

**SUMMARY OF REVENUE PROVISIONS  
IN THE PRESIDENT'S  
FISCAL YEAR 1991 BUDGET PROPOSAL**

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PREPARED BY THE STAFF  
OF THE  
JOINT COMMITTEE ON TAXATION



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## INTRODUCTION

This pamphlet,<sup>1</sup> prepared by the staff of the Joint Committee on Taxation, provides a summary of the revenue provisions included in the President's budget proposal for fiscal year 1991, submitted to the Congress on January 29, 1990.<sup>2</sup>

The first part of the pamphlet is a summary of the revenue proposals contained in the President's budget proposal, including present law and a reference to any recent prior Congressional action on the topic and whether the proposal was also included in fiscal year 1989 or 1990 budget proposals.<sup>3</sup> The second part of the pamphlet presents the Administration's (Treasury Department) estimates of the budget effects of the revenue proposals, as they affect budget receipts.

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<sup>1</sup> This pamphlet may be cited as follows: Joint Committee on Taxation, *Summary of Revenue Provisions in the President's Budget Proposal for Fiscal Year 1991* (JCS-3-90), February 5, 1990.

<sup>2</sup> The pamphlet includes those fee proposals in the President's budget proposal that are classified as budget receipts by the Administration's budget documents, *except* for the D.C. contribution to the Civil Service Retirement System, modify Federal Reserve Bank reimbursement, and the delay in the Federal employee pay raise. See Department of the Treasury, *General Explanations of the President's Budget Proposals Affecting Receipts*, January 1990; also *Budget of the United States Government, Fiscal Year 1991*. Neither the inclusion of these fee proposals nor the exclusion of other fee proposals in the budget is intended to create any inference as to the jurisdiction of either the House Committee on Ways and Means or the Senate Committee on Finance with respect to such fee proposals.

<sup>3</sup> *Budget of the United States Government, Fiscal Year 1989; Budget of the United States Government, Fiscal Year 1990*.



## **I. SUMMARY OF PRESIDENT'S REVENUE PROPOSALS**

### **A. Income Tax Provisions**

#### **1. Capital Gains Tax Rate Reduction for Individuals**

##### ***Present Law***

Under present law, net gain from the sale or exchange of capital assets is taxed at the same rates as ordinary income. Individuals with a net capital loss generally may deduct up to \$3,000 of the loss each year against ordinary income. Net capital losses in excess of the \$3,000 limit may be carried forward indefinitely.

##### ***President's Budget Proposal***

The President's budget proposal would allow individuals an exclusion of a percentage of the gain realized upon the disposition of qualified capital assets. Assets held 3 years or more would qualify for a 30-percent exclusion; assets held at least 2 years but less than 3 years would qualify for a 20-percent exclusion; and assets held at least one year but less than 2 years would qualify for a 10-percent exclusion. For a taxpayer in the 28 percent tax bracket, this would result in a regular tax rate of 19.6 percent for assets held 3 years or more, 22.4 percent for assets held between 2 and 3 years and 25.2 percent for assets held between one and 2 years.

Qualified capital assets generally would be capital assets as defined under present law, except that collectibles would be excluded. In addition, all depreciation would be recaptured in full as ordinary income.

The capital gains exclusion would be a preference for purposes of the alternative minimum tax. The amount treated as investment income for purposes of the investment interest limitation would be reduced by the capital gains exclusion attributable to investment assets.

The provision would apply to dispositions (and installment payments received) after the date of enactment. For the portion of 1990 to which the proposal applies, a 30-percent exclusion would apply for all assets held one year or more. For 1991, the exclusion would be 20 percent for assets held between one and 2 years and 30 percent for assets held at least 2 years.

##### ***Prior Action***

The Tax Reform Act of 1986 repealed the prior law exclusion of 60 percent of net long-term capital gains, effective January 1, 1987.

The President's budget proposal for fiscal year 1990 would have reduced the capital gains rate for individuals on qualified assets generally to 15 percent.



The Omnibus Budget Reconciliation Act of 1989 (H.R. 3299) as passed by the House of Representatives would have provided a 19.6-percent maximum regular tax rate on individual capital gains for a temporary period through 1991. That bill would have provided for indexing to account for inflation for certain assets acquired after 1991. These provisions were deleted from the legislation in conference. The identical provisions also passed the House as a separate bill (H.R. 3628).

## 2. Family Savings Accounts

### *Present Law*

Under present law, contributions to savings by an individual generally are not deductible when made and earnings on amounts contributed generally are included in the income of the individual. An exception to these general rules exists with respect to individual retirement accounts (IRAs), as well as certain other types of retirement savings plans. The maximum contribution that may be made to an IRA generally is the lesser of \$2,000 or 100 percent of an individual's compensation. Special rules exist with respect to whether or not the contribution is deductible.

### *President's Budget Proposal*

Under the President's budget proposal, an individual could make nondeductible contributions to a family savings account. If these contributions remain in the account for 7 years or more, amounts withdrawn (including both the contributions and earnings thereon) would be excluded from gross income.

The maximum annual amount that could be contributed by an individual under the proposal would be limited to the lesser of \$2,500 or 100-percent of the individual's compensation. Dependents could not make contributions to the account.

Only individuals meeting certain AGI limitations would be able to make a contribution to a family savings account. Contributions would be permitted for single individuals filing with AGI of less than \$60,000, for heads of households with AGI of less than \$100,000, and for married taxpayers filing joint returns with AGI of less than \$120,000. Amounts contributed to accounts would not affect the amount that could otherwise be contributed to retirement plans (e.g., section 401(k) plans or IRAs) or to other tax-favored forms of saving.

Special rules would apply with respect to withdrawals of earnings allocable to contributions not held in the account for 7 years. If the amount withdrawn constitutes earnings allocable to contributions held less than 3 years, the earnings would be includible in gross income. The individual also would be subject to an additional 10-percent tax on the amount withdrawn. If the amount withdrawn constitutes earnings allocable to amounts held at least 3 years but less than 7 years, the earnings would be includible in gross income, but no additional tax would apply.

The proposal would be effective on January 1, 1990.



### 3. Penalty-Free IRA Withdrawals for First-Time Home Buyers

#### *Present Law*

Under present law, withdrawals from an individual retirement account (IRA) (other than withdrawals of nondeductible contributions) are includible in gross income. In addition, amounts withdrawn prior to age 59½, death, or disability are subject to an additional 10-percent income tax, unless the distribution is in the form of periodic payments.

#### *President's Budget Proposal*

The President's budget proposal would allow certain individuals to withdraw up to \$10,000 from an IRA for the purchase of a first home without imposition of the 10-percent additional tax. This provision would apply to individuals who did not own a home in the last three years and who are purchasing or constructing a principal residence that costs no more than 110 percent of the median home price in the area where the residence is located.

The proposal would be effective on January 1, 1990.

#### *Prior Action*

The 1989 budget reconciliation provisions as approved by the Senate Finance Committee (included in S. 1750 as reported by the Senate Budget Committee) contained a provision that would have allowed first-time home buyers to make withdrawals from an IRA without imposition of the 10-percent additional tax. This provision was removed from the bill by Senate floor amendment.

### 4. New Child Tax Credit and Refundable Child and Dependent Care Tax Credit

#### *Present Law*

#### *Earned income tax credit*

Under present law, low-income workers with minor dependents are eligible for a refundable income tax credit of up to 14 percent of the first \$6,810 of earned income for 1990. The maximum amount of the credit is \$953. The credit is reduced by an amount equal to 10 percent of the excess of the greater of (a) adjusted gross income (AGI) or (b) earned income over \$10,730. The credit is not available to taxpayers with AGI over \$20,264. The maximum amount of earnings with respect to which the credit may be claimed and the income level at which the phaseout of the credit begins are adjusted annually for inflation.

Earned income eligible for the credit includes wages, salaries, tips, and other employee compensation, plus the amount of the taxpayer's net earnings from self employment. Eligible individuals may utilize an advance payment system to receive the benefit of the credit in their paychecks.

