subsequently occur as scheduled.

This provision applies to tax years beginning after the date of enactment.

Senate amendment

No provision.

Conference agreement

The conference agreement follows the House bill.

F. TAX INCENTIVES FOR ALTERNATIVE ENERGY SOURCES

32. Exemption for Interest on IDBs for Coal Gasification and Liquefaction

House bill

No provision.

Senate amendment

Under present law, interest on State or local obligations generally is exempt from Federal tax, except when the obligations are industrial development bonds (i.e., the proceeds are to be used by a non-exempt person). IDBs issued for certain specified purposes are exempt, but coal gasification and liquefaction are not one of the exempt purposes.

Present law provides an exemption for bonds for facilities for the local furnishing of electric energy or gas, but not if the facilities are part of a system furnishing electricity or gas to more than two contiguous counties (or their political equivalents).

The Senate amendment provides that industrial development bonds for the furnishing of coal gasification and liquefaction facilities would be exempt from Federal tax. The exemption would be allowed even if the products of the facilities are furnished to more than two contiguous counties. The provision applies with respect to obligations issued after December 31, 1977.

Conference agreement

The conference agreement does not include this provision.

33. Exemption for Interest on IDBs for Bioconversion Facilities for the Conversion of Wastes into Energy or Fuels

House bill

No provision.

Senate amendment

Under present law, interest on State or local obligations generally is exempt from Federal tax, except when the obligations are industrial development bonds (i.e., the proceeds are to be used by a non-exempt person). IDBs issued for certain specified purposes are exempt, but the conversion of waste into energy generally is not one of the exempt purposes.

In the case of IDBs for sewage or solid waste disposal facilities, an exemption is provided by present law but only if at least 65 percent of the material processed is completely worthless.

Present law also provides an exemption for the local furnishing of electric energy or gas, but not if the facilities are part of a system furnishing electricity or gas to more than two contiguous counties (or their political equivalents).

The Senate amendment provides that interest on industrial development bonds for bioconversion facilities for the donversion of municipal and agricultural wastes and other organic matter into energy or into synthetic gaseous, liquid, or solid fuels would be exempt from Federal tax. The exemption would be allowed even if less than 65 percent of the materials processed are completely worthless, and even if the products of the facilities are furnished to more than two contiguous counties. The provision applies with respect to obligations issued after December 31, 1977.

Conference agreement

The conference agreement does not include this provision.

34. Exemption for Interest on IDBs for Facilities for Local Furnishing of Electricity or Gas

House bill

No provision.

Senate amendment

Under present law, interest on State or local obligations generally is exempt from Federal tax, except when the obligations are industrial development bonds (i.e., the proceeds are to be used by a non-exempt person). IDBs issued for certain specified purposes are exempt.

Present law provides an exemption for bonds for the local furnishing of electric energy or gas, but not if the facilities are part of a system furnishing electricity or gas to more than two contiguous counties (or their political equivalents).

The Senate amendment extends the exemption from Federal tax on interest from industrial development bonds for facilities for the furnishing of electricity or gas to bonds issued by an authorized State agency for facilities to produce electric energy that is consumed in more than two contiguous counties within one State. The provision applies with respect to obligations issued after December 31, 1977.

Conference agreement

The conference agreement does not include this provision.

35. Geothermal Provisions—Depletion for Geothermal Deposits

House bill

Under present law, geothermal resources are ineligible for percentage depletion deductions. However, the Ninth Circuit Court of Appeals has ruled that certain geothermal steam deposits are gas wells and are eligible for percentage depletion as natural gas. The various restrictions on percentage depletion for oil and gas enacted in the Tax Reduction Act of 1975 do not apply to the gas produced from the deposits involved in these court decisions.

The House bill provides a 10-percent deduction for depletion for all resources from geothermal deposits, including natural gas produced from geopressured brine. Under the House bill the amount of percentage depletion deductions allowable with respect to any geothermal property may not exceed the taxpayer's adjusted cost basis in the property.

Senate amendment

The Senate amendment provides percentage depletion for geothermal resources located in the United States or its possessions. It contains a separate rule, described below, for gas produced from geopressured brine.

