NOTE: JCX-73-89 reflects a possible conference agreement on the revenue provisions of H.R. 3299, as presented to the conferees 11:00 p.m. November 17, 1989. This document does not reflect actions of the conferees after that time.

JCX-73-89
November 17, 1989
11:00 p.m.

POSSIBLE CONFERENCE AGREEMENT ON REVENUE PROVISIONS OF H.R. 3299

This document is keyed to the spreadsheet, JCS-18A-89, and the revenue table, JCX-70-89.

Identical Provisions

The conference agreement includes the identical provisions listed on p. III of the spreadsheet (JCS-18A-89).

Non-Identical Provisions

A. Corporate Provisions

1. Treatment of distributions by certain corporations filing consolidated returns--House recedes with modifications.

   Instead of denying the dividends received deduction, the agreement provides that the group must compute its tax without permitting income distributed on section 1504(a)(4) stock of a subsidiary to be offset by losses or credits (including foreign tax credits) of other group members. Other modifications are made to the manner in which the offsets are computed.

   The effective date follows the Senate amendment except that November 17, 1989 is substituted for October 2, 1989 and transition is provided for auction rate preferred stock issued no later than 30 days after enactment of the provision if the issuing subsidiary was incorporated and a rating agency retained for the purpose of issuing such stock prior to July 10, 1989.

2. Treatment of certain high-yield original issue discount (OID) obligations--House recedes with modification. Interest in excess of 6 points over AFR on instruments described in the Senate Amendment (certain long-term instruments with interest exceeding 5 points over AFR) is treated as an equity distribution for certain purposes. It is nondeductible to the issuer and is eligible for the dividends received deduction to the holder.

3. Limit nonrecognition treatment in certain section 351 transactions--House recedes with technical correction deleting exceptions for exchanges in pursuance of a plan of reorganization and transactions to which section 355

applies.

4. Regulated investment companies (RICs)

a. Mutual fund load charge--Senate recedes with an amendment providing that the holding period is 90 days.

b. Inclusion of dividends by mutual funds--House recedes with an amendment providing that dividends on stock held on the record date are includible in income on the later of the ex-dividend date or the date of acquisition.

5. Reduce built-in gain or loss threshold of sections 382 and 384--Senate recedes, with the following modifications. The provision is generally effective for ownership changes and acquisitions after October 2, 1989. The provision does not apply to any ownership change or acquisition pursuant to a written binding contract in effect on October 2, 1989, and at all times thereafter. The provision does not apply to any ownership change or acquisition of a corporation resulting from a bankruptcy reorganization of such corporation if the petition was filed with the court before October 3, 1989. In addition, the provision does not apply to any built-in losses of non-bankrupt subsidiaries of a parent company which files bankruptcy before the effective date of the provision if such subsidiaries are disposed of within 2 years of the filing of the bankruptcy petition.

6. Require Treasury study of "debt versus equity" and integration issues--House recedes.

7. Limit interest deductions for earnings-stripping payments to related tax-exempt parties--Senate recedes with modification to the definition of adjusted taxable income; modification to apply look-thru treatment to a partnership if all tax-exempt partners own less than 10 percent of the partnership; modifications to allow debt-equity safe harbor, carryforward of limitation in excess of net interest, and some alteration of mechanical rules by regulation; and clarification of the treatment of guarantees.

8. Exempt from corporate-level tax certain distributions made by cooperative housing corporations--House recedes.

9. Modify treatment of safe-harbor leases entered into by rural electric cooperatives--House recedes.

B. <u>Employee Benefit Provisions</u>

1. Repeal section 89 and reinstate prior law--House recedes. Provisions similar to those of the House bill

were included in Public Law No. 101-140, providing for an increase in the public debt.