#### *Child and dependent care credit*

Under present law, a nonrefundable income tax credit is allowed for up to 30 percent of a limited dollar amount of employment-re-

lated child or dependent care expenses. Eligible employment-related expenses are limited to \$2,400 in the case of one qualifying individual (\$4,800 in the case of two or more qualifying individuals). The 30-percent credit rate is reduced by one percentage point for each \$2,000 (or fraction thereof) of the taxpayer's AGI between \$10,000 and \$28,000. The credit rate is 20 percent for taxpayers with AGI in excess of \$28,000.

The term "qualifying individual" means (1) a dependent of the taxpayer who is under age 13 and with respect to whom the taxpayer is entitled to claim a dependent exemption, (2) a dependent of the taxpayer who is physically or mentally incapable of caring for himself or herself, or (3) a spouse of the taxpayer if the spouse is physically or mentally incapable of caring for himself or herself.

Under present law, the dollar amount of expenses eligible for the dependent care credit of any taxpayer is reduced dollar for dollar by the amount of expenses excludable from that taxpayer's income under the dependent care exclusion.

### *President's Budget Proposal*

#### *Proposed child tax credit*

Under the President's budget proposal, low-income families with at least one working individual would be entitled to claim a new refundable tax credit of up to \$1,000 for each dependent child under age four. For each child under the age of four, families could claim a credit equal to 14 percent of earned income, with a maximum credit equal to \$1,000 per child. Initially, the credit would be reduced by an amount equal to (1) 20 percent times the number of such children multiplied by (2) the excess of the greater of (a) AGI or (b) earned income over \$8,000. The credit would not be available to families with AGI or earned income greater than \$13,000. In subsequent years, both the starting and end points of the phaseout range would be increased by \$1,000 increments. In 1994, the credit would phase out between \$15,000 and \$20,000.

The credit would be effective for taxable years beginning on or after January 1, 1990. Families would have the option of receiving the tax benefit through an advance payment system similar to the earned income tax credit. Under such an advance payment system, the individual would file a claim with the individual's employer to adjust income tax withholding to take account of the available credit. In the event that the amount of the credit exceeds total withholding, then the employer would make a payment to the employee in conjunction with the regular employee paycheck. The employer would reduce the amount of withholding it submits to the Treasury by the amount of the payment made to the employee.

#### *Refundable child and dependent care credit*

Under the President's budget proposal, the existing child and dependent care tax credit would be made refundable. Families could not claim both the new child credit and the child and dependent care credit with respect to the same child, but could choose the larger of the two credits. The refundable child and dependent care credit would be effective for taxable years beginning on or after January 1, 1990.

### *Prior Action*

The President's budget proposal for 1990 contained the same proposal. The Omnibus Budget Reconciliation Act of 1989 (H.R. 3299) as passed by the House contained an extension of the earned income tax credit where the amount of credit was adjusted for family size. In addition, H.R. 3299 as passed by the House included a supplemental young child credit for qualified children under six years of age of low-income taxpayers. These provisions were not included in the Act as enacted. The Senate passed S. 5, which contained a provision to make the dependent care credit 90-percent refundable. In addition, S. 5 also included a supplemental young child credit for qualified children under four years of age of low income taxpayers. These provisions were not enacted in the first session of the 101st Congress.

## **5. Deductions for Special Needs Adoptions**

### *Present Law*

The Tax Reform Act of 1986 (the 1986 Act) repealed the deduction for adoption expenses associated with special needs children, effective for taxable years beginning on or after January 1, 1987. Under prior law, a deduction of up to \$1,500 of expenses associated with the adoption of special needs children was allowed. The 1986 Act provided for a new outlay program under the existing Adoption Assistance Program to reimburse expenses associated with the adoption process of these children. The Title IV-E Adoption Assistance outlay program provides assistance for adoption expenses for these special needs children receiving Federally assisted adoption assistance payments as well as special needs children in private and State-only programs.

One component of the Adoption Assistance Program requires States to reimburse certain costs incurred for special needs children. The Federal Government shares 50 percent of these costs up to a maximum Federal share of \$1,000 per child. Reimbursable expenses include those associated directly with the adoption process such as legal costs, social service review, and transportation costs.

### *President's Budget Proposal*

The President's budget proposal would permit an itemized deduction for certain incurred expenses associated with the adoption of special needs children up to a maximum of \$3,000 per child. Eligible expenses would be limited to those: (1) directly associated with the adoption process and (2) that are of a type eligible for reimbursement under the Adoption Assistance Program. These include court costs, legal expenses, social service review, and transportation costs. A deduction of up to \$3,000 would be allowed for eligible expenses regardless of the level of reimbursement allowed under the Adoption Assistance Program. Expenses which were deducted and reimbursed would be included in income in the year in which the reimbursement occurred.

The proposal also clarifies that all reimbursements are includible in income to the recipient unless deductible under this provision.



The proposal would be effective for calendar years after December 31, 1990.

### *Prior Action*

This proposal was included in the President's budget proposal for fiscal year 1990. A similar provision was approved by the Senate Finance Committee in its 1989 budget reconciliation provisions (included in S. 1750 as reported by the Senate Budget Committee), but the provision was removed from the bill by Senate floor amendment.

## **6. Permit Limited Use of Excess Pension Funds to Pay Retiree Health Benefits**

### *Present Law*

Under present law, pension plan assets may not revert to an employer prior to the termination of the plan and the satisfaction of all plan liabilities. Any assets that revert to the employer upon such termination are included in the gross income of the employer and are subject to a 15-percent excise tax.

Under section 401(h) of the Code, a pension plan may provide retiree medical benefits through a separate account if certain requirements are satisfied. The assets of a pension plan may not be transferred to a section 401(h) account without disqualifying the plan and subjecting the amounts transferred to income tax and the excise tax on reversions.

### *President's Budget Proposal*

The President's budget proposal would permit the transfer of excess pension plan assets to a section 401(h) medical benefits account that is part of such plan without termination or disqualification of the plan. The amount of the transfer could not exceed the amount of assets in excess of 140 percent of the plan's current liability or, if less, the plan's current retiree health liabilities for the current year. Amounts transferred would not be includible in the gross income of the employer or subject to the excise tax on reversions.

In the event of a transfer, the pension plan would be subject to additional requirements with respect to pension benefits, such as full vesting. Only one transfer would be permitted. The transfer would have to occur before January 1, 1993, and in a plan year beginning after December 31, 1990.

### *Prior Action*

The Omnibus Budget Reconciliation Act of 1989 as passed by the House (H.R. 3299) and the 1989 budget reconciliation provisions as approved by the Senate Finance Committee (included in S. 1750 as reported by the Senate Budget Committee) had similar provisions permitting the transfer of pension plan excess assets to pay retiree health benefits. The provisions were not included in the Act as enacted.

## 7. Energy Tax Initiatives

### a. Tax credits for oil and gas exploration and tertiary recovery

#### *Present Law*

New oil and gas reserves are typically identified by exploratory drilling (i.e., drilling in a property not previously drilled and not located next to another producing property). Present law does not provide any income tax credit for exploratory drilling. However, intangible drilling and development costs ("IDCs"), including IDCs attributable to domestic exploratory drilling, generally may be deducted as an expense.

Tertiary enhanced recovery techniques increase available reserves by producing oil and gas that often cannot be recovered economically through conventional recovery techniques. Present law does not provide any credit for projects using these techniques. However, certain tertiary injectant expenses may be deducted in the year paid or incurred.

#### *President's Budget Proposal*

The President's budget proposal would provide a 10-percent tax credit for the first \$10 million (per year per company) of IDCs attributable to exploratory drilling. A 5-percent credit would be allowed for the balance of the IDCs attributable to exploratory drilling.

In addition, the President's budget proposal would provide a 10-percent tax credit for all capital expenditures on projects that represent the initial application of tertiary enhanced recovery techniques to a property.

These tax credits could be applied against both the regular tax and the alternative minimum tax. However, these credits, in conjunction with all other credits and net operating loss carryforwards, could not eliminate more than 80 percent of the tentative minimum tax liability in any year. Unused credits could be carried forward.

The tax credits would be phased out if the average daily U.S. wellhead price of oil is at or above \$21 per barrel for an entire calendar year.

The credits would be effective for costs incurred on or after January 1, 1991.

#### *Prior Action*

The President's budget proposal for fiscal year 1990 contained the same recommendation.

