



**DESCRIPTION OF CHAIRMAN'S MODIFICATIONS TO
THE PROVISIONS OF THE "CARE ACT OF 2003"
SCHEDULED FOR A MARKUP BY THE
SENATE COMMITTEE ON FINANCE ON FEBRUARY 5, 2003¹**

A. Modifications to the CARE Act of 2003

The following modifications are made to the provisions of the CARE Act of 2003.²

1. Notification requirement for exempt entities not currently required to file an annual information return

The proposal requires certain tax-exempt organizations that are exempt from the information return (Form 990) filing requirement to file an annual notice with the Secretary of the Treasury. The penalty for failure to file the notice for three consecutive years is loss of exempt status.

The Chairman's modification extends the penalty of revocation of tax-exempt status to organizations that are required to file an information return under section 6033(a) (Form 990). Under the modification, if an organization fails to file such an information return for three consecutive years, the organization's tax-exempt status is revoked. In addition, an organization's tax-exemption is revoked if the organization fails to meet its filing obligation to the Secretary for three consecutive years in cases where the organization is subject to the information return requirement in one or more years during a three-year period and also is subject to the notice requirement for one or more years during the same three-year period.

The revocation is effective from the date that the Secretary determines was the last day the organization could have timely filed the third required information return or notice. To again be recognized as tax-exempt, the organization must apply to the Secretary for recognition of tax-

¹ This document may be cited as follows: Joint Committee on Taxation, *Description of Chairman's Modifications to the Provisions of the "CARE Act of 2003" Scheduled for a Markup By the Senate Committee on Finance on February 5, 2003* (JCX-07-03), February 5, 2003.

² A description of the provisions of the "CARE Act of 2003" is contained in Joint Committee on Taxation, *Description of the "CARE Act of 2003"* (JCX-04-03), February 3, 2003.

exemption, irrespective of whether the organization was required to make an application for recognition of tax-exemption in order to gain tax-exemption originally.

If, upon application for tax-exempt status after a revocation under the proposal, the organization shows to the satisfaction of the Secretary reasonable cause for failing to timely file the required annual returns, the organization's tax-exempt status will be reinstated retroactive to the date of revocation. An organization may not challenge under the Internal Revenue Code's declaratory judgment procedures (section 7428) a revocation of tax-exemption made pursuant to the modification. The modification does not affect an organization's obligation under present law to file required information returns or existing penalties for failure to file such returns.

In addition to the Secretary's outreach requirements described in the Chairman's mark with respect to the notice, the Secretary is required to publicize in a timely manner the requirements of the modification in appropriate forms and instructions and other means of outreach, with respect to the penalty for failure to file the information return. The Secretary is authorized to publish a list of organizations whose exempt status is revoked under the modification.

2. Suspension of tax-exempt status of terrorist organizations

The Chairman's modification clarifies that the proposal to suspend the tax-exempt status of certain terrorist organizations applies to organizations that are designated or identified as a terrorist organization prior to, on, or after the date of enactment. In addition, if an organization is designated or identified as a terrorist organization prior to the date of enactment, the suspension of the organization's tax-exemption begins from the date of enactment and is not retroactive to the date the organization is designated or identified as a terrorist organization.

3. Payments by charitable organizations to victims of war on terrorism

The Chairman's modification extends the proposal to apply to the families of astronauts killed in the line of duty. The Chairman's modification is effective for astronauts killed and payments made since January 1, 2003.

4. Revenue raising proposals

The Chairman's modification changes the effective date with respect to the clarification of the economic substance doctrine (and the related penalty for transactions that lack economic substance) to transactions after February 15, 2004.

B. New Provisions

The Chairman's modification would add the following provisions to the CARE Act of 2003:

1. Charitable contribution deduction for certain expenses in support of Native Alaskan subsistence whaling

Present Law

In computing taxable income, individuals who do not elect the standard deduction may claim itemized deductions, including a deduction (subject to certain limitations) for charitable contributions or gifts made during the taxable year to a qualified charitable organization or governmental entity.³ Individuals who elect the standard deduction may not claim a deduction for charitable contributions made during the taxable year.