2. Employee Stock Ownership Plans (ESOPs)

a. Partial interest exclusion for ESOP loans--Follow House Bill and Senate Amendment with the following modifications. Substitute "more than 50%" for 30% under House Bill. House recedes with respect to Revenue Ruling 89-76. With respect to plans that meet the 30-percent requirement of the House Bill, but do not meet the more than 50-percent requirement, the provision is effective with respect to loans made after November 17, 1989, other than loans pursuant to a binding loan commitment or a binding contract to acquire employer securities in effect on such date.

b. Deduction for dividends paid on employer securities held by an ESOP (section 404(k))--House recedes, except with respect to the provision providing that dividends used to repay an acquisition loan are deductible only with respect to dividends on employer securities acquired with the loan. The provision is modified by substituting August 4, 1989, for July 10, 1989 in the effective date.

c. ESOP holding period requirement (sec. 1042)--Senate recedes.

d. Repeal special ESOP contribution limit (section 415(c)(6))--Senate recedes.

e. Repeal of estate tax liability assumption (sec. 2210)--Senate recedes.

f. Repeal ESOP/estate tax deduction (sec. 2057)--Senate recedes, effective for decedents dying after date of enactment.

g. Special ESOP net operating loss rule (sec. 382(l)(3)(C))--Senate recedes.

3. Modification of full funding limitation--House recedes.

4. Permit limited use of excess pension funds to pay current retiree health benefits--House recedes.

5. Limit contributions to section 401(h) accounts--House recedes with transition relief with respect to contributions made on or before December 31, 1989, for plans that have received IRS rulings and letters prior to October 3, 1989, with respect to funding of the section 401(h) account.

6. Modify rules affecting lump-sum distributions by certain pension plans--House recedes.

C. <u>Foreign Provisions</u>

1. Conform tax years of controlled foreign corporations--House recedes.

2. Improve information reporting by U.S. subsidiaries and branches of foreign corporations--House recedes with modifications regarding judicial review of substantial compliance with a summons and the exposure of persons and documents to nontax legal process while required by a summons to be present in the U.S.; and clarifications regarding the location where records may be required to be maintained, the use of summonses to obtain testimony of employees of foreign related parties, the scope of judicial review of the Secretary's discretion in the event of noncompliance, and the consistency of the provision with U.S. treaty obligations.

3. Tax stock gains of certain foreign persons--House recedes.

4. Repeal transition rule for certain high withholding tax interest--Senate recedes with modification under which repeal of the transition rule would not apply to a taxpayer, any of whose published financial statements as of dates from March 31, 1989 to December 31, 1989 reflect that it has loss reserves against its portfolio of Baker 33 country loans (other than reserves which are based on expected future tax benefits from the write off of such loans) of at least 25 percent.

5. Deny expensing for certain R&D not performed in the United States--House recedes.

6. Modify interest allocation rules for foreign tax credit limitation purposes for certain financial services companies--House recedes.

7. Treat certain foreign corporate dividends and deemed income inclusions as unrelated business taxable income--House recedes.

8. Exclude certain overseas allowances received by certain Department of Defense personnel--House recedes.

D. <u>Excise Tax Provisions</u>

1. Aviation excise taxes

   a. Suspend Airport-Airway trigger--Senate recedes.

b. Collection period for airline ticket tax--Senate recedes.

c. Increase air passenger international departure tax--House recedes.

d. Impose air passenger international departure fee--Senate recedes.

2. Cruise ship passenger international departure taxes/fee

Departure tax--House recedes.

Departure fee--Senate recedes.

3. Oil Spill Liability Trust Fund and Taxes

Senate recedes on level of tax (5 cents) and cap on the fund balance ($1 billion, inclusive of transfers from other funds and interest on the trust fund), with tax reinstated if fund falls below $1 billion. Modifications made to expenditure purposes.

4. Excise tax on ozone depleting chemicals

Fee and related items--Senate recedes.

CFC tax--The agreement generally follows the Senate amendment but modifies the base tax rate to be $1.37 per pound in both 1990 and 1991, $1.67 per pound in 1992, and $2.65 per pound in both 1993 and 1994. In each year after 1994 the base rate will increase by 45 cents per pound.

5. Telephone excise tax

a. Extension of tax--House recedes.

b. Modify collection period of tax--House recedes.

c. Exemption certificates--House recedes.

