[JOINT COMMITTEE PRINT]

SUMMARY OF REVENUE PROVISIONS IN THE PRESIDENT'S FISCAL YEAR 1992 BUDGET PROPOSAL

PREPARED BY THE STAFF

OF THE

JOINT COMMITTEE ON TAXATION

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INTRODUCTION

This pamphlet,[1] 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 1992, submitted to the Congress on February 4, 1991.[2]

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 budget proposals for fiscal years 1989, 1990, or 1991.[3] The revenue proposals in this pamphlet are organized as follows: (A) Income tax provisions; (B) Expiring tax provisions; (C) Compliance provisions; (D) Other tax provisions; and (E) Certain user fees. The second part of the pamphlet presents the Joint Committee on Taxation staff's estimates of the budget effects of the President's revenue proposals for fiscal years 1991-1996.

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[1] This pamphlet may be cited as follows: Joint Committee on Taxation, *Summary of Revenue Provisions in the President's Budget Proposal for Fiscal Year 1992* (JCS-1-91), February 25, 1991.

[2] This pamphlet includes those fee proposals in the President's budget proposal that are classified as budget receipts by the Administration's budget documents. See Department of the Treasury, *General Explanations of the President's Budget Proposals Affecting Receipts*, February 1991; also *Budget of the United States Government, Fiscal Year 1992*. 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, nor is it intended to create any inference regarding the classification of such fees under the categories established by the Budget Enforcement Act of 1990.

[3] *Budget of the United States Government, Fiscal Year 1989*; *Budget of the United States Government, Fiscal Year 1990*; *Budget of the United States Government, Fiscal Year 1991.*

I. SUMMARY OF PRESIDENT'S REVENUE PROPOSALS

A. Income Tax Provisions

1. Capital Gains Tax Rate Reduction for Individuals

Present Law

Under present law, the net capital gain of an individual is taxed generally at the same rates applicable to ordinary income, subject to a maximum marginal rate of 28 percent. (Net capital gain is the excess of net long-term capital gain over net short-term capital loss.) Individuals with a net capital loss generally may deduct up to $3,000 ($1,500 for married persons filing a separate return) of the loss each year against ordinary income. Net capital losses in excess of the $3,000 ($1,500) 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 whose capital gains would otherwise be subject to a 28-percent rate, 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 date of enactment. For the portion of 1991 to which the proposal would apply, a 30-percent exclusion would apply for all assets held one year or more. For 1992, 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 the 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 President's budget proposal for fiscal year 1991 contained the same capital gains recommendation as the fiscal year 1992 budget proposal.

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 also 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 in 1989 as a separate bill (H.R. 3628).

The Omnibus Budget Reconciliation Act of 1990 (H.R. 5835) as passed by the House of Representatives would have provided a 50-percent exclusion of individual capital gains on nontraded property, with a lifetime cap of $200,000 of gain. That bill also would have provided generally a deduction of up to $1,000 of capital gains each year for individuals with an adjusted gross income of less than $150,000. These provisions were deleted from the legislation in conference.

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 saved 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 annual contribution that may be made to an IRA generally is the lesser of $2,000 or 100 percent of an individual's compensation. Earnings on IRA contributions are not subject to tax until withdrawn, and certain rules apply to determine whether a contribution is deductible when made.

A single taxpayer is permitted to deduct the maximum permitted contribution for a year if the individual is not an active participant in an employer-sponsored retirement plan for the year or the individual has adjusted gross income (AGI) of less than $25,000. A married taxpayer filing a joint return is permitted to deduct the maximum permitted IRA contribution for a year if neither spouse is an active participant in an employer-sponsored plan or the couple has combined AGI of less than $40,000.

If a single taxpayer or either spouse (in the case of a married taxpayer) is an active participant in an employer-sponsored retirement plan, the IRA maximum deduction is phased out over certain AGI levels. For single taxpayers, the maximum IRA deduction is phased out between $25,000 and $35,000 of AGI. For married taxpayers, the maximum deduction is phased out between $40,000 and $50,000 of AGI. In the case of a married taxpayer filing a separate return, the deduction is phased out between $0 and $10,000 of AGI.

President's Budget Proposal

Under the President's budget proposal, certain individuals 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 taxpayers with AGI of no more than $60,000, for heads of households with AGI of no more than $100,000, and for married taxpayers filing joint returns with AGI of no more than $120,000. Amounts contributed to a family savings account would not affect the amount that could otherwise be contributed to employer-provided retirement plans (e.g., section 401(k) plans) or to other tax-favored forms of saving (e.g., IRAs).

