[JOINT COMMITTEE PRINT]

DESCRIPTION OF TAX BILLS (H.R. 3139, H.R. 3301, H.R. 4056, H.R. 4077, H.R. 4379, and H.R. 4595)

SCHEDULED FOR A HEARING

BEFORE THE

SUBCOMMITTEE ON SELECT REVENUE MEASURES

OF THE

COMMITTEE ON WAYS AND MEANS

ON MAY 19, 1986

PREPARED BY THE STAFF

OF THE

JOINT COMMITTEE ON TAXATION

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INTRODUCTION

The bills described in this pamphlet [1] have been scheduled for a public hearing on May 19, 1986, by the Subcommittee on Select Revenue Measures of the House Committee on Ways and Means.

The six bills scheduled for the hearing are: (1) H.R. 3139 (exemption of certain emergency medical helicopter transportation from air transportation excise taxes); (2) H.R. 3301 (exemption for corporations or trusts that acquire and manage real property for certain exempt organizations); (3) H.R. 4056 (disallowance of foreign earned income exclusion for individuals who are in foreign countries in violation of an Executive Order); (4) H.R. 4077 (denial of tax exemption for interest on certain electric utility bonds); (5) H.R. 4379 (nonrecognition of gain on sale of principal residence where one spouse dies before occupying new residence); and (6) H.R. 4595 (tax rules relating to limited profit housing cooperatives).

The first part of the pamphlet is a summary of the bills. The second part provides a more detailed description of the bills, including present law, explanation of provisions, and effective dates.

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[1] This pamphlet may be cited as follows: Joint Committee on Taxation, *Description of Tax Bills (H.R. 3139, H.R. 3301, H.R. 4056, H.R. 4077, H.R. 4379, and H.R. 4595)* (JCS-11-86), May 16, 1986.

I. SUMMARY

1. H.R. 3139—Mrs. Kennelly and others

Exempt Certain Emergency Medical Helicopter Transportation From Air Transportation Excise Taxes

The bill would exempt certain emergency medical helicopter transportation from the 8-percent excise tax on domestic air passengers and the 5-percent excise on domestic air cargo.

To qualify for exemption, the helicopter must be used primarily for purposes of providing emergency medical services, must be owned or leased by a nonprofit health care facility, and must be operated exclusively under the control of the facility. Also, the exemption would apply only if the helicopter does not use facilities eligible for assistance under the Airport and Airway Development Act of 1970 or services provided under the Airport and Airway System Improvement Act of 1982.

The bill would apply retroactively to transportation beginning after January 1, 1985.

2. H.R. 3301—Messrs. Matsui and Archer

Tax-Exempt Status for Corporations or Trusts that Acquire and Manage Real Property for Certain Exempt Organizations

The bill would provide tax-exempt status for a corporation or trust that is organized for the exclusive purposes of acquiring and holding title to real property, collecting income from the real property, and remitting the income to certain tax-exempt organizations. A trust that meets all of the requirements of these title holding corporations would also be entitled to use the exception from the debt-financed property rules for real property, if certain other requirements are met.

Tax-exempt organizations eligible to hold interests in a title holding corporation would include (1) a qualified pension, profit-sharing, or stock bonus plan, (2) a governmental pension plan, (3) the United States, or any State or political subdivision, or (4) any charitable organization described in section 501(c)(3).

The bill would apply retroactively to taxable years beginning after December 31, 1984.

3. H.R. 4056—Messrs. Archer, Daub, Downey, Heftel, Gregg, Schulze, Vander Jagt, and others

Disallowance of Foreign Earned Incomme Exclusion for Individuals Who Are in a Foreign Country in Violation of an Executive Order

Under Code section 911, an individual may exclude up to $80,000 in foreign earned income from U.S. income tax. For periods after January 31, 1986, the bill would deny this foreign earned income exclusion for individuals present in a foreign country in violation of an Executive Order. These countries currently are North Korea, Cuba, Vietnam, Cambodia, Iran, and Libya.

4. H.R. 4077—Mr. Torricelli

Denial of Tax Exemption for Interest on Certain Electric Utility Bonds

In general, facilities for municipally owned and operated electric utilities qualify for tax-exempt financing as governmental activities.