### b. Modification of oil and gas percentage depletion rules

#### *Present Law*

Under present law, independent oil producers and royalty owners (but not integrated oil companies) recover certain costs incurred prior to drilling an oil- or gas-producing property using the higher of cost or percentage depletion. Under percentage depletion,

15 percent of the taxpayer's gross income from an oil- or gas-producing property is allowed as a deduction in each taxable year. The amount deducted may not exceed 50 percent of the taxable income from the property for the taxable year, computed without regard to the depletion deduction (the "net income limitation"). Additionally, the deduction for all oil and gas properties may not exceed 65 percent of the taxpayer's overall taxable income (determined with certain adjustments).

In addition, percentage depletion for oil and gas properties for independent producers and royalty owners is limited to 1,000 barrels of average daily domestic crude oil production (or an equivalent amount of natural gas). If an interest in a proven oil or gas property is transferred after 1974, production from that interest generally does not qualify for percentage depletion.

### *President's Budget Proposal*

The President's budget proposal would increase the net income limitation from 50 percent to 100 percent.

In addition, the President's budget proposal would repeal the percentage depletion anti-transfer rule.

The proposal would be effective on January 1, 1991.

### *Prior Action*

The President's budget proposals for fiscal years 1989 and 1990 contained the same recommendation.

The 1989 budget reconciliation provisions as approved by the Senate Finance Committee (included in S. 1750 as reported by the Senate Budget Committee) would have repealed the net income limitation for certain marginal oil and gas production. The provision was removed from the bill by Senate floor amendment.

### **c. Modification of tax preference for IDCs in the alternative minimum tax**

Under present law, domestic IDCs generally may either be currently expensed or else may be capitalized and recovered through depletion or depreciation deductions (as appropriate), at the election of the taxpayer. In general, IDCs include expenditures by the property owner incident to and necessary for the drilling and the preparation of wells for the production of oil and gas (or geothermal energy) which are neither for the purchase of tangible property nor part of the acquisition price of an interest in the property. IDCs include amounts paid for labor, fuel, repairs, and site preparation. Costs that do not qualify as IDCs generally must be capitalized and recovered through depreciation or depletion.

Taxpayers are subject to an alternative minimum tax which is payable, in addition to all other tax liabilities, to the extent it exceeds the taxpayer's regular tax. The tax is calculated with respect to alternative minimum taxable income, which generally is the taxpayer's taxable income, as increased or decreased by certain adjustments and preferences. IDC deductions on successful oil and gas wells are a tax preference item for this purpose, to the extent that the taxpayer's "excess IDCs" exceed 65 percent of the taxpayer's net income from oil and gas properties (before deducting excess



IDCs). Excess IDCs are defined generally as (1) IDC deductions (attributable to successful wells) for the taxable year, minus (2) the amount that would have been deductible in that year had the IDCs been capitalized and recovered over a 10-year, straight-line amortization period. At the election of the taxpayer, the cost depletion method may be substituted for the 10-year amortization schedule in determining the amount of the tax preference. Also, the minimum-tax preference does not apply if the taxpayer elects to amortize IDCs over 60 months for both regular tax and minimum tax purposes.

### ***President's Budget Proposal***

The President's budget proposal would eliminate 80 percent of the present-law minimum tax preference item for IDCs attributable to exploratory drilling incurred by independent producers.<sup>4</sup>

The proposal would be effective on January 1, 1991.

### ***Prior Action***

The President's budget proposal for fiscal year 1990 contained the same recommendation.

## **8. Enterprise Zone Tax Incentives**

### ***Present Law***

#### ***Targeted area***

The Internal Revenue Code does not contain general rules for targeting areas for special tax treatment. Within certain Code sections, however, there are definitions of targeted areas for limited purposes. For example, the provisions relating to qualified mortgage bonds define targeted areas for the purpose of promoting housing development within economically distressed areas.

#### ***Tax credits for employers and employees***

There are no general provisions in present law under which an employer's or employee's tax liability varies according to the location of the employment. The targeted jobs tax credit in present law does, however, provide a tax credit for a portion of wage payments made to certain groups of employees. In addition, certain low-income workers with minor dependents are eligible for a refundable earned income tax credit (EITC) of up to 14 percent of the first \$6,500 of earned income for 1989. The credit is not available to taxpayers with adjusted gross income over \$19,360.

#### ***Deduction for purchase of stock***

In general, present law provides a deduction to certain taxpayers for contributions to an individual retirement account ("IRA"). Such contributions may be used to purchase corporate stock. The maximum annual deductible contribution of an individual that can be made to an IRA generally is the lesser of \$2,000 or 100 percent of

<sup>4</sup> The proposal does not discuss the treatment of IDCs under the present-law corporate adjusted current earnings adjustment.

the individual's compensation. All or a portion of amounts withdrawn from IRAs are includible in income when withdrawn.

### ***Capital gains***

Net capital gain is taxed at the same rates applicable to ordinary income under present law. Before 1987, net capital gain from the sale or exchange of a capital asset was taxable at a reduced rate. Noncorporate taxpayers could reduce net capital gain by 60 percent, and the remainder was taxed as ordinary income—effectively establishing a maximum 20-percent rate. Before 1987, the maximum tax rate for corporate capital gain was 28 percent.

### ***President's Budget Proposal***

The enterprise zone proposal includes three tax incentives applicable to qualifying investments and employees in up to 50 enterprise zones that will be selected over a 4-year period.

(1) The proposal would provide a 5-percent refundable tax credit to employees with total wages less than \$20,000 for the first \$10,500 of wages earned in an enterprise zone.

(2) In addition, taxpayers could deduct up to \$50,000 annually, with a lifetime maximum of \$250,000, for contributions to capital of certain small corporations which use the contributions to acquire tangible assets in conducting a business in an enterprise zone.

(3) Finally, any capital gain realized on tangible property located within an enterprise zone for 2 years would be excludible from taxable income.

### ***Prior Action***

As part of his Message to Congress of February 9, 1989, entitled "Building a Better America," the President proposed creating up to 70 enterprise zones and providing unspecified tax benefits for the enterprise zones. Subsequently, hearings were held by the House Committee on Ways and Means on a proposal submitted by the administration which was substantially identical to the current proposal.

During the 100th Congress, the Senate Finance Subcommittee on Taxation and Debt Management held a hearing on S. 788 and S. 983, which would provide special tax incentives for certain designated Indian enterprise zones and rural enterprise zones. The Housing and Community Development Act of 1987 authorizes the establishment of 100 enterprise zones. The Act establishes the criteria to be used in nominating and selecting areas to be designated as enterprise zones, but does not provide any tax incentives.

## **9. Treatment of Salvage Value by Property and Casualty Insurance Companies**

### ***Present Law***

Under present law, property and casualty insurance companies may deduct losses in the year in which they are incurred. The deduction for losses incurred consists of a deduction for losses paid during the taxable year, and a deduction for the increase in dis-

counted reserves for losses incurred during the taxable year but still unpaid as of the end of the taxable year.

The deduction for losses paid during the taxable year must be reduced to take into account salvage and reinsurance. However, under regulations, insurance companies are not required to reduce paid losses by salvage attributable to such losses if any State, Territory, or the District of Columbia prohibits the company from treating the salvage value as an asset for statutory purposes.

### *President's Budget Proposal*

The President's budget proposal would require that the deduction for losses incurred, both paid and unpaid, be reduced by estimated recoveries of salvage (including subrogation claims) attributable to such losses, whether or not the salvage is treated as an asset for statutory purposes. Regulatory authority also would be provided to the Secretary of the Treasury to provide for the discounting of any salvage to be taken into account.

The provision would apply to taxable years beginning after December 31, 1989. Application of this provision would be a change in the taxpayer's method of accounting for tax purposes.

### *Prior Action*

In the 1986 Tax Reform Act, Congress directed the Secretary of Treasury to provide, in regulations, for the proper treatment of salvage and reinsurance recoverable with respect to unpaid losses. The Treasury Department issued temporary regulations on December 30, 1987 (T.D. 8171) which required that estimated recoveries on account of salvage and reinsurance attributable to unpaid losses be taken into account in the computation of unpaid losses and that adjustments to deductions for losses paid include all salvage in the course of liquidation, and all reinsurance in the process of collection.