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 and 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 for years beginning on or after January 1, 1991.

Prior Action

The President's budget proposal for fiscal year 1991 contained the same proposal.

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 substantially equal periodic payments over the life (or life expectancy) of the IRA owner or over the joint lives (or life expectancies) of the IRA owner and his or her spouse.

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 3 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 for years beginning on or after January 1, 1991.

Prior Action

The President's budget proposal for fiscal year 1991 contained the same proposal.

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. Deduction 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, as a substitute for the deduction, 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 a 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. This deduction would be allowed for eligible expenses regard-less of the level of reimbursement allowed under the Adoption Assistance Program. Any reimbursement of expenses that were previously deducted 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, 1991.

Prior Action

This proposal was included in the President's budget proposal for fiscal years 1990 and 1991. 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.

5. Enterprise Zone Tax Incentives

Present Law

Targeted area

The Internal Revenue Code does not contain general rules for targeting geographic 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 children are eligible for a refundable earned income tax credit (EITC) of up to 16.7 percent (17.3 percent for taxpayers with 2 or more qualifying children) of the first $7,140 of earned income for 1991. The EITC is not available to taxpayers with adjusted gross income over $20,260.

Deduction for purchase of stock

In general, amounts paid to purchase corporate stock are not currently deductible, but instead are treated as the cost basis of such stock. Present law provides a deduction to certain taxpayers for contributions to an individual retirement account ("IRA"), and such contributions may be used to purchase corporate stock. All or a portion of amounts withdrawn from IRAs are includible in income when withdrawn.

Capital gains

Under present law, the net gain from the sale or exchange of capital assets of an individual is taxed at the same rates applicable to ordinary income, subject to a maximum rate of 28 percent. Between 1988 and 1990, net capital gain was taxed at the same rates applicable to ordinary income. 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 gains was 28 percent.

President's Budget Proposal

The President's budget 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. (The proposal does not describe the selection criteria.)

(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. The credit would phase out for employees with annual wage earnings between $20,000 and $25,000.

(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

The President's budget proposal for fiscal year 1991 contained the same proposal.

6. Extend Tax Deadlines for Desert Shield Participants

Present Law

In general

Section 7508 suspends the period of time for performing various acts under the Internal Revenue Code, such as filing tax returns, paying taxes, or filing a claim for credit or refund of tax, for any individual serving in the Armed Forces of the United States (or in support of the Armed Forces) in an area designated as a "combat zone" during the period of combatant activities. An individual who becomes a prisoner of war is considered to continue in active service, and is therefore also eligible for these suspension of time provisions. The designation of a combat zone must be made by the President in an Executive Order.

Executive Order

On January 21, 1991, President Bush signed Executive Order 12744, designating the Persian Gulf Area as a combat zone. The designation was retroactive to January 17, 1991, the date combat commenced in that area, and continues in effect until terminated by another Executive Order. Thus, individuals serving in the Persian Gulf Area are eligible for the suspension of time provisions described above, beginning January 17, 1991.

The Executive Order specifies that the Persian Gulf Area is the Persian Gulf, the Red Sea, the Gulf of Oman, a portion of the Arabian Sea, the Gulf of Aden, and the total land areas of Iraq, Kuwait, Saudi Arabia, Oman, Bahrain, Qatar and the United Arab Emirates.

H.R. 4 (P.L. 102-2)

Congress recently passed H.R. 4, which was signed into law (P.L. 102-2) by the President on January 30, 1991, amending section 7508 in several respects. It provides that any individual who performs Desert Shield services (and the spouse of such an individual) is entitled to the benefits of the suspension of time provisions of section 7508. Desert Shield services are defined as services in the Armed Forces of the United States (or in support of those Armed Forces) if such services are performed in the area designated by the President as the "Persian Gulf Desert Shield Area" and such services are performed during the period beginning August 2, 1990, and ending on the date on which any portion of the area is designated by the President as a combat zone.

H.R. 4 also amends section 7508 by providing that the rules for determining the amount of interest on a tax refund generally applicable to other taxpayers also apply to those eligible for the benefits of these suspension of time provisions. In addition, a special rule applies in the case of returns claiming refunds filed during this suspension period. With respect to these qualifying returns, interest will be paid on tax refunds from April 15 (in the case of calendar-year individuals).