The bill would deny tax exemption for interest on bonds to finance facilities for electric utilities which are in arrears under certain take or pay agreements involving the Washington Public Power Supply System. These agreements involve electricity which was to be generated by two planned (but unconstructed) nuclear generating facilities.

The bill would apply to obligations issued after the date of enactment and with respect to interest payable on bonds during periods when a purchasing utility was in default under the agreements.

5. H.R. 4379—Mr. Jenkins

Nonrecognition of Gain on Sale of Principal Residence Where One Spouse Dies Before Occupying New Residence

Taxpayers may defer recognition of gain on the sale of their principal residence if they purchase a new principal residence within a specified period and meet other qualifications. One such qualification is that both spouses must file a consent to allow the application of this provision on the sale of their principal place of residence.

The bill would provide that in the event one spouse dies after the date of the sale of the old residence but before the purchase of the new residence, the deceased spouse would be deemed to consent to the application of this provision to the sale. Also, the requirement that both spouses must use the new residence as their principal place of residence would not apply.

The bill would apply retroactively to sales and exchanges of old residences after December 31, 1984.

6. H.R. 4595—Mr. Rangel

Tax Rules Relating Relating to Limited Profit Housing Cooperatives

The bill would provide that earnings of the reserve fund of a limited-profit housing cooperative would be treated as income derived from members for taxable years beginning before January 1, 1986. The bill also would provide that the creation of a reserve fund or the payment of closing costs for such a cooperative in connection with certain mortgage refinancings does not constitute income for the cooperative.

Further, the bill would provide that certain deductions claimed by certain cooperatives would be treated as paid by those cooperatives.

II. DESCRIPTION OF THE BILLS

1. H.R. 3139—Mrs. Kennelly and others

Exempt Certain Emergency Medical Helicopter Transportation From Air Transportation Excise Taxes

Present Law

An excise tax of 8 percent is imposed on the payment for air transportation of any person that begins and ends in the United States (Code sec. 4261). The tax is paid by the person who pays for the transportation. Revenues from this tax go into the Airport and Airway Trust Fund.

Exemptions from the air passenger tax apply for helicopter transportation of individuals, equipment, or supplies in connection with certain mining, oil, or gas exploration and certain timber or logging activities. These exemptions apply only if the helicopter neither takes off from, nor lands at, a facility eligible for assistance under the Airport and Airway Development Act of 1970, nor uses services provided under the Airport and Airway Improvement Act of 1982 (sec. 4261(e)).[2]

A 5-percent excise tax is imposed on the cost of air transportation of property within the United States (sec. 4271). Revenues from this tax go into the Airport and Airway Trust Fund.

The taxes on air passenger and air cargo transportation do not apply to small aircraft (having a maximum certificated take-off weight of 6,000 pounds or less) not operating on an established line (sec. 4281).[3]

Explanation of the Bill

The bill would provide an exemption from the tax on air passenger transportation by helicopter for certain emergency medical transportation.

The exemption would apply if the helicopter—

(1) is used primarily for purposes of providing emergency medical services,

(2) is owned or leased by a nonprofit health care facility and is operated exclusively under the control of the facility,

(3) does not take-off from, or land at, a facility eligible for assistance under the Airport and Airway Development Act of 1970, and

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[2] Section 4041(l) also exempts such helicopter transportation from the excise taxes on noncommercial aviation fuels (12 cents per gallon for gasoline and 14 cents per gallon for nongasoline fuels).

[3] Such small aircraft, unless meeting the above helicopter exemption requirements, are subject to the excise taxes on noncommercial aviation fuels.

(4) does not otherwise use services provided under the Airport and Airway System Improvement Act of 1982 during such transportation.

The bill also would exempt emergency medical transportation, as defined above, from the 5-percent tax on the air transportation of property under section 4271.

Effective Date

The bill would apply retroactively to transportation that begins after January 1, 1985.