For geothermal resources, 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. The limitations enacted in 1975 are those which deny percentage depletion to integrated oil companies, limit percentage depletion for any taxpayer to 65 percent of taxable income, and limit percentage depletion to the equivalent of a certain average daily production of oil and gas. However, present law restrictions which apply to percentage depletion for all minerals also apply to percentage depletion for geothermal resources under the Senate amendment. Thus, the Senate amendment provides that depletion in excess of basis is an item of tax preference under the minimum tax, and that 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). Under the Senate amendment there is no basis limitation on the amount of allowable depletion deductions.

Conference agreement

The conference agreement follows the Senate amendment. This section of the conference agreement shall take effect on October 1, 1978, and shall apply to taxable years ending on or after October 1, 1978.

36. Geothermal Provisions—Depletion for Geopressured Natural Gas

House bill

Under present law, natural gas is eligible for percentage depletion at a 22-percent rate. The rate is scheduled to phase down to 15 percent by 1984. Integrated oil and gas producers generally may not claim percentage depletion except for gas sold under pre-1975 fixed price contracts in which the price cannot be adjusted upward to reflect the limitations on percentage depletion enacted in the Tax Reduction Act of 1975. In addition, the amount of oil or gas eligible for percentage depletion for any producer or royalty holder is limited to the equivalent of 1,400 barrels per day in 1978 (scheduled to phase down to 1,000 barrels per day in 1980 and subsequent years). Percentage depletion on oil and gas is limited to 65 percent of taxable income computed without regard to the deduction for depletion. In addition, for any property the allowable percentage depletion deduction is limited to 50 percent of the taxable income from that property computed without regard to the deduction for depletion.

The House bill contains no provision specifically relating to natural gas produced from geopressured brine. Under the House bill, geopressured brine is treated as a geothermal resource.

Senate amendment

The Senate amendment 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 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—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 restrictions on percentage depletion generally. The allowable deduction on any property is to be subject to the limitation that it 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 under the minimum tax.

Under the Senate amendment, the definition of natural gas produced from geopressured brine is to be issued by the Secretary of the Treasury in consultation with the Secretary of Energy.

The Senate amendment is effective for taxable years ending after December 31, 1977.

Conference agreement

The conference agreement generally follows the Senate amendment with the following modifications. The conference agreement provides that the term "natura gas produced from geopressured brine" is to be precisely the same gas 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. The conferees intend that, 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.

Ten-percent depletion for natural gas produced from geopressured brine is to be allowed only for wells drilled 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 conference agreement shall take effect on October 1, 1978, and shall apply to taxable years ending on or after October 1, 1978.

37. Geothermal Provisions—Intangible Drilling Costs: Option to Deduct Drilling Costs

House bill

Under present law, oil and gas producers may elect to deduct intangible drilling costs (IDCs) rather than capitalize them and generally may recover those costs as part of the depletion or depreciation deduction. This election must be made for all of a taxpayer's oil and gas wells.

The House bill extends similar treatment to geothermal wells and provides that a separate election can be made for a taxpayer's geothermal wells, on the one hand, and for his oil and gas wells on the other.

Under the House bill, wells producing natural gas from geopressured brine are treated as geothermal wells, and intangible drilling costs for wells producing natural gas from geopressured brine must be expensed if a taxpayer elects to expense intangible drilling costs for his geothermal wells.

Senate amendment

The Senate amendment is the same as the House bill except that it provides for separate elections for (a) oil and gas wells, (b) geothermal wells, and (c) wells producing natural gas from geopressured brine.

Conference agreement

The conference agreement allows an election to deduct IDCs for geothermal wells. The election is to be separate from that for oil and gas wells. The conference agreement 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 conference agreement does not change the IDC treatment of wells producing natural gas from geopressurized brine, the conferees intend that this provision is not be to construed to be a special tax provision or comparable adjustment under section 107(d) of the Natural Gas Policy Act of 1978.

38. Geothermal Provisions—Intangible Drilling Costs: Application of the Minimum Tax

House bill

Under present law, the deduction for intangible drilling costs on productive wells 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 (excess IDCs) is 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, excess IDCs in excess of oil and gas production income would constitute a tax preference item.

The House bill extends to geothermal properties for all future years a provision similar to the minimum tax provision on intangible drilling costs of individuals which was applicable for 1977. As a result, the item of tax preference will be the amount (if any) by which the amount of excess IDC's on geothermal properties in the taxable year is greater than the amount of the net income of the taxpayer from geothermal properties for the taxable year. Excess IDCs will be the amount of IDCs on productive wells, reduced by the deduction which would have been allowed with respect to those costs through cost depletion. The amount of the net income of the taxpayer from geothermal properties for the taxable year will be the excess of (a) the aggregate amount of gross income (within the meaning of section 613(a)) from all geothermal properties of the taxpayer received or accrued by the taxpayer during the taxable year, over (b) the amount of any deductions allocable to such properties (reduced by the excess IDCs) for such taxable years.