The suspension of time provided by section 7508, as amended, encompasses the period of service in the combat zone during the period of combatant activities in the zone, as well as (1) any time in continuous hospitalization (subject to a limit of five years once the individual returns to the United States) resulting from injury received in the combat zone or (2) time in missing in action status, plus the next 180 days.

Spouses of qualifying individuals are entitled to the same suspension of time, except that: (1) the spouse is ineligible for this suspension for any taxable year beginning more than two years after the date of termination of combatant activities in the combat zone, and (2) the suspension of time provisions based on continuous hospitalization inside the United States are applicable only to the hospitalized individual; they are not applicable to the spouse of such individual.

President's Budget Proposal

The President's budget proposal would extend coverage of section 7508 to individuals participating in the Desert Shield operation.

The President's proposal has already been enacted as part of H.R. 4, as described above.

B. Expiring Tax Provisions

1. 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, 1991.

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 expenditures 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 expenditures for the 1984-1988 period bears to its total gross receipts for this period (subject to a maximum ratio of .16).[4]

Qualified research expenditures 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 section 174 are reduced by an amount equal to 100 percent of the taxpayer's research credit determined for that year.

President's Budget Proposal

The President's budget proposal would make permanent the 20-percent research tax credit for qualified research expenditures and university basic research expenditures.

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

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[4] If a taxpayer did not both incur qualified research expenditures and have gross receipts during each of at least three years between 1984-1988, then it is assigned a fixed-base percentage of .03.

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.

The Omnibus Budget Reconciliation Act of 1990 extended the research credit through December 31, 1991 (and repealed the special rule to prorate qualified expenses incurred during 1990).

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 two taxable years beginning after August 1, 1989 and on or before August 1, 1991, the R&D allocation regulation has been 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), the Omnibus Budget Reconciliation Act of 1989 (OBRA89), and the Omnibus Budget Reconciliation Act of 1990 (OBRA90). 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. For this purpose total expenses for the year were deemed to be incurred evenly throughout the year. For expenses deemed paid or incurred during the first four months of such year (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 were allocated to U.S. source income, 64 percent of foreign-incurred R&D expenses were allocated to foreign source income, and the remainder of R&D expenses were allocated and apportioned either on the basis of sales or gross income, but subject to the condition that if income-based apportionment was used, the amount apportioned to foreign source income could have been no less than 30 percent of the amount that would have been apportioned to foreign source income had the sales method been used. For expenses deemed paid or incurred during the remainder of such year, the R&D allocation regulation applied.

In taxable years governed by OBRA89 and OBRA90, the same statutory allocation rule applies as was applicable to expenses deemed incurred in the first four months of the year governed by TAMRA. That allocation rule is codified as section 864(f) of the Internal Revenue Code.

President's Budget Proposal

Under the President's budget proposal, the statutory R&D allocation rules of section 864(f) would be extended for one year, so as to apply to all R&D expenses paid or incurred in taxable years beginning after August 1, 1991 and on or before August 1, 1992.[5] Under these rules, R&D expenses (other than amounts incurred to meet certain legal requirements, and thus allocable to one geographical source) are sourced as follows: 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 is 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.

Prior Action

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

[5] The Treasury Department's *General Explanation of the President's Budget Proposals Affecting Receipts* erroneously describes the effective date of the proposal as "taxable years beginning after August 1, 1991 and *ending* on or before August 1, 1992."

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 Technical and Miscellaneous Revenue Act of 1988 (TAMRA) included statutory R&D allocation rules which were similar to the proposal included in H.R. 3545 with three primary modifications: (1) 64 percent of U.S.-incurred R&D expenses were allocated to U.S. source income, rather than 67 percent; (2) 64 percent of foreign-incurred R&D expenses were 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. In addition, 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).

The President's budget proposal for fiscal year 1990 included a permanent extension of the statutory R&D allocation rules contained in TAMRA. OBRA89 included a temporary extension of those R&D allocation rules, which it codified in section 864(f) of the Internal Revenue Code. 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).

The President's budget proposal for fiscal year 1991 included a permanent extension of the statutory R&D allocation rules of section 864(f). No R&D allocation rules were included in OBRA90 (H.R. 5835) as passed by the House on October 16, 1990. The Senate amendment to H.R. 5835, which passed the Senate on October 18, 1990, included an extension of the R&D allocation rules of section 864(f) covering a period that included the remainder of the taxable year covered by OBRA89 plus the subsequent taxable year. The conference agreement on OBRA90 included the extension of section 864(f) as passed by the Senate.