## B. Expiring Tax Provisions

### 1. Permanent Research and Experimentation Tax Credit

#### *Present Law*

A 20-percent tax credit is allowed to the extent that a taxpayer's qualified research expenditures for the current year exceed its base amount for that year. The credit will not apply to amounts paid or incurred after December 31, 1990, and a special rule to prorate qualified research expenditures applies in the case of any taxable year which begins before October 1, 1990, and ends after September 30, 1990.<sup>5</sup> Under this special proration rule, the amount of qualified research expenses incurred by a taxpayer prior to January 1, 1991, is multiplied by the ratio that the number of days in that taxable year before October 1, 1990, bears to the total number of days in such taxable year before January 1, 1991.<sup>6</sup>

The base amount for the current year generally is computed by multiplying the taxpayer's "fixed-base percentage" by the average amount of the taxpayer's gross receipts for the four preceding years. If a taxpayer both incurred qualified research expenses and had gross receipts during each of at least three years from 1984 to 1988, then its "fixed-base percentage" is the ratio that its total qualified research expenses for the 1984-1988 period bears to its total gross receipts for this period (subject to a maximum ratio of .16).<sup>7</sup>

Qualified research expenses consist of: (1) in-house expenses of the taxpayer for research wages and supplies used in research; (2) certain time-sharing costs for computer use in research; and (3) 65 percent of amounts paid by the taxpayer for contract research conducted on the taxpayer's behalf.

In addition, the 20-percent tax credit also applies to the *excess* of (1) 100 percent of corporate cash expenditures (including grants or contributions) paid for university basic research *over* (2) the sum of (a) the greater of two fixed research floors plus (b) an amount reflecting any decrease in nonresearch giving to universities by the corporation as compared to such giving during a fixed base period, as adjusted for inflation.

Deductions for qualified research expenditures allowed to a taxpayer under sec. 174 are reduced by an amount equal to 100 percent of the taxpayer's research credit determined for that year.

<sup>5</sup> Qualified research expenses incurred in taxable years ending on or before September 30, 1990, are eligible for the full credit. Research expenses incurred after December 31, 1990, are not eligible for the research credit.

<sup>6</sup> The taxpayer's base amount as otherwise determined also is prorated by multiplying such amount by the ratio that the number of days in the taxable year before October 1, 1990, bears to the total number of days in such taxable year.

<sup>7</sup> If a taxpayer did not both incur qualified research expenses and have gross receipts during each of at least three years between 1984-1988, then it is assigned a fixed-base percentage of .03.



## *President's Budget Proposal*

The President's proposal would make permanent the 20-percent research tax credit by allowing 100 percent of total research expenses to be used for the computation of the credit for all years after December 31, 1989.

### *Prior Action*

The research credit initially was enacted in the Economic Recovery Tax Act of 1981 as a credit equal to 25 percent of the excess of qualified research expenses in the current year over the average of qualified research expenses in the prior three taxable years. The research credit was modified in the Tax Reform Act of 1986 which (1) extended the credit through December 31, 1988, (2) reduced the credit rate to 20 percent, (3) tightened the definition of research expenditures eligible for the credit, and (4) modified the university basic research credit.

The Technical and Miscellaneous Revenue Act of 1988 extended the credit for one additional year, through December 31, 1989. The 1988 Act also reduced the deduction allowed under section 174 for qualified research expenses by an amount equal to 50 percent of the research credit determined for the year.

The Omnibus Budget Reconciliation Act of 1989 effectively extended the research credit for nine months (by prorating qualified expenses incurred before January 1, 1991). The 1989 Act also modified the method for calculating a taxpayer's base amount and further reduced the deduction allowed under section 174 for qualified research expenses by an amount equal to 100 percent of the research credit determined for the year.

## **2. Research and Experimentation Expense Allocation Rules**

### *Present Law*

Computation of the foreign tax credit requires the taxpayer to distinguish between taxable income from U.S. sources and taxable income from foreign sources, and thus to allocate and apportion deductions among items of U.S. source and foreign source gross income. Treasury regulations prescribe a detailed method for allocating and apportioning research and experimental (R&D) expenses for this purpose, among others.

Effective for taxable years beginning after August 13, 1981, and on or before August 1, 1987, as well as for a taxpayer's first taxable year beginning after August 1, 1987, and for a taxpayer's first taxable year beginning after August 1, 1989 and before August 2, 1990, the R&D allocation regulation was in part suspended (for purposes of determining the source of taxable income) by a succession of statutes: the Economic Recovery Tax Act of 1981 (ERTA), the Deficit Reduction Act of 1984 (DEFRA), the Consolidated Omnibus Budget Reconciliation Act of 1985 (COBRA), the Tax Reform Act of 1986 (TRA), the Technical and Miscellaneous Revenue Act of 1988 (TAMRA), and the Omnibus Budget Reconciliation Act of 1989 (OBRA89). In taxable years governed by ERTA, DEFRA, and COBRA, all U.S.-incurred R&D expenses were allocated to U.S. source income. In taxable years governed by TRA, 50 percent of

such expenses (other than amounts incurred to meet certain legal requirements, and thus allocable to one geographical source) were allocated to U.S. source income, with the remainder allocated and apportioned either on the basis of sales or gross income.

Expenses incurred during the taxable year governed by TAMRA (for any taxpayer, its first taxable year beginning after August 1, 1987) were treated in one of two alternative ways depending upon whether the expenses were in effect deemed to have been incurred in the first four months of the year, or incurred instead during the remaining eight or fewer months of the year. Similarly, expenses incurred during the taxable year governed by OBRA89 (for any taxpayer, its first taxable year beginning after August 1, 1989 and before August 2, 1990) are treated in one of the same two alternative ways depending on whether the expenses were in effect deemed to have been incurred in the first nine months of the year, or incurred instead during the remaining three or fewer months of the year. For these purposes total expenses for the year were deemed to be incurred evenly throughout the year. For expenses deemed paid or incurred during the earlier period of such years (other than amounts incurred to meet certain legal requirements, and thus allocable to one geographical source), 64 percent of U.S.-incurred R&D expenses are allocated to U.S. source income, 64 percent of foreign-incurred R&D expenses are allocated to foreign source income, and the remainder of R&D expenses are allocated and apportioned either on the basis of sales or gross income, but subject to the condition that if income-based apportionment is used, the amount apportioned to foreign source income can be no less than 30 percent of the amount that would be apportioned to foreign source income were the sales method used. For expenses deemed paid or incurred during the later period of such years, the R&D allocation regulation applies.

### *President's Budget Proposal*

Under the President's budget proposal, R&D expenses (other than amounts incurred to meet certain legal requirements, and thus allocable to one geographical source) would be sourced as follows: 64 percent of U.S.-incurred R&D expenses would be allocated to U.S. source income; 64 percent of foreign-incurred R&D expenses would be allocated to foreign source income; and the remainder of R&D expenses would be allocated and apportioned either on the basis of sales or gross income, but subject to the condition that if income-based apportionment is used, the amount apportioned to foreign source income can be no less than 30 percent of the amount that would be apportioned to foreign source income were the sales method used. The proposal would apply to all R&D expenses paid or incurred in taxable years beginning after August 1, 1990.

The substantive R&D allocation rules of the President's budget proposal are similar to those applicable in the first four months of the taxable year governed by TAMRA and the first nine months of the taxable year governed by OBRA89.



### *Prior Action*

In COBRA, Congress extended by one year the ERTA/DEFRA modification of the R&D regulation. In TRA, Congress enacted the temporary allocation rule that generally allowed taxpayers to allocate at least 50 percent of domestic R&D expense to U.S. source income.

At a hearing before a subcommittee of the Senate Finance Committee on April 3, 1987, the Administration testified in favor of a proposal under which taxpayers would be permitted to allocate 67 percent of expenses for R&D conducted in the United States to U.S. source income. The remainder of such expenses would be apportioned on the basis of either gross sales or gross income, with no limitation on the amount apportioned to U.S. source income using the gross income method. The Administration's 1987 proposal was included in H.R. 3545, the Omnibus Budget Reconciliation Act of 1987 (OBRA87), as passed by the House. The proposal also was included in the October 1987 budget reconciliation submission of the Senate Finance Committee to the Senate Budget Committee. The proposal was not included in the conference agreement on OBRA87.