Under the House bill, natural gas produced from geopressured brine is treated as a geothermal resource for purposes of the minimum tax.

This provision applies to wells commenced on or after April 20, 1977, in taxable years ending after that date.

Senate amendment

The Senate amendment is the same as the House bill, except that the intangible drilling costs computation is to be made separately for geothermal resources, natural gas from geopressured brine, and oil and gas wells. Thus, the offset for related income in computing the minimum tax preference is to be made separately for each of the three categories.

Conference agreement

The conference agreement generally follows the House bill. In addition, it continues the present law treatment of wells producing natural gas from geopressured brine as gas wells. Thus, income and deductions from wells producing natural gas from geopressured brine will continue to be aggregated with income and deductions from all oil and gas property for purposes of the related income offset under the minimum tax.

The conference agreement with respect to the application of the minimum tax to intangible drilling costs is the same as the rule applicable to those costs for 1977. Thus, a taxpayer's IDC preference is the amount (if any) 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 cost incurred in drilling a nonproductive well) allowable for the taxable year, over (ii) the amount 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 oil and gas properties for the taxable year is the excess of (i) the aggregated amount of gross income (within the meaning of section 613(a)) from all oil and gas 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 conference agreement shall take effect on October 1, 1978, and shall apply to taxable years ending on or after October 1, 1978.

39. Geothermal Provisions—Intangible Drilling Costs: Recapture

House bill

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 a disposition of an oil and gas property.

The House bill extends present law to geothermal (including geopressured natural gas) properties, and applies it separately from recapture as to oil and gas properties. This provision would apply to wells commenced on or after April 20, 1977, in taxable years ending after that date.

Senate amendment

The Senate amendment is the same as the House bill, except that oil and gas, geothermal, and geopressured natural gas properties would be treated separately.

Conference agreement

The conference agreement essentially follows the House bill in applying recapture to geothermal wells. However, geopressured natural gas wells are to be treated as gas wells as under present law. This section of the conference agreement shall take effect on October 1, 1978, and shall apply to taxable years ending on or after October 1, 1978.

40. Geothermal Provisions—Intangible Drilling Costs: At Risk Limitation

House bill

Under present law, the amount of any loss (otherwise allowable for the year) which may be deducted in connection with exploring for, or exploiting, oil and gas cannot exceed the aggregate amount with respect to which the taxpayer is at risk with regard to the property at the close of the taxable year.

The House bill extends present law to geothermal (including geopressured natural gas) properties, and treats developing those properties as an activity separate from developing oil and gas properties. This provision would apply to wells commenced on or after April 20, 1977, in taxable years ending after that date.

Senate amendment

The Senate amendment is the same as the House bill, except that exploiting and developing oil and gas, geothermal, and geopressured natural gas are treated as separate activities.

Conference agreement

The conference agreement follows the House bill. However, geopressured natural gas is aggregated with oil and gas as one activity. This section of the conference agreement shall take effect on October 1, 1978, and shall apply to taxable years ending on or after October 1, 1978.

41. Percentage Depletion for Peat

House bill

No provision.

Senate amendment

Under present law, peat is allowed 5 percent depletion.

The Senate amendment allows a 10-percent depletion deduction for peat from U.S. deposits which is used as fuel or otherwise to produce energy. (Peat for other purposes is still allowed 5 percent depletion.) This provision applies to taxable years ending after December 31, 1977.

Conference agreement

The conference agreement does not include this provision.

42. Production Credits for Nonconventional Oil and Gas

House bill

No provision.

Senate amendment

Present law contains no provision for production incentives.

The Senate amendment provides nonrefundable income tax credits for production of nonconventional oil and gas in or offshore of the United States or its possessions. The credits are:

(a) $3 per barrel for shale oil;
(b) $3 per barrel for oil from tar sands;
(c) 50 cents per mcf for geopressured natural gas; and
(d) 50 cents for tight rock formation gas.