3. Low-Income Rental Housing Tax Credit

Present Law

A tax credit is allowed in annual installments over 10 years for qualifying low-income rental housing, which may be newly constructed, or newly acquired existing residential rental property that is substantially rehabilitated. For most newly constructed housing and for rehabilitation costs on most existing housing, 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 the acquisition cost of existing housing (satisfying rehabilitation requirements) and of all 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 is recaptured. The 30-year extended use agreement creates a State law right to enforce low-income use for an additional 15 years after the 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 is $1.25 per resident of each State.

The low-income housing credit is scheduled to expire after December 31, 1991.

President's Budget Proposal

The President's budget proposal would extend the credit for one year, through December 31, 1992.

Prior Action

The low-income housing credit was enacted in the Tax Reform Act of 1986, with an expiration date of December 31, 1988. As enacted under the 1986 Act, the annual State credit allocation was $1.25 per resident. The Technical and Miscellaneous Revenue Act of 1988 extended the credit for one year (through December 31, 1989). The credit was substantially revised and extended through December 31, 1990, in the Omnibus Budget Reconciliation Act of 1989. As extended under the 1989 Act, the annual State credit allocation was $.9375 per resident for 1990. The Omnibus Budget Reconciliation Act of 1990 increased the annual State allocation to $1.25 per resident for 1990, and extended the credit through December 31, 1991, with an annual State credit allocation of $1.25 per resident.

4. Targeted Jobs Tax Credit

Present Law

Tax credit

The targeted jobs tax credit is available on an elective basis for hiring individuals from nine targeted groups. The targeted groups are: (1) vocational rehabilitation referrals; (2) economically disadvantaged youths aged 18 through 22; (3) economically disadvantaged Vietnam-era veterans; (4) Supplemental Security Income (SSI) recipients; (5) general assistance recipients; (6) economically disadvantaged cooperative education students aged 16 through 19; (7) economically disadvantaged former convicts; (8) Aid to Families with Dependent Children (AFDC) recipients and Work Incentive (WIN) registrants; and (9) economically disadvantaged summer youth employees aged 16 or 17. Certification of targeted group membership is required as a condition of claiming the credit.

The credit generally is equal to 40 percent of the first $6,000 of qualified first-year wages paid to a member of a targeted group. Thus, the maximum credit generally is $2,400 per individual. With respect to economically disadvantaged summer youth employees, however, the credit is equal to 40 percent of up to $3,000 of wages, for a maximum credit of $1,200.

The credit is not available for wages paid to a targeted group member unless the individual either (1) is employed by the employer for at least 90 days (14 days in the case of economically disadvantaged summer youth employees), or (2) has completed at least 120 hours of work performed for the employer (20 hours in the case of economically disadvantaged summer youth employees). Also, the employer's deduction for wages must be reduced by the amount of the credit claimed.

The credit is available with respect to targeted-group individuals who begin work for the employer before January 1, 1992.

Authorization of appropriations

Present law also authorizes appropriations for administrative and publicity expenses relating to the targeted jobs credit. These monies are to be used by the Internal Revenue Service and the Department of Labor to inform employers of the credit program. As modified by the 1990 Act, such appropriations are authorized for each fiscal year in amounts as may be necessary for the program (the current credit expires after December 31, 1991).

President's Budget Proposal

The President's budget proposal would extend the credit for one year. Therefore, the credit would be available for workers who begin work for the employer before January 1, 1993. (Thus, appropriations would also be authorized, as under present law, for administrative and publicity expenses related to the credit extension.)

Prior Action

The targeted jobs tax credit was enacted by Congress in the Revenue Act of 1978. The credit was initially scheduled to apply to qualified wages paid before 1982. It was extended for one year by the Economic Recovery Tax Act of 1981, extended for two years by the Tax Equity and Fiscal Responsibility Act of 1982, extended for one year by the Deficit Reduction Act of 1984, extended for three years by the Tax Reform Act of 1986, extended for one year by the Technical and Miscellaneous Revenue Act of 1988, extended for nine months by the Omnibus Budget Reconciliation Act of 1989, and extended for fifteen months by the Omnibus Budget Reconciliation Act of 1990.

5. Business Energy Tax Credits for Solar and Geothermal Property

Present Law

Nonrefundable business energy tax credits are allowed for 10 percent of the cost of investment in qualified solar and geothermal property. These credits apply to property placed in service by December 31, 1991.

President's Budget Proposal

The President's budget proposal would extend the business credits for solar and geothermal property for one year, through December 31, 1992.