No charitable contribution deduction is allowed for a contribution of services. However, unreimbursed expenditures made incident to the rendition of services to an organization, contributions to which are deductible, may constitute a deductible contribution.⁴ Specifically, section 170(j) provides that no charitable contribution deduction is allowed for traveling expenses (including amounts expended for meals and lodging) while away from home, whether paid directly or by reimbursement, unless there is no significant element of personal pleasure, recreation, or vacation in such travel.

Description of Proposal

The proposal allows individuals to claim a deduction under section 170 not exceeding \$10,000 per taxable year for certain expenses incurred in carrying out sanctioned whaling activities. The deduction would be available only to an individual who is recognized by the Alaska Eskimo Whaling Commission as a whaling captain charged with the responsibility of maintaining and carrying out sanctioned whaling activities. The deduction would be available for reasonable and necessary expenses paid by the taxpayer during the taxable year for: (1) the acquisition and maintenance of whaling boats, weapons, and gear used in sanctioned whaling activities, (2) the supplying of food for the crew and other provisions for carrying out such activities, and (3) storage and distribution of the catch from such activities.

For purposes of the provision, the term "sanctioned whaling activities" means subsistence bowhead whale hunting activities conducted pursuant to the management plan of the Alaska Eskimo Whaling Commission.

³ Sec. 170. Section references are to the Internal Revenue Code of 1986 unless otherwise indicated.

⁴ Treas. Reg. sec. 1.170A-1(g).

Effective Date

The proposal is effective for contributions made after December 31, 2003.

2. Matching grants to low-income taxpayer clinics for return preparation

Present Law

The Secretary is authorized to provide up to \$6 million per year in matching grants to certain low-income taxpayer clinics that represent low-income taxpayers in controversies with the IRS or that operate programs to inform individuals for whom English is a second language about their tax-related rights and responsibilities.⁵

Description of Proposal

The provision authorizes the Secretary to create a separate grant program to provide up to \$10 million per year in matching grants to not for profit organizations that assist low-income taxpayers in the preparation of their Federal tax returns.

Effective Date

The provision is effective on the date of enactment.

3. Extend enhanced deduction for inventory to include public schools

Present Law

Under present law, a taxpayer's deduction for charitable contributions of inventory generally is limited to the taxpayer's basis (typically, cost) in the inventory.

However, for certain contributions of inventory, C corporations may claim an enhanced deduction equal to the lesser of (1) basis plus one-half of the item's appreciated value (i.e., basis plus one half of fair market value in excess of basis) or (2) two times basis.⁶ To be eligible for the enhanced deduction, the contributed property generally must be inventory of the taxpayer, contributed to a charitable organization described in section 501(c)(3) (except for private nonoperating foundations), and the donee must (1) use the property consistent with the donee's exempt purpose solely for the care of the ill, the needy, or infants, (2) not transfer the property in exchange for money, other property, or services, and (3) provide the taxpayer a written statement that the donee's use of the property will be consistent with such requirements. In the case of contributed property subject to the Federal Food, Drug, and Cosmetic Act, the property must satisfy the applicable requirements of such Act on the date of transfer and for 180 days prior to the transfer.

⁵ Sec. 7526.

⁶ Sec. 170(e)(3). In general, a C corporation's charitable contribution deductions for a year may not exceed 10 percent of the corporation's taxable income. Sec. 170(b)(2).

Donations to educational organizations described in section 170(b)(1)(A)(ii) are not eligible to receive the enhanced deduction. An organization is described in section 170(b)(1)(A)(ii) if it 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 regularly carried on. Donations to such organizations are eligible to receive an enhanced deduction if the donation qualifies as a qualified computer contribution.⁷

Description of Proposal

The proposal would extend the enhanced deduction for inventory property to donations to educational organizations described in section 170(b)(1)(A)(ii). Charitable contributions of computer technology and equipment continue to be covered by the present law enhanced deduction of section 170(e)(6) and are not eligible property for an enhanced deduction under the proposal.

The proposal retains present law requirements that the donated property be used solely for the care of the ill, the needy, or infants, (2) that the organization not transfer the property in exchange for money, other property, or services, and (3) that the organization provide the taxpayer a written statement that the donee's use of the property will be consistent with such requirements.

Effective Date

The proposal is effective for contributions made after December 31, 2003.

⁷ Sec. 170(e)(6).