Permanent statutory R&D allocation rules similar to those in H.R. 3545 as passed by the House in 1987 were included in the President's budget proposal for fiscal year 1989. The Miscellaneous Revenue Act of 1988, H.R. 4333, as passed by the House in August 1988, included statutory modifications to the R&D allocation regulation, which modifications were to be in effect from the expiration of the TRA R&D allocation rules through taxable years beginning before 1991. The substantive provisions of H.R. 4333 as passed by the House would have been similar to the proposal included in H.R. 3545 with three primary modifications: (1) 64 percent of U.S.-incurred R&D expenses would be allocated to U.S. source income, rather than 67 percent; (2) 64 percent of foreign-incurred R&D expenses would be allocated to foreign source income; (3) if income-based apportionment was used, the amount apportioned to foreign source income could be no less than 30 percent of the amount that would have been apportioned to foreign source income had the sales method been used.

The Senate substitute for H.R. 4333 (passed on October 11, 1988) included substantive R&D allocation rules like those in the House-passed bill, but under the Senate bill the statutory rules expired, in effect, after the first four months of the taxpayer's first taxable year beginning after August 1, 1987 (treating R&D expenses for the entire year as if incurred ratably throughout the year). In conference, the Senate version was adopted and became part of TAMRA.

The Presidential budget proposals for fiscal year 1990 included permanent R&D allocation rules similar to the Administration's 1987 proposal. Permanent R&D allocation rules similar to those contained in TAMRA were included in OBRA89 (H.R. 3299) as passed by the House on October 5, 1989. The October 1989 budget reconciliation submission of the Senate Finance Committee to the Senate Budget Committee (included in S. 1750) included a two-year extension of the same substantive R&D allocation rules as were provided in TAMRA and in the 1989 House bill. No R&D allocation

rules were included in the Senate substitute to H.R. 3299, passed on October 13, 1989. The conference agreement on OBRA89 included the substantive R&D allocation rules passed by the House and approved by the Senate Finance Committee, but under the conference agreement the statutory rules expired, in effect, after the first nine months of the taxpayer's first taxable year beginning after August 1, 1989 (treating R&D expenses for the entire year as if incurred ratably throughout the year).

### 3. Low-Income Housing Tax Credit

#### *Present Law*

A credit is allowed in annual installments over 10 years for qualifying low-income rental housing, which may be newly constructed, substantially rehabilitated, or newly acquired existing residential rental property. For most newly constructed and rehabilitated housing placed in service after 1987, the credit percentages are adjusted monthly to maintain a present value of the credit stream of 70 percent of the total qualified expenditures. In the case of acquisition of existing housing and of newly constructed or rehabilitated housing receiving other Federal subsidies (including tax-exempt bonds), monthly adjustments are made to maintain a 30-percent present value for the credit.

A residential rental project qualifies for the low-income housing credit only if (1) 20 percent or more of the aggregate residential rental units are occupied by individuals with incomes of 50 percent or less of area median income, as adjusted for family size, or (2) 40 percent or more of the aggregate residential rental units in the project are occupied by individuals with incomes of 60 percent or less of area median income, as adjusted for family size. Credit eligibility also depends on the existence of a 30-year extended low-income use agreement for the property. If property on which a low-income housing credit is claimed ceases to qualify as low-income rental housing or is disposed of before the end of a 15-year credit compliance period, a portion of the credit may be recaptured. The 30-year extended use agreement creates a State law right to enforce low-income use for an additional 15 years after the initial 15-year recapture period.

In order for a building to be a qualified low-income building, the building owner generally must receive a credit allocation from the appropriate credit authority. An exception is provided for property which is substantially financed with the proceeds of tax-exempt bonds subject to the State's private-activity bond volume limitation. The low-income credit is allocated by State or local government authorities subject to an annual limitation for each State. The annual credit allocation was \$1.25 per resident for years before 1990 and is \$0.9375 per resident for 1990.

The low-income housing credit expires on December 31, 1990.

#### *President's Budget Proposal*

The proposal would extend the credit through 1991, and would make each State's credit allocation authority for 1990 and 1991 equal to the product of \$1.25 and the State's population.

### *Prior Action*

The low-income housing credit was enacted by the Tax Reform Act of 1986, with an expiration date of December 31, 1988. The Technical and Miscellaneous Revenue Act of 1988 included a provision to extend the credit for one year. The credit was substantially revised and extended through December 31, 1990, by the Omnibus Budget Reconciliation Act of 1989.

#### **4. Extend Special Rules for Health Insurance Costs of Self-Employed Individuals**

### *Present Law*

Under present law, self-employed individuals are entitled to deduct 25 percent of the amount paid for health insurance for the individual and the individual's spouse and dependents. The deduction expires for taxable years beginning after September 30, 1990. For taxable years beginning in 1990, the deduction applies only to amounts paid before October 1, 1990, for insurance for periods before October 1, 1990. Health benefits provided by a self-employed individual to his or her employees are fully deductible as compensation.

### *President's Budget Proposal*

The President's budget proposal would make the 25-percent deduction permanent.

### *Prior Action*

The 25-percent deduction was originally enacted on a temporary basis in the Tax Reform Act of 1986 (the "1986 Act"). The provision was to expire for taxable years beginning after December 31, 1989. Prior to the 1986 Act, health expenses of self-employed individuals were deductible under the rules applicable to personal medical expenses, i.e., if the total medical expenses of the individual exceeded 5 percent of adjusted gross income. The Omnibus Budget Reconciliation Act of 1989 as passed by the House (H.R. 3299) and the 1989 budget reconciliation provisions as approved by the Senate Finance Committee (included in S. 1750 as reported by the Senate Budget Committee) would have extended the 25-percent deduction through December 31, 1991. The 1989 Act as enacted extended the provision through September 30, 1990.

#### **5. Airport and Airway Trust Fund Excise Taxes**

### *Present Law*

#### *Tax rates*

Excise taxes are imposed on air passenger tickets (8 percent), domestic air freight (5 percent), international departures (\$6 per person), and fuels for noncommercial aviation (12 cents per gallon on gasoline and 14 cents per gallon on jet and other fuels). Under the Airport and Airway Revenue Act of 1987, these aviation taxes are scheduled to expire after December 31, 1990. The Omnibus



Budget Reconciliation Act of 1989 increased the international departure tax from \$3 to \$6 per person on January 1, 1990.

Revenues from the aviation excise taxes are transferred to the Airport and Airway Trust Fund to finance Federal airport and airway programs.

### ***Tax reduction trigger***

The 1989 Act provides for an automatic 50-percent reduction in the air passenger ticket tax, the air freight tax, and the tax on nongasoline fuels <sup>8</sup> on January 1, 1991, if the total appropriations for fiscal years 1989 and 1990 for airport improvements, airway facilities and equipment, and research, engineering and development are less than 85 percent of the total amounts authorized for these programs for fiscal years 1989 and 1990. Under the 1987 Act, the tax reduction trigger would have been effective on January 1, 1990.

### ***President's Budget Proposal***

The President's budget proposal would repeal the aviation tax reduction trigger. The proposal also would extend the Trust Fund taxes beyond 1990 at increased rates (except for the \$6 international departure tax), without a recommendation regarding an expiration date.

The air passenger ticket tax would be increased to 10 percent; the air freight tax would be increased to 6.25 percent; and the taxes on noncommercial aviation fuels would be increased to 15 cents and 17.5 cents per gallon, respectively, for gasoline and nongasoline fuels.

The proposal would be effective on January 1, 1991.

### ***Prior Action***

The Trust Fund tax reduction trigger was postponed for one year (to January 1, 1991) in the Omnibus Budget Reconciliation Act of 1989. The 1989 Act also increased the international departure tax from \$3 to \$6 per person on January 1, 1990.

The President's budget proposals for fiscal years 1989 and 1990 also proposed repeal of the Trust Fund tax reduction trigger.

## **6. Extension of 3-Percent Telephone Excise Tax and Modification of Collection Period**

### ***Present Law***

#### ***Imposition of tax***

The Federal telephone excise tax is 3 percent on local and long distance telephone service and on teletypewriter exchange service. The telephone tax is scheduled to expire after December 31, 1990; the 3-percent rate has been in effect since January 1, 1983.