6. Collection of gasoline excise tax

a. Impose gasoline excise tax on arrival at terminal--House recedes.

b. Acceleration of gasoline excise tax deposits--House recedes.

7. Eliminate the excise tax imposed on the Inactivated Polio Vaccine--House recedes.

8. Modify taxation of bulk cigar imports--House recedes.

E. Like-Kind Exchanges

House recedes, except that foreign real property and U.S. real property are not like-kind property.

F. Accounting Provisions

1. Repeal of the completed contract method of accounting.--Senate recedes with the modification that a taxpayer may elect not to recognize income under a long-term contract and not to take into account any costs allocable to such long-term contract until the taxable year as of the end of which at least 10 percent of the estimated total contract costs have been incurred.

2. Modify treatment of costs of acquiring franchises, trademarks, and trade names.--House recedes with the modification that a taxpayer may elect to amortize certain fixed-sum payments and contingent payments that are chargeable to capital account and that are part of the same transaction (or series of related transactions) over a 25-year period that begins with the taxable year in which the transfer occurs.

3. Adjust regular and alternative minimum tax treatment of installment sales of timeshares and residential lots of C corporations--House recedes.

G. Employment Tax Provisions

Payroll tax speedup--$100,000 threshold.

H. Miscellaneous Provisions

1. Limit section 104 exclusion for personal injury--Senate recedes with respect to nonphysical punitive damages. House recedes with respect to actual damages.

2. Tax pre-contribution gain on certain in-kind partnership distributions--House recedes with modification to substitute 5-year for 3-year distribution period.

3. Cellular telephone depreciation--Senate recedes with modifications.

4. Repeal amortization of life estate in related-party joint purchases--Senate recedes with an amendment exempting term interests held by tax-exempt persons and certain other technical changes, including an amendment allowing the term holder a full depreciation deduction for the underlying property.

5. Require reporting of mortgage points by lender--Senate

recedes with modification that the provision would be effective for returns due on or after January 1, 1992.

6. Codify tax exemption for Overseas Private Investment Corporation--House recedes.

7. Permit use of tax return information by Department of Veterans Affairs--House recedes.

8. Require IRS to provide notice of certain amounts withheld--House recedes.

9. Modify treatment of investment-oriented life insurance contracts--Senate recedes.

10. Increase Joint Committee on Taxation refund review threshold to $1 million--House recedes.

11. Require Treasury study of IRS private letter ruling process--House recedes.

12. Provide for nonrecognition of capital gains on divestiture of property--House recedes.

13. Recapture of bad-debt reserves of mutual savings banks and other thrift institutions--Senate recedes.

14. Modify treatment of certain timber activities under the passive loss rules--House recedes.

15. Rehabilitation tax credit

    a. Modify rehabilitation tax credit under passive loss rule--House recedes.

    b. Treat certain relocated buildings as qualifying property--House recedes.

I. <u>Tax-Exempt</u> <u>Bond</u> <u>Provisions</u>

1. Allow use of multifamily residential rental bonds for transitional housing--House recedes.

2. Allow issuers of certain qualified mortgage bonds additional time to elect to rebate arbitrage--House recedes.

3. Impose restrictions on hedge bonds--The conference agreement follows the House bill with modifications; (1) the reasonable expectation of actual expenditures is modified to: 10 percent by the end of year 1, 30 percent by the end of year 2, 60 percent by the end of year 3 and 85 percent by the end of year 5; (2) Treasury Authority to issue guidance on self insurance bonds is

deleted; (3) the definition of hedge bonds is modified to exclude issues substantially all the proceeds of which are invested in non-AMT tax-exempts; (4) the refunding rules are modified; and (5) other modifications.

4. Expand 6-month exception to tax-exempt bond arbitrage rebate rules--The agreement generally follows the House bill with a modification to the expenditure requirements. The new requirements are that at least 10 percent of proceeds be expended within 6 months, 45 percent within 12 months, 75 percent within 18 months, 95 percent within 24 months, and 100 percent within 36 months. Should the requirements not be satisfied, the issuer may elect, at time of issue, to rebate arbitrage or pay a penalty equal to 3 percent of the difference between the unexpended proceeds and the required expenditure amount. Additional modifications were also made.