2. H.R. 3301—Messrs. Matsui and Archer

Tax-Exempt Status for Corporations or Trusts that Acquire and Manage Real Property for Certain Exempt Organizations

Present Law

Under present law, a corporation that is organized for the exclusive purpose of holding title to property, collecting income therefrom, and distributing the income (less expenses) to a tax-exempt organization is itself exempt from Federal income tax (sec. 501(c)(2)). Present law is unclear whether an exempt title holding company may have more than one unrelated parent. The Internal Revenue Service has taken the position, in a General Counsel Memorandum (G.C.M. 37351, December 20, 1977), that in order to qualify for tax-exempt status, a title holding corporation may distribute income only to one or more related tax-exempt organizations.

Explanation of the Bill

The bill would add a new category of section 501(c) tax-exempt organizations to apply to certain corporations or trusts that are organized for the exclusive purposes of acquiring and holding title to property, collecting income from the property, and remitting the income to certain tax-exempt organizations. Tax-exempt status in this category would apply only if the corporation or trust (1) has no more than 35 shareholders or beneficiaries, (2) has only one class of stock or beneficial interest, and (3) is organized for the exclusive purpose of acquiring property and holding title to, and collecting income from, such property, and remitting the entire amount of income from such property (less expenses) to one or more eligible tax-exempt organizations which are shareholders or beneficiaries of such corporation or trust.

A corporation or trust that meets all of these requirements would also be entitled to use the exception to the tax on unrelated business income under the debt-financed property rules for real property (sec. 514(c)(9)).

In order to qualify for exemption under the new category, a title-holding company would be required to permit its shareholders or beneficiaries (1) to dismiss, after reasonable notice, the corporation's or trust's investment advisor by majority vote of the shareholders or beneficiaries and (2) to terminate their interest by either (a) selling or exchanging their stock or beneficial interest (subject to Federal or State securities law) to any other eligible organization as long as such sale or exchange would not increase the total number of shareholders or beneficiaries to more than 35, or (b) redeeming their stock or beneficial interest after providing 90 days notice to the corporation or trust.

Tax-exempt organizations eligible to hold interests in a title holding corporation would include (1) a qualified pension, profit-sharing, or stock bonus plan (sec. 401(a)); (2) a governmental pension plan (sec. 414(d)); (3) the United States, States or political subdivision, or governmental agencies or instrumentalities; and (4) tax-exempt charitable, educational, religious, etc. organizations described in section 501(c)(3).

The bill would not change present law with respect to title holding organizations (described in sec. 501(c)(2)) holding title to property for one or more tax-exempt organizations.

Effective Date

The bill would be effective retroactively for taxable years beginning after December 31, 1984.

3. H.R. 4056—Messrs. Archer, Daub, Downey, Heftel, Gregg, Schulze, Vander Jagt, and others

Disallowance of Foreign Earned Income Exclusion for Individuals Who are in a Foreign Country in Violation of an Executive Order

Present Law

Under Code section 911, an individual whose tax home is in a foreign country and who either is present overseas for 330 days out of any 12 consecutive months or is a bona fide resident of a foreign country for an entire taxable year can elect to exclude an amount of foreign earned income from gross income. The maximum exclusion is $80,000 in 1986, and is scheduled to increase to $85,000 in 1988, $90,000 in 1989, and to $95,000 in 1990 and thereafter.[4]

An individual meeting the eligibility requirements may also elect to exclude housing costs above a floor amount. The combined earned income exclusion and housing amount exclusion may not exceed the taxpayer's total foreign earned income for the taxable year.

Explanation of the Bill

The bill would provide that individuals who are present in a foreign country in violation of an Executive Order would lose certain tax benefits, as described below. An individual who is present in a foreign country where U.S. citizens and residents generally are prohibited from being present would not lose tax benefits unless that individual's presence violates the Executive Order.

Under the bill, an individual would not be treated as a bona fide resident of, or as present in, a foreign country for any day during

[4] The House-passed Tax Reform Act of 1985 (H.R. 3838) would reduce the maximum exclusion to $75,000 permanently, for taxable years beginning after 1985.

which the individual was present in a country in violation of an Executive Order. Foreign earned income, otherwise eligible for the exclusion, would not include any income from sources within that country attributable to services performed during a period when such an Executive Order was in effect. Housing expenses eligible for tax benefits would not include any expenses (allocable to a period in which presence was prohibited) for housing in such a country or for housing of the spouse or dependents of the taxpayer in another country while the taxpayer is present in such a country.