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<sup>8</sup> The tax on noncommercial aviation gasoline would be reduced from 12 cents per gallon to the general highway rate of 9 cents per gallon.

*Collection of tax*

Under present regulations, telephone tax billed to the customer in a semi-monthly period is considered to be collected during the second following semi-monthly period. The tax must be deposited within 3 banking days after the end of the semi-monthly period for which the tax is considered collected.

*President's Budget Proposal**Extension of tax*

The President's budget proposal would extend permanently the Federal telephone excise tax at its current 3-percent rate.

*Collection of tax*

The President's budget proposal would modify the collection period so that the tax for a semi-monthly period would be considered as collected during the first week of the second semi-monthly period. Deposit of tax would be required to be made within 3 banking days after the end of the week for which the tax is considered to be collected. The change would be effective for taxes considered collected for semi-monthly periods beginning after December 31, 1990.

*Prior Action*

The 3-percent tax rate was extended through 1990 in the Omnibus Budget Reconciliation Act of 1987. The Omnibus Budget Reconciliation Act of 1989 as passed by the House (H.R. 3299) included a permanent extension of the telephone excise tax. The provision was dropped in conference. In addition, in 1989, the Senate passed, as part of S. 5, a permanent extension of the telephone excise tax. Also, both H.R. 3299, as passed by the House, and S. 5, as passed by the Senate, would have modified the collection period as in the President's budget proposal.

## **C. Other Excise Tax Provisions**

### **1. Increase in Harbor Maintenance Excise Tax**

#### *Present Law*

A harbor maintenance tax is imposed on the use of U.S. ports. The tax is 0.04 percent of the value of commercial cargo loaded or unloaded at U.S. ports. Passengers fares are generally included under the tax, except for certain ferry boats.

The tax does not apply to cargo donated for foreign use. In addition, the tax does not apply to (1) cargo shipped between a U.S. mainland port and Alaska, Hawaii, or a U.S. possession for ultimate use or consumption therein; (2) cargo shipped between Alaska, Hawaii, or a U.S. possession (or between two possessions) for ultimate use or consumption therein; and (3) cargo loaded and unloaded within Alaska, Hawaii, or a U.S. possession. This exception does not apply to cargo destined for foreign consumption or to crude oil cargo with respect to Alaska.

The tax was enacted in the Harbor Maintenance Revenue Act of 1986, effective on April 1, 1987.

#### *President's Budget Proposal*

The President's budget proposal would increase the harbor maintenance tax to 0.125 percent of the value. The increase is intended to fully offset the cost of Corps of Engineers harbor maintenance dredging, as well as the cost of certain National Oceanic and Atmospheric Administration marine programs (including coastal mapping, marine weather, and circulation and tide data).

The proposal would be effective on October 1, 1990.

### **2. Modification of Alcohol Occupational Excise Taxes**

#### *Present Law*

Present law imposes a special occupational tax of \$250 a year upon retail dealers in distilled spirits, wines, or beer (sec. 5121). Wholesale dealers in distilled spirits, wines, or beer are subject to a special occupational tax of \$500 a year (sec. 5111). In addition, producers of distilled spirits, wines, or beer are subject to a special occupational tax of \$1,000 a year per premise (secs. 5081 and 5091).<sup>9</sup>

#### *President's Budget Proposal*

The President's proposal would eliminate the special occupation taxes currently levied on retailers in connection with liquor occu-

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<sup>9</sup> The tax is \$500 a year per premise for businesses with gross receipts of less than \$500,000 in the preceding year.



pations, and would increase existing taxes on liquor wholesalers and manufacturers, effective October 1, 1990.

### *Prior Action*

The Omnibus Budget Reconciliation Act of 1987 established the present-law rates for the special occupational taxes imposed on alcoholic beverage retailers, wholesalers, and producers.

A 1989 budget reconciliation provision approved by the Committee on Finance (included in S. 1750 as reported by the Senate Budget Committee) would have reduced from \$250 to \$150 per year the occupational tax for certain small dealers in alcoholic beverages (i.e., dealers with annual gross receipts from the sale of alcoholic beverages less than \$250,000 and in which at least one-third of the alcoholic beverages sold are consumed on the premises of the dealer). The provision was removed from the bill by Senate floor amendment.

## **D. Employment Tax Provisions**

### **1. Payroll Tax Deposit Stabilization**

#### ***Present Law***

Treasury regulations have established the system under which employers deposit income taxes withheld from employees' wages and FICA taxes. The frequency with which these taxes must be deposited increases as the amount required to be deposited increases.

Employers are required to deposit these taxes as frequently as eight times per month, provided that the amount to be deposited equals or exceeds \$3,000. These deposits must be made within three banking days after the end of the eighth-monthly period.

Effective August 1, 1990, employers who are on this eighth-monthly system are required to deposit income taxes withheld from employees' wages and FICA taxes by the close of the applicable banking day (instead of by the close of the third banking day) after any day on which the business cumulates an amount to be deposited equal to or greater than \$100,000 (regardless of whether that day is the last day of an eighth-monthly period).

For 1990, the applicable banking day is the first. For 1991, the applicable banking day is the second. For 1992, the applicable banking day is the third. For 1993 and 1994, the applicable banking day is the first. The applicable banking day varies from year to year to minimize unevenness in the receipts effects of this provision. The Treasury Department is given authority to issue regulations for 1995 and succeeding years to provide for similar modifications to the date by which deposits must be made in order to minimize unevenness in the receipts effects of this provision.

#### ***President's Budget Proposal***

The President's budget proposal would require that deposits equal to or greater than \$100,000 must be made by the close of the next banking day for all years. Thus, no change from present law would be necessary for calendar year 1990, but for calendar years 1991 and 1992 deposits would be accelerated. The regulatory authority provided to the Treasury Department would be repealed.

#### ***Prior Action***

The present-law rules relating to deposits that equal or exceed \$100,000 were added by the Omnibus Budget Reconciliation Act of 1989.

## **2. Medicare Hospital Insurance (HI) for State and Local Employees**

### ***Present Law***

Prior to enactment of the Consolidated Omnibus Budget Reconciliation Act of 1985 (COBRA), State and local government employees were covered under the Medicare system only if the State and the Secretary of Health and Human Services entered into a voluntary agreement providing for coverage under the social security and medicare programs. In COBRA, the Congress extended Medicare coverage (and the corresponding hospital insurance payroll tax) on a mandatory basis to State and local government employees hired after March 31, 1986, for services performed after that date.

Under present law, State and local government employees hired before April 1, 1986, are not covered under Medicare unless a voluntary agreement is in effect. Medicare coverage (and the hospital insurance payroll tax) is mandatory for Federal employees.

For wages paid in 1990 to Medicare-covered employees, the total hospital insurance tax rate is 2.9 percent of the first \$51,300 of wages (Code secs. 3101, 3111, and 3121). One-half of this tax is paid by the employee and one-half by the employer.

### ***President's Budget Proposal***

The President's budget proposal would extend Medicare coverage on a mandatory basis to all employees of State and local governments not otherwise covered under present law, without regard to their dates of hire. These employees and their employers would become liable for the hospital insurance portion of the FICA tax, and the employees would earn credit toward Medicare eligibility based on their covered earnings.

This proposal would be effective on October 1, 1990.

### ***Prior Action***

During the 99th Congress, the Senate amendment to H.R. 5300 (the Omnibus Budget Reconciliation Act of 1986) included a provision similar to the President's budget proposal. This provision was deleted from the legislation in conference.

This provision also was included in President Reagan's budget proposals for fiscal years 1988, 1989, and 1990, and in President Bush's budget proposal for fiscal year 1990.

## **3. Extend Social Security Retirement Coverage (OASDI) to State and Local Employees Not Participating In Public Employee Retirement**

### ***Present Law***

State and local employees are covered by Old-Age, Survivors, and Disability Insurance (OASDI) only if the State enters into a voluntary agreement with the Secretary of Health and Human Services. With certain exceptions, the State has broad latitude to decide which groups of State and local employees are covered.

For 1990, the OASDI tax is 6.20 percent of wages up to \$51,300, and is imposed on both the employer and employee.