5. Modify placed-in-service date for certain tax-exempt bond-financed property--House recedes.

J. <u>Corporate Alternative Minimum Tax</u>

Senate recedes.

K. <u>Extension of Expiring Provisions</u>

Senate recedes with the following modifications: (a) all expiring provisions are extended through 1990 (except the section 861 allocation rule, which is extended for the taxpayer's first taxable year beginning after August 1, 1989, for a single 12-month period); (b) add the exclusion for employer provided group legal services (secs. 120 and 501(c)(20)); (c) add solar and ocean thermal business energy credits; and (d) make the following modifications to the low income housing credit and the research and experimentation credit.

1. **Low-income rental housing tax credit**

The Senate Amendment contains no provision for the extension or modification of the low income housing tax credit. However, the Finance Committee amendment to the Revenue Reconciliation bill did contain certain provisions which were agreed to by the conference committee.

a. Extension of credit

The conference agreement extends the credit for one year, through December 31, 1990.

b. Carryover of credit authority

The Conference agreement follows the House bill, with an amendment which increases an allocating agency's credit volume cap by the amount of credit previously allocated to a project that does not become a qualified low-income housing project within specified time limits. In addition, any authority unused, by the allocating agency, after the one-year carryforward provided in the House bill, is reallocated to other States through a national pool of unused authority.

c. Payment of credit

The conference agreement does not include the House bill provision.

d. Credit recapture

The conference agreement does not include the House bill provision.

e. Extended low-income use and rights of first refusal

The conference agreement follows the House bill on extended low-income use, with an amendment in the nature of a substitute which makes a 30-year extended low-income use agreement a requirement for credit eligibility. If the taxpayer is unable to transfer property at the end of the initial compliance period for continued low-income use, the allocating agency is allowed one year (beginning at the end of the 14th year of compliance period) to find an eligible buyer at a specified price based on outstanding indebtedness and investor equity contributions. If no such buyer is located, the property may be converted to market rate use with the qualification that existing low-income tenants may not be evicted within three years after the end of the compliance period. The conference agreement follows the House bill on rights of first refusal.

f. Allowance of credit for acquisition of existing property and substantial rehabilitation

The conference agreement follows the House bill.

(1) <u>Minimum qualifying expenditure</u>

The conference agreement follows the House bill.

(2) <u>Exception for buildings owned by governmental units</u>

The conference agreement follows the House bill.

g. Passive loss restriction on credit use

The conference agreement follows the House bill.

h. Tax-exempt bond financed property: Annual credit limitation

The conference agreement follows the House bill.

i. High-cost areas

The conference agreement follows the House bill with respect to high-cost areas, with a modification that extends the authority of the Secretary of HUD to designate as difficult to develop areas certain qualified census tracts. Within such qualified census tracts, the eligible basis of a new building or the eligible basis of rehabilitation expenditures in the case of an existing building undergoing substantial rehabilitation is deemed to be 130 percent of eligible basis claimed for depreciation, as is the case for high cost areas.

A qualified census tract is any census tract of a metropolitan statistical area in which 50 percent or more of the households have an income which is less than 60 percent of the area median gross income. No more than 20 percent of the population of a metropolitan statistical area may be designed as satisfying the requirements of a qualified census tract.

j. 10-year rule

The conference agreement follows the House bill.

k. Credit and HUD section 8 programs

The conference agreement follows the House bill, with an amendment that denies any credit to property receiving assistance under the HUD Section 8 mod rehab program.

l. Compliance with local building and health regulations

The conference agreement follows the House bill.

m. Single room occupancy units, transitional housing for the homeless

The conference agreement follows the House bill, with an amendment to clarify that month-to-month leases do not disqualify single room occupancy units for the credit.

n. Four-unit, owner-occupied structures

The conference agreement follows the House bill.

o. Special needs services

The conference agreement amends the definition of gross rent to exclude certain fees for supportive services which are paid to the owner of the unit by a government program or 501(c)(3) organization under a program which provides assistance to low-income individuals.