It is understood that the presence of U.S. citizens and residents in six countries has been generally prohibited currently by Executive Order. These countries are North Korea, Cuba, Vietnam, Cambodia, Iran, and Libya. In certain cases, exceptions to these prohibitions are available. For instance, in certain cases, American individuals may be present in one of these countries to visit close family members, to engage in journalistic activity, or to perform research. The Executive Order prohibiting travel to Libya, for example, prohibits presence in Libya after January 31, 1986, unless necessary to effect the individual's departure from Libya or for journalistic activity by persons regularly employed in such capacity by a newsgathering organization.

Accordingly, the bill would, for example, deny tax benefits to U.S. persons present in Libya in violation of the January 31, 1986, Executive Order to work for an oil company. The bill would not, however, deny tax benefits to U.S. persons present in Libya to report news for a newspaper or television network, because such persons would not be present there in violation of the Order.

Effective Date

The bill would be retroactively effective for periods after January 31, 1986.

4. H.R. 4077—Mr. Torricelli

Denial of Tax Exemption for Interest on Certain Electric Utility Bonds

Present Law

Interest on State and local government obligations generally is exempt from Federal income tax. However, since 1968, tax exemption generally has been denied to State and local government issues of industrial development bonds (IDBs). A State or local government bond is an IDB if (1) all or a major portion of the proceeds of the issue is to be used in any trade or business of a person other than a State or local government or tax-exempt organization and (2) payment of principal or interest is secured by an interest in, or derived from payments with respect to, property or borrowed money used in a trade or business. Interest on IDBs is tax-exempt only if the bonds are issued for specific exempt activities, are for industrial parks, or are small-issue IDBs.[5] Present law also re-

[5] H.R. 3838 (the Tax Reform Act of 1985), as passed by the House in December 1985, would repeal the exception for certain types of IDBs and make various other changes to the rules regarding tax-exempt bonds.

stricts tax-exemption for private loan bonds, defined as bonds 5 percent or more of the proceeds of which are reasonably expected to be used (directly or indirectly) to make or finance loans to nonexempt persons.

In general, electric utilities that are owned and operated by State or local governments and that serve the general public are eligible for tax-exempt financing as governmental activities (rather than a private trade or business use).

Explanation of the Bill

The bill would deny tax exemption for interest on obligations used to provide property for use by any electric utility, if the utility is in arrears under an agreement to take or pay for electricity which was to be generated by certain planned (but unconstructed) nuclear generating facilities. (The affected obligations need not relate directly to the take or pay agreement.)

The bill would apply to bonds used to provide property for any electric utility if:

(1) The utility (or a predecessor utility) was one of 88 utilities which entered into agreements during 1974 (with a corporation incorporated in 1957) for purpose of constructing five nuclear electric generating facilities;

(2) Only one of the five facilities was constructed; and

(3) The utility (or a predecessor utility) entered into an agreement to take or pay for certain amounts of electricity to be generated by either of two of the specified facilities which were not constructed.

For purposes of determining the amount of payments which is in arrears under these agreements, an agreement would be treated as binding and would be construed as if electricity were generated by (and available for purchase from) the generating facility involved.

While the bill would apply to any obligations which meet the criteria described above, the principal utilities affected by the provisions would be those utilities that contracted with the Washington Public Power Supply System for the purchase of power from planned nuclear generating units 4 and 5 of that system.

Effective Date

The bill would apply to obligations issued after the date of enactment and with respect to interest payable on bonds during periods when a purchasing utility was in default under the agreements described.

5. H.R. 4379—Mr. Jenkins

Nonrecognition of Gain on Sale of Principal Residence Where One Spouse Dies Before Occupying New Residence

Background and Present Law

Present law provides for the nonrecognition, or "rollover," of gain on the sale of a taxpayer's principal residence, if a new principal residence is purchased and used by the taxpayer within a specified period beginning before, and ending after, the date of sale

(Code sec. 1034). This rule applies only to the extent that the purchase price of the replacement residence equals or exceeds the sale price of the residence sold. The replacement period begins two years before the sale and ends two years after the sale. Thus, a taxpayer may roll over gain on the sale of a principal residence if he or she purchases and uses a new principal residence within a period beginning two years before, and ending two years after, the sale.