### *President's Budget Proposal*

Under the President's budget proposal, mandatory social security coverage would be extended to those employees of State and local governments who do not participate in a retirement system in conjunction with their employment for the State or local government.

The proposal would be effective on October 1, 1990.

#### **4. Extend Social Security Retirement and Medicare Hospital Tax and Coverage (OASDHI) to D.C. Employees**

### *Present Law*

With respect to certain employees of the District of Columbia, the exception from Old-Age, Survivors and Disability Insurance (OASDI) available to State and local employees applies if the employee is covered under a retirement program established under Federal law. This exception now applies only to general government employees hired before October 1, 1987, and (regardless of their date of hire) to police, firefighters, teachers, and judges.

Under the Consolidated Omnibus Budget Reconciliation Act of 1985 (COBRA), the Congress extended Medicare coverage (and the corresponding hospital insurance payroll tax (HI)) on a mandatory basis to State and local government employees, as well as District of Columbia employees, hired after March 31, 1986, for services performed after that date.

For 1990, the OASDI tax is 6.20 percent and the HI tax is 1.45 percent of wages up to \$51,300. The tax is imposed on both the employer and the employees.

### *President's Budget Proposal*

Under the President's budget proposal, OASDHI coverage would be extended to all newly hired employees of the District of Columbia.

The proposal would be effective on January 1, 1991.

#### **5. Extend and Expand Railroad Unemployment Insurance Fund**

### *Present Law*

The railroad unemployment and sickness benefit program is financed by payroll taxes paid by railroad employers. The employees themselves do not contribute. Currently, the taxable earnings base is the first \$600 of each employee's monthly earnings. The payroll tax rate may vary from 0.5 percent to 8.0 percent (depending on the unemployment experience of the employer).

The Technical and Miscellaneous Revenue Act of 1988 provided an exemption from the full railroad unemployment tax rate for public commuter railroads in 1989 and 1990. Such public commuter railroads will reimburse the unemployment system for the amount of benefits paid during the year to their employees. Starting in 1991, those railroads will again be subject to payroll taxes on the same basis as other railroads.

### *President's Budget Proposal*

The President's budget proposal would extend the exemption provided to commuter railroads beyond 1990. The proposal would also extend the same exemption to Amtrak beginning in 1991.

### *Prior Action*

The Amtrak provision in the President's budget proposal was also included in President Bush's budget proposal for fiscal year 1990. It was also included in President Reagan's budget proposal for fiscal year 1989 (with an effective date of fiscal 1990).



## **E. IRS Provisions**

### **1. Extend User Fees**

#### ***Present Law***

The Internal Revenue Service (IRS) provides written responses to questions of individuals, corporations, and organizations relating to their tax status or the effects of particular transactions for tax purposes. The IRS responds to these inquiries through the issuance of letter rulings, determination letters, and opinion letters. The IRS charges a fee for most requests for a letter ruling, determination letter, opinion letter, or other similar ruling or determination. The legislation that requires the establishment of this fee program provides that it is not to apply to requests made after September 30, 1990.

#### ***President's Budget Proposal***

The IRS program that requires the payment of a fee for most requests for a letter ruling, determination letter, opinion letter, or other similar ruling or determination would be permanently extended.

#### ***Prior Action***

The Omnibus Budget Reconciliation Act of 1987 required the IRS to establish a program that requires the payment of a fee for most requests for a letter ruling, determination letter, opinion letter, or other similar ruling or determination (with the September 30, 1990 sunset date).

### **2. Initiate IRS Management Reforms**

#### ***Present Law***

The budget for the Internal Revenue Service (IRS), as passed by the Congress and signed by the President, specifies amounts to be expended in broad categories. IRS management has broad authority (within the constraints of the budget) to determine the relative priority and level of spending for specific activities within each category.

#### ***President's Budget Proposal***

The President's budget proposal states that IRS will undertake several management initiatives that would increase revenue yields without requiring additional expenditures. Implementation of these measures does not require that any change be made to the IRS budget or to the Internal Revenue Code; IRS has already begun work on some of these measures.



Although the details of this management initiative are not specified in the President's proposed budget, the Department of the Treasury's *General Explanations of the President's Budget Proposals Affecting Receipts* (January 1990) provides some detail. There are five major elements to this management initiative:

- (1) Accelerate the examination process for and expedite closings of tax shelter cases;
- (2) Accelerate resolution of issues raised during examination of tax returns of very large corporations;
- (3) Reassign current examination employees from lower yielding areas to examination of higher yielding excise tax returns;
- (4) Increase examination of small retirement plans by reassigning current employees; and
- (5) Reassign current Examination employees to Appeals to help close 47 targeted large cases.

### **3. Increase in IRS FY 1991 Enforcement Funding**

#### ***Present Law***

In fiscal year 1989, the IRS had approximately 114,750 full-time equivalent employees with total budget authority of about \$5.2 billion.

#### ***President's Budget Proposal***

The President's budget proposal would increase IRS budget authority for fiscal year 1991 to about \$6.1 billion. The budget document states that IRS funding for enforcement is to be increased. The increases are to be used to collect delinquent taxes, improve the examination of tax returns, and increase document matching.

It is not possible from the budget document to determine readily which specific IRS functions would receive an increase in funding and which would receive a decrease, in that the budget document significantly reorganizes the structure of the IRS budget.

#### ***Prior Action***

President Bush's budget proposal for fiscal year 1990 included an IRS enforcement initiative. Earlier budget proposals of President Reagan contained different IRS enforcement funding proposals.

## **F. Certain User Fees Classified as Receipts**

### **1. Commodity Futures Trading Commission (CFTC) transaction fee**

#### ***Present Law***

There are no fees currently imposed on futures and options transactions regulated by the CFTC.

#### ***President's Budget Proposal***

A fee of 11 cents per transaction for CFTC-regulated futures and options trades would be imposed beginning October 1, 1990. The fees generated would be deposited as a governmental receipt to the general fund of the Treasury.

### **2. Securities and Exchange Commission (SEC) transaction fees**

#### ***Present Law***

Securities market transactions on organized exchanges are currently assessed a fee of 1/300 of one percent of dollar volume. Merger and proxy filings are currently assessed a fee of 1/50 of 1 percent per transaction. Securities offerings are currently assessed a registration fee of 1/50 of 1 percent of the value of the offering.

#### ***President's Budget Proposal***

The fee on securities market transactions would be increased to 1/220 of 1 percent of the dollar volume traded. This fee would be extended to most over-the-counter securities transactions (e.g., those transactions on the National Association of Securities Dealers Automatic Quotation (NASDAQ) system). The fee on merger and proxy filings would be increased to 1/40 of 1 percent of the value of the transaction. The registration fee on securities offerings would be increased to 1/40 of 1 percent of the value of the offering.

The proposed fee increases and fee impositions would be effective July 1, 1990. Revenue generated by these fees would be counted as offsetting receipts for the SEC.

### **3. Federal Emergency Management Agency (FEMA) User Fees**

#### ***Present Law***

The Federal Emergency Management Agency (FEMA) acts as the agent of the Nuclear Regulatory Commission in reviewing evacuation plans submitted by nuclear power plants. FEMA currently assesses no fees for reviewing these plans.

### *President's Budget Proposal*

The President's budget proposal would impose user fees on the owners of nuclear power plants sufficient to recover 100 percent of the costs incurred in its capacity of regulator of the evacuation plans for nuclear power plants. Revenue generated by these fees would be counted as offsetting receipts for FEMA.

### *Prior Action*

An identical provision was included in the President's budget proposals for fiscal years 1989 and 1990.

## **4. Extend Abandoned Mine Reclamation Fees**

### *Present Law*

Owners of coal mines are assessed a fee to help pay for the reclamation of abandoned mines. These fees provide the amounts available for appropriation from the Abandoned Mine reclamation Fund. The current rates are 35 cents per ton for surface mined coal and 15 cents per ton for underground mined coal. These fees are scheduled to expire in August, 1992.

### *President's Budget Proposal*

The President's budget proposal would extend these fees permanently.

## **5. Corps of Engineers Application Fees**

### *Present Law*

Currently, the Corps of Engineers does not charge fees on requests for permits for development or other activities on navigable waterways and wetlands.