p. Scattered site projects

The conference agreement follows the House bill.

q. Credits allocated to projects

The conference agreement follows the House bill. The conferees intend that each building will still be assigned a separate building identification number (B.I.N.) and a separate Form 8609.

r. Determination of eligible basis

The conference agreement follows the House bill, with an amendment to make the provision relating to determination of eligible basis effective as if included in the Tax Reform Act of 1986. The conference agreement follows the House bill on the treatment of HUD Community Development Block Grants.

s. Determination of rent for rent-restricted units

The conference agreement follows the House bill.

t. Rent floors

The conference agreement follows the House bill provision.

u. Rents for previously qualifying tenants whose incomes now exceed the qualifying income limitations

The House recedes and accepts an amendment providing that when the income of a tenant in a qualified rent restricted unit exceeds 140 percent of the qualifying income limitation that unit continue to be a qualified low-income unit, but the rent restriction under the credit will continue to apply until the tenant vacates the unit.

v. Determination of gross income

The conference agreement follows the House bill.

w. Deep rent skewing

The conference agreement follows the House bill.

x. At-risk rule for qualified nonprofit organizations

The conference agreement expands the present law at-risk rules for property financed by qualified nonprofit organizations by delaying the deadline for full repayment of such financing to conform to extended use period (described in K.1.e., above).

y. State plans

The conference agreement follows the House Bill.

z. Allocation of only necessary credits

The conference agreement follows the House bill.

aa. Project evaluation

The conference agreement generally follows the House bill, with three amendments: (1) the House bill selection criteria are expanded to include consideration of local tax-exempt organizations, the preferential treatment of persons on a public housing waiting list, and project feasibility; (2) allocation plans should give highest priority to projects with the lowest percentage of intermediary costs unless granting this priority would impede the development of projects in certain hard-to-develop areas, and (3) the allocating agency would be required to monitor compliance with the credit and report projects in noncompliance to the IRS.

bb. Semiannual determination of credit percentage

The conference agreement does not include the House bill provision.

cc. Administrative provisions

The conference agreement follows the House bill.

dd. Effective date

The conference agreement follows the House bill, with an amendment: the provision relating to determination of eligible basis is effective as if passed as part of the Tax Reform Act of 1986.

2. R&D credit

Senate recedes to an extension through December 31, 1990, with the following additional modifications:

a. Computation of the base amount

The base amount would be computed by multiplying the taxpayer's fixed-based percentage by its average gross receipts for the four preceding years. The fixed-based percentage would equal the ratio of total qualified research expenditures to total gross receipts from the 1984-88 period.

b. Start-up companies

The 1984-88 period would be used to determine whether a firm qualifies as a start-up company.

c. Fixed-based cap

In no case would a taxpayer's fixed based percentage exceed .16.

d. Base limitation

The base limitation would be 50 percent for all firms (i.e., there would be no special base limitation rule for start-up firms).

e. Trade or business limitation

Senate recedes.

f. Treasury study

House recedes.

g. Consistent treatment of R&E expenses

Senate recedes.

h. Regulatory authority to adjust for accounting changes

The Secretary would be granted authority to prevent distortions in calculation of the credit due to a change in accounting methods used by the taxpayer.

i. University basic research credit

Senate recedes.

j. Relation to deduction for research expenses

Senate recedes.

k. Reasonableness requirement under section 174

Senate recedes.

l. Effective date

Senate recedes.

L. Revision of Civil Penalties

Senate recedes.

M. Individual Capital Gains

House recedes.

N. Other Provisions (Technicals Involving Revenue Effect)

1. Marital deduction for property passing to noncitizen spouses

   Senate recedes to all provisions except with respect to exemption from tax on distributions from qualified domestic trusts (distributions for hardship would be exempt from tax).

2. Coordination of foreign tax credit and tax on lump-sum distributions--Senate recedes.

O. Technical Corrections

Senate recedes with modifications.

Pension technicals--Senate recedes to Ways and Means Committee technicals with modifications.

P. Child Care and Earned Income Tax Credit Provisions

House recedes.