Credits are allowed according to the ratio of the taxpayer's gross income from the property to total gross income from the property. Credits are reduced on a project-by-project basis according to the ratio between Federal grants for equipment and facilities and total investment in equipment and facilities for nonconventional energy processes. The credits apply for taxable years beginning after December 31, 1977.

Conference agreement

The conference agreement does not include these provisions.

G. LIMITATION OF PRESIDENT'S AUTHORITY TO ADJUST OIL IMPORTS; IMPORT ADJUSTMENT TAX CREDIT

43. Amendments to Trade Expansion Act of 1962

House bill

No provision.

Senate amendment

Under present law, the President may adjust imports of petroleum or petroleum products by quotas or monetary exactions (tariffs, duties, or fees) so that such imports do not threaten national security.

The Senate amendment nullifies the President's authority to adjust imports of petroleum or petroleum products under section 232(b) of the Trade Expansion Act of 1962, except for:

(a) military and defense emergencies involving national security; or

(b) adjustments of imports of refined petroleum products for reasons of national security.

The Senate amendment expressly recognizes the close relation between national security and a U.S. refining industry competitive with foreign refineries. Present law contains no such provision.

The amendment also provides for a 2-House veto of any proposed Presidential adjustment of imports of refined petroleum products under the Trade Expansion Act of 1962 authority within 30 days of the proposal's transmittal to Congress.

The amendment requires the President to establish procedures for refunding all or part of any increased tariff, fees, etc., on imported refined petroleum products to a public utility which demonstrates that it imports such products solely because of the unavailability of domestic supplies (regardless of price) of such product or of alternate domestic fuels or energy sources. Present law has no comparable provision.

Conference agreement

The conference agreement does not include this provision.

44. Amendments to Trade Act of 1974

House bill

No provision.

Senate amendment

Present law allows the President to impose or increase duties on any import pursuant to trade agreements with foreign countries. He also may designate imports from a developing country for duty-free import treatment.

The Senate amendment bars the presidential imposition of, or increase in, import duties on petroleum or petroleum products pursuant to trade agreements with foreign countries under authority granted the

President in Title I of the Trade Act of 1974, and also prohibits the President from designating imported petroleum or petroleum products as eligible articles for duty-free import treatment under Title V of the Trade Act of 1974.

This provision is effective as of the date of enactment.

Conference agreement

The conference agreement does not include this provision.

45. Refined Petroleum Product Import Adjustment Tax Credit

House bill

No provision.

Senate amendment

The Senate amendment provides a refundable tax credit for the cost of purchasing refined petroleum products (both imported and domestic) for use in tax-exempt residences, hospitals, churches and schools.

The amount of credit is determined by multiplying units of such products used by an adjustment amount. The adjustment amount is determined by dividing the net revenues from any increased duty or fee imposed by the President under section 232(f) of the Trade Expansion Act of 1962 on imported refined petroleum products by the number of units used for qualified uses.

Present law contains no comparable provision.

The provision would be effective in taxable years beginning after December 31, 1976.

Conference agreement

The conference agreement does not include this provision.

H. OTHER PROVISIONS

46. Intangible Drilling Cost Deductions for Oil and Gas Wells and the Minimum Tax

House bill

Under present law, the deduction for intangible drilling costs on productive wells 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 (excess IDCs) is treated as a tax preference item for purposes of the minimum tax for individuals.

In the Tax Reduction and Simplification Act of 1977, Congress provided that for taxable years beginning only in 1977, the tax preference would be excess IDCs in excess of oil and gas production income.

The House bill extends for all future years the minimum tax provision on intangible drilling costs of individuals which was applicable for 1977. Thus, with respect to all oil and gas properties of the taxpayer, the tax preference will be the amount (if any) by which the amount of excess IDCs arising in the taxable year is greater than the amount of the net income of the taxpayer from oil and gas properties for the taxable year. The amount of the net income of the taxpayer from oil and gas properties for the taxable year is the excess of (a) the aggregate amount of gross income (within the meaning of section 613(a)) from all oil and gas properties of the taxpayer received or accrued by the taxpayer during the taxable year, over (b) the amount of any deductions allocable to such properties, reduced by excess IDCs, for such taxable year.

These provisions are effective for taxable years ending December 31, 1977.

Senate amendment

The Senate amendment is the same as the House bill.

Conference agreement

The conference agreement follows the House bill and the Senate amendment.