### *President's Budget Proposal*

The President's budget proposal would enable the Corps of Engineers to begin collecting fees from non-Federal interests for services provided through the Flood Plain Management Services and Planning Assistance to States programs. These fees would be phased in over a three year period. Revenue generated by these fees would be counted as offsetting receipts for the Corps of Engineers.

## **6. Environmental Protection Agency (EPA) Fees**

### *Present Law*

Various fees are assessed on the beneficiaries of certain activities undertaken by the EPA.

### *President's Budget Proposal*

Fees would be imposed for the following activities undertaken by the EPA: auto fuel and certification tests; radon proficiency ratings; pesticide registrations; and EPA-issued water permits. A spe-

cial fund under the authority of the EPA would be established for the deposit of these fee receipts.

### ***Prior Action***

A special fund was established in 1988 for the deposit of receipts associated with the licensing of pesticides. Collection of these fees was suspended by the Federal Insecticide, Fungicide, and Rodenticide Act Amendments of 1988.

## **7. Housing and Urban Development (HUD) Interstate Land Sales Fees**

### ***Present Law***

A statement of record must be filed with the Secretary of HUD before a subdivision with 100 or more lots can be sold in interstate commerce. The Secretary is authorized to charge the developer a fee (up to \$1000 per developer) for the filing of this statement. These fee receipts are permanently appropriated to HUD and offset a portion of the direct administrative costs of the program.

### ***President's Budget Proposal***

The proposal would eliminate the \$1000 per developer fee limit and would allow the fee to be increased to fully offset program costs.



## II. ADMINISTRATION'S ESTIMATES OF BUDGET EFFECTS OF REVENUE PROVISIONS IN PRESIDENT'S FISCAL YEAR 1991 BUDGET PROPOSAL

Fiscal Years 1990-1995

[Billions of dollars]

Provision	1990	1991	1992	1993	1994	1995	1990-95
<b>A. Income Tax Provisions</b>							
1. Capital gains tax rate reduction for individuals .....	0.5	4.9	2.8	1.2	1.7	1.4	12.5
2. Family Savings Accounts .....	( <sup>1</sup> )	-0.2	-0.6	-1.0	-1.3	-1.6	-4.7
3. Penalty-free IRA withdrawal for first-time homebuyers .....	( <sup>1</sup> )	( <sup>1</sup> )	-0.1	-0.1	-0.1	-0.1	-0.4
4. Child tax credit provisions ( <sup>2</sup> ) .....	.....	( <sup>1</sup> )	( <sup>1</sup> )	( <sup>1</sup> )	-0.1	-0.1	-0.2
5. Adoption expense deduction .....	.....	( <sup>1</sup> )	( <sup>1</sup> )	( <sup>1</sup> )	( <sup>1</sup> )	( <sup>1</sup> )	( <sup>3</sup> )
6. Excess pension funds to pay retiree health benefits .....	.....	0.2	0.4	0.2	.....	.....	0.8
7. Energy tax incentives:							
a. Tax credits for oil and gas exploration and tertiary recovery .....	.....	-0.2	-0.3	-0.3	-0.4	-0.4	-1.6
b. Modification of oil and gas depletion percentage depletion rules .....	.....	( <sup>1</sup> )	( <sup>1</sup> )	( <sup>1</sup> )	( <sup>1</sup> )	( <sup>1</sup> )	( <sup>3</sup> )
c. Modification of tax preference for IDCs in the alternative minimum tax .....	.....	-0.1	-0.1	-0.1	-0.1	-0.1	-0.5
8. Enterprise zone tax incentives .....	.....	-0.1	-0.2	-0.3	-0.5	-0.8	-1.9
9. Loss deductions and salvage values for insurance companies .....	0.2	0.2	0.2	0.2	0.1	0.1	1.0

Footnotes at end of table.

## II. ADMINISTRATION'S ESTIMATES OF BUDGET EFFECTS OF REVENUE PROVISIONS IN PRESIDENT'S FISCAL YEAR 1991 BUDGET PROPOSAL—Continued

[Billions of dollars]

Provision	1990	1991	1992	1993	1994	1995	1990-95
<b><i>B. Expiring Tax Provisions</i></b>							
1. Permanent research and experimentation tax credit .....	-0.1	-0.5	-0.9	-1.1	-1.3	-1.6	-5.5
2. Foreign allocation and apportionment of research expenses .....	.....	-0.4	-0.7	-0.8	-0.8	-0.9	-3.6
3. Extend low-income housing tax credit .....	( <sup>1</sup> )	-0.1	-0.3	-0.4	-0.4	-0.4	-1.6
4. Extend deduction for self-employed health insurance .....	( <sup>1</sup> )	-0.2	-0.4	-0.5	-0.5	-0.6	-2.2
5. Extend and increase Airport Trust Fund aviation excise taxes ( <sup>4</sup> ) .....	.....	0.5	0.8	0.9	0.9	1.0	4.1
6. Permanently extend telephone excise tax and modify collection period ( <sup>4</sup> ) .....	.....	1.5	2.5	2.7	2.9	3.1	12.7
<b><i>C. Other Excise Tax Provisions</i></b>							
1. Increase harbor maintenance excise tax .....	.....	0.3	0.3	0.3	0.4	0.4	1.7
2. Modify alcohol occupational excise taxes .....	.....	( <sup>5</sup> )	( <sup>5</sup> )	( <sup>5</sup> )	( <sup>5</sup> )	( <sup>5</sup> )	( <sup>3</sup> )
<b><i>D. Employment Tax Provisions</i></b>							
1. Payroll tax deposit stabilization .....	.....	0.9	2.2	-3.1	.....	.....	.....
2. Extension of Medicare hospital insurance (HI) to all State and local government employees ( <sup>4</sup> ) .....	.....	1.7	1.7	1.7	1.7	1.6	8.4

3. Extend social security retirement coverage (OASDI) to State and local employees not in public retirement plan <sup>(4)</sup> .....	.....	2.1	2.2	2.3	2.5	2.7	11.8
4. Extend social security retirement and Medicare hospital insurance coverage (OASDHI) to D.C. employees not covered.....	.....	(5)	(5)	(5)	(5)	(5)	(3)
5. Railroad unemployment insurance fund.....	.....	(1)	(1)	.....	(1)	(1)	(3)

#### ***E. IRS Provisions***

1. Extend IRS user fees.....	.....	0.1	0.1	0.1	0.1	0.1	0.5
2. IRS management reforms.....	0.1	2.5	1.1	0.5	(1)	-0.4	3.8
3. Increase in IRS enforcement funding for FY 1991.....	.....	0.5	0.8	1.3	1.5	1.6	5.7

#### ***F. Certain User Fees Classified as Receipts***

1. Commodity Futures Trading Commission (CFTC) transaction fee.....	.....	(5)	(5)	(5)	0.1	0.1	0.2
2. Securities and Exchange Commission (SEC) transaction fees.....	(5)	0.1	0.1	0.1	0.1	0.1	0.5
3. Federal Emergency Management Agency (FEMA) user fees.....	(5)	(5)	(5)	(5)	(5)	(5)	(3)
4. Extend abandoned mine reclamation fees.....	.....	.....	0.1	0.3	0.3	0.3	1.0
5. Corps of Engineers application fees.....	.....	(5)	(5)	(5)	(5)	(5)	(3)
6. Other: HUD interstate land fee and EPA fees....	.....	-0.1	-0.2	(1)	(1)	(1)	-0.3
<b>Grand Totals.....</b>	<b>0.7</b>	<b>13.6</b>	<b>11.5</b>	<b>4.1</b>	<b>6.8</b>	<b>5.5</b>	<b>42.2</b>

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(1) Loss of less than \$50 million.

(2) Refundable tax credits involving refunds which exceed tax liability are shown as increased outlays. Outlays will increase by \$0.2 billion in FY1991, \$1.8 billion in FY1992, \$2.0 billion, in FY1993, \$2.1 billion in FY1994, and \$2.2 billion in FY1995.

(3) Totals are not available for estimates represented by footnotes.

(4) Estimate is net of income tax offset.

(5) Gain of less than \$50 million.

Source: Department of the Treasury, *General Explanations of the President's Budget Proposals Affecting Receipts*, January 1990.