Prior Action

The tax credits for solar and geothermal energy properties were enacted in the Energy Tax Act of 1978, effective after April 20, 1977, through December 31, 1982. A similar credit for ocean thermal energy property was enacted in the Windfall Profit Tax Act of 1980, effective through 1985. In the same Act, the solar and geothermal credits were extended through 1985. In the Tax Reform Act of 1986, these three credits were extended for three additional years (through 1988) at rates which phased down to 10 percent for solar and geothermal property and 15 percent for ocean thermal property. In the Technical and Miscellaneous Revenue Act of 1988, these credits were extended for one year. In the Omnibus Budget Reconciliation Act of 1989, these credits were extended for nine months (through September 30, 1990). In the Omnibus Budget Reconciliation Act of 1990, the solar and geothermal credits were extended for fifteen months (through December 31, 1991) and the ocean thermal credit was allowed to expire.

6. Deduction 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 December 31, 1991. 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 extend the 25-percent deduction for one year.

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 extended the provision through September 30, 1990. The Omnibus Budget Reconciliation Act of 1990 extended the provision through 1991.

The President's budget proposal for fiscal year 1991 proposed making the 25-percent deduction permanent.

C. Compliance Provisions

1. Increase in IRS FY 1992 Enforcement Funding

Present Law

In fiscal year 1990, the IRS had approximately 111,960 full-time equivalent employees with total budget authority of about $5.5 billion. The IRS budget authority for fiscal year 1991 is $6.1 billion.

President's Budget Proposal

The President's budget proposal would increase IRS budget authority for fiscal year 1992 to about $6.7 billion. The budget document states that IRS funding for enforcement is to be increased. Part of the increase in budget authority is to be used to collect delinquent taxes and increase the audit workforce.

Prior Action

President Bush's budget proposals for both fiscal years 1990 and 1991 included a similar IRS enforcement initiative.

2. Retail Alcoholic Beverage Occupational Tax Compliance

Present Law

Present law imposes a special occupational tax of $250 a year per premise on 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 per premise (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).[6]

President's Budget Proposal

The President's budget proposal provides that, to increase compliance rates and revenues, wholesalers would be required to ensure that their retail customers pay the special taxes in connection with liquor occupations that are levied on retailers. The proposal would be effective beginning October 1, 1991.

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.

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[6] The tax is $500 a year per premise for businesses with gross receipts of less than $500,000 in the preceding year.

A 1989 budget reconciliation provision approved by the Senate Finance Committee (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.

The President's budget proposal for fiscal year 1991 proposed that the special occupation taxes currently levied on liquor retailers be eliminated and that existing occupation taxes on liquor wholesalers and manufacturers be increased.

D. Other Tax Provisions

1. Highway Trust Fund Excise Tax Extension

Present Law

Federal excise taxes generally are imposed on gasoline (14 cents per gallon) and diesel fuel (20 cents per gallon) used in highway transportation.[7] Amounts equivalent to 11.5 cents per gallon from the tax on gasoline and 17.5 cents per gallon from the tax on diesel fuel are dedicated to the Highway Trust Fund.[8] Amounts equivalent to 2.5 cents per gallon from these taxes are retained in the General Fund.

In addition, Highway Trust Fund excise taxes are imposed as follows: a 12-percent retail tax on sales of heavy trucks (over 33,000 pounds) and truck trailers (over 26,000 pounds); a tax on heavy tires for highway use (graduated rate on tires weighing 40 pounds or more); and an annual use tax on heavy highway vehicles (graduated rate on vehicles weighing 55,000 pounds or more).

The motor fuels excise taxes and the other Highway Trust Fund excise taxes are scheduled to expire after September 30, 1995.

President's Budget Proposal

The President's budget proposal would extend the Highway Trust Fund portion of the Federal excise taxes on gasoline and diesel fuel through September 30, 1996, but at a reduced rate of 9 cents per gallon for gasoline and 15 cents per gallon for diesel fuel for the period after September 30, 1995. The budget proposal also would extend the other current Highway Trust Fund taxes through September 30, 1996.

Subsequent to the budget proposal, the Department of Transportation submitted a 5-year highway and mass transit reauthorization program to the Congress. This proposed program would extend the Highway Trust Fund taxes through September 30, 1998 (at levels as in the President's budget proposal).[9]

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[7] A tax of 0.1 cent per gallon also is imposed on gasoline and other motor fuels for the Leaking Underground Storage Tank Trust Fund.