Currently, when taxpayers qualify for nonrecognition treatment of the gain on the sale of their principal residence, their basis in the new residence is reduced by the amount of gain which is not recognized due to the application of the rollover provision. Therefore, on the subsequent sale of the new residence, the gain previously deferred generally will be recognized. In the case of a husband and wife, to qualify for this deferral, present law requires that both spouses file a consent to the basis reduction in the new principal place of residence and that both spouses use the new residence as their principal place of residence.

Explanation of the Bill

The bill would provide that if one spouse dies after the date of sale of the old residence but before the date of the purchase of the new residence by the surviving spouse, the deceased spouse shall be treated as having consented to the application of the rollover provision to the new residence. Also, the requirement that married taxpayers must use the new residence as their principal residence would be satisfied where the surviving spouse uses the new residence as his or her principal residence.

Effective Date

The bill would apply retroactively to sales and exchanges of old residences after December 31, 1984.

6. H.R. 4595—Mr. Rangel

Tax Rules Relating to Limited Profit Housing Cooperatives

Present Law

Under present law (Code sec. 216), a tenant-stockholder in a cooperative housing corporation is entitled to deduct amounts paid or accrued to the cooperative to the extent such amounts represent the tenant-stockholder's proportionate share of (1) real estate taxes allowable as a deduction to the cooperative which are paid or incurred by the cooperative with respect to the cooperative's land or buildings, and (2) interest allowable as a deduction to the corporation, paid or incurred by the corporation with respect to indebtedness contracted in the acquisition of the cooperative's land or in the acquisition, construction, rehabilitation, etc. of the cooperative's buildings. The tenant-stockholder's proportionate share is that portion of the cooperative's interest and taxes that bears the same ratio to the cooperative's total expenses for interest and taxes that the portion of the cooperative's stock held by the tenant-stockholder bears to the total outstanding stock of the cooperative.

In general, a cooperative housing corporation is a corporation (1) that has one class of stock, (2) each of the stockholders of which is entitled, solely by reason of ownership of stock, to occupy a dwelling owned or leased by the cooperative, (3) no stockholder of which is entitled to receive any distribution not out of earnings and profits of the cooperative, except on a complete or partial liquidation of the cooperative, and (4) 80 percent or more of the gross income for the taxable year of which is derived from tenant-stockholders. A tenant-stockholder generally is an individual owning fully paid up stock in the cooperative corporation, the purchase price of which bears a reasonable relationship to the value of the cooperative's equity in its land and buildings which is attributable to the dwelling unit that the individual is entitled to occupy.

Under section 277, deductions attributable to providing services or goods to members of a cooperative organization are allowed only to the extent of income derived from members. Section 277 has been held to apply to cooperative housing corporations.[6] The Internal Revenue Service takes the position that interest on a cooperative housing corporation's reserve fund does not constitute income derived from members.

Explanation of the Bill

Under the bill, income derived from the reserve fund of a limited profit cooperative housing corporation [7] is treated as derived from its members for the purposes of section 216 and section 277. In addition, any amount of interest claimed by such a cooperative with respect to a second mortgage loan made by a city housing development corporation and reported before April 16, 1986, by such a cooperative to its tenant-stockholders would be treated as having been paid by the cooperative.

The bill also provides that the payment of closing costs or the creation of certain reserve funds in connection with certain refinancings of a first mortgage of such a cooperative prior to January 1, 1984 would not be treated as taxable income to the cooperative, but that the basis of property acquired after December 31, 1985 with untaxed amounts in the reserve fund would be zero.

Effective Date

The bill generally would be effective for taxable years beginning before January 1, 1986.

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[6] *Shore Drive Apts., Inc.* v. *U.S.*, 76–2 U.S.T.C. para. 9808, (M.D. Fla. 1976). See also, Joint Committee on Taxation, *General Explanation of the Tax Reform Act of 1976* (JCS–33–76), December 29, 1976, p. 603.

[7] A limited profit housing cooperative is a housing cooperative for which the resale price of its shares is limited to the seller's basis in the stock plus the seller's proportionate share of the amortization of the corporation's indebtedness on its property.

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