The conference agreement with respect to the application of the minimum tax to intangible drilling costs is the same as the rule applicable to those costs for 1977. Thus, a taxpayer's IDC preference is the amount (if any) 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 cost incurred in drilling a nonproductive well) allowable for the taxable year, over (ii) the amount 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 oil and gas properties for the taxable year is the excess of (i) the aggregated amount of gross income (within the meaning of section 613(a)) from all oil and gas 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.

47. Rerefined Lubricating Oil

House bill

Under present law, a 6-cent-per-gallon manufacturers excise tax is imposed on lubricating oil (other than cutting oils) sold in the United States by a manufacturer or producer, or used anywhere by a manufacturer or producer. The sale of recycled oil is not subject to the tax unless the recycled oil is mixed with new lubricating oil. In such a case, the excise tax is imposed on the portion of the mixture which consists of new lubricating oil.

The House bill exempts the sale of lubricating oil from the 6-cent-per-gallon manufacturers excise tax where the lubricating oil is sold for use in a mixture with 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 with regard to the portion of the new oil that does not exceed 55 percent of the mixture.

The provision is effective for sales on or after the first day of the first calendar month beginning more than 10 days after enactment.

Senate amendment

The Senate amendment is the same as the House bill.

Conference agreement

The conference agreement follows the House bill and the Senate amendment.

48. Annual Report on Energy and Revenue Effects of the Bill

House bill

The House bill requires the President to submit an annual report to the Congress every August after 1977. The report is to provide estimates of the amount of revenue increases or decreases resulting from each energy tax provision, and an evaluation of the extent to which each provision has resulted in increased energy conservation and production. The President is expected to include in his report the petroleum (or natural gas) savings resulting from each provision and the extent of any shifts from petroleum and natural gas to other materials

resulting from each provision. This provision is effective upon enactment.

Senate amendment

The Senate amendment is the same as the House bill.

Conference agreement

The conference agreement does not include this provision.

49. White House Conference on Energy Conservation, and National Energy Conservation Planning and Advisory Council

House bill

No provision.

Senate amendment

The Senate amendment requires the President to convene a White House Conference on Energy to assess problems and make recommendations relating to energy conservation, no later than December 31, 1978.

Conference agreement

The conference agreement does not include this provision.

50. Suspension of Import Duty on Insulation Materials

House bill

No provision.

Senate amendment

The Senate amendment suspends present law import duties on glass fiber, mineral wool and related insulation materials, and boric acid with respect to material entered or withdrawn from warehouse for consumption. The suspension of duty would be effective through June 30, 1979.

Conference agreement

The conference agreement does not include this provision.

51. Energy Stamp Program

House bill

No provision.

Senate amendment

The Senate amendment authorizes annual appropriations of $25 million for each of fiscal years 1978, 1979, and 1980, for five pilot projects to demonstrate an energy-stamp program providing financial assistance to low- and fixed-income households (homeowners or apartment dwellers) for residential energy costs. Participants must pay one-third the value of energy stamps received.

The authorization applies for fiscal years 1978–80.

There is no comparable program in present law.

Conference agreement

The conference agreement does not include this provision.

52. Expedited Consideration of Authorization for U.S. Oil Pipelines From West Coast

House bill

No provision.

Senate amendment

The Senate amendment sets deadlines and otherwise expedites consideration of Federal authorizations for proposed U.S. pipeline systems to carry crude oil supplies inland from the West Coast. The Senate amendment also expedites judicial review of any such authorizations.

This provision is effective upon enactment.

Conference agreement

The conference agreement does not include this provision.

53. Coordination of Effective Dates With the Congressional Budget Act

House bill

No provision.

Senate amendment

The Senate amendment provides that notwithstanding any other provision of the amendment, the Secretary of Treasury is to postpone (but not later than September 30, 1978) any of the effective dates of the amendment to insure that revenues for the fiscal year 1978 will not be less than $397 billion.

Conference agreement

The conference agreement does not include this provision.

54. Sense of the Senate Regarding Revenue Loss From the Bill for Fiscal Year 1978

House bill

No provision.

Senate amendment

The Senate amendment expresses the sense of the Senate that the conferees on the part of the Senate shall, to the extent practical, limit the revenue loss from this amendment to $972 million for the fiscal year 1978.

Conference agreement

The conference agreement does not include this provision.

The Appendix: Budget Effects of Energy Tax Provisions of H.R. 5263 (pages 83-86) has been omitted

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