[8] Of the amounts dedicated to the Highway Trust Fund, 1.5 cents per gallon is set aside in the Mass Transit Account for certain mass transit purposes.

[9] Department of Transportation (DOT) transportation authorization program, submitted to the Congress on February 13, 1991 (proposed "Surface Transportation Assistance Act of 1991"). The DOT transportation reauthorization program also would include a separate authorization for fiscal years 1993–1996 to fund a Highway Tax Compliance Project to improve Federal and State motor fuels tax compliance. (The projected impact of this compliance project on budget receipts is not included in the President's fiscal year 1992 budget estimates nor in the Joint Committee on Taxation staff estimates in Part II of this pamphlet.)

Prior Action

The Federal excise tax on highway gasoline was raised from 9 to 14 cents per gallon and the tax on highway diesel fuel was raised from 15 to 20 cents per gallon on December 1, 1990, as part of the Omnibus Budget Reconciliation Act of 1990 (P.L. 101-508). The excise taxes on highway gasoline and diesel fuel were increased from 4 to 9 cents per gallon, effective April 1, 1983, as part of the Highway Revenue Act of 1982 (P.L. 97-424); the tax rate on highway diesel fuel was subsequently increased to 15 cents per gallon by the Deficit Reduction Act of 1984 (P.L. 98-369).

The Highway Trust Fund taxes were extended from October 1, 1993 through September 30, 1995, in the 1990 Act.

2. Extend Medicare Hospital Insurance to All 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 1991 to Medicare-covered employees, the total hospital insurance tax rate is 2.9 percent of the first $125,000 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 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 January 1, 1992.

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. During the 101st Congress, the Senate Amendment to H.R. 5835 (the Omnibus Budget Reconciliation Act of 1990) included a provision similar to the President's budget proposal. In both cases, these provisions were 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 proposals for fiscal years 1990 and 1991.

3. 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 railroad unemployment tax rate for public commuter railroads in 1989 and 1990. Instead, such public commuter railroads reimbursed the unemployment system for the amount of actual unemployment and sickness benefits paid during those years to their employees. Starting in 1991, these 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 present-law exemption provided to commuter railroads, effective January 1, 1991. The proposal would also extend the exemption to Amtrak, effective January 1, 1991.

Prior Action

This same proposal was included in President Bush's fiscal year 1991 budget proposal. The Amtrak provision was also included in President Bush's budget proposal for fiscal year 1990 and in President Reagan's budget proposal for fiscal year 1989.

E. Certain User Fees

1. 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 after September 30, 1995.

President's Budget Proposal

The President's budget proposal would extend these fees. The budget documents do not specify the duration of the proposed extension.

Prior Action

The Omnibus Budget Reconciliation Act of 1990 extended the expiration date of these fees from August 1992 through September 30, 1995. The President's fiscal year 1991 budget proposed that these fees be extended permanently.

2. 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 or leased in interstate commerce. The Secretary is authorized to charge the developer a fee (up to $1,000 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 $1,000 per developer fee limit, and would permit the fee to be increased to the extent needed to fully offset program costs.

Prior Action

The President's budget proposal for fiscal year 1991 contained the same proposal.

II. ESTIMATED BUDGET EFFECTS

Table 1.—Estimated Budget Effects of Revenue Provisions in the President's Fiscal Year 1992 Budget Proposal

Fiscal Years 1991–1996

[Billions of Dollars]

Provisions	1991	1992	1993	1994	1995	1996	1991–96
A. Income Tax Provisions							
1. Capital gains tax rate reduction for individuals	0.8	3.7	−3.2	−4.4	−4.1	−3.4	−10.6
2. Establish family savings accounts	......	−0.4	−0.6	−1.0	−1.4	−1.8	−5.2
3. Waive penalty tax for early withdrawals from IRAs for first-time home buyers	......	−0.2	−0.1	−0.1	−0.1	−0.1	−0.6
4. Restore and double deduction for adoption of special needs children	......	......	(1)	(1)	(1)	(1)	(1)
5. Establish enterprise zone tax incentives	(2)	(2)	(2)	(2)	(2)	(2)	(2)
6. Extend tax deadlines for Desert Shield participants (enacted in H.R. 4)	......	......	......	......	......	......	......
B. Expiring Tax Provisions							
1. Permanent extension of R&E credit	......	−0.5	−1.0	−1.3	−1.6	−1.8	−6.2
2. Extend R&E allocation rules (1 year)	......	−0.4	−0.3	......	......	......	−0.7
3. Extend low-income housing tax creedit (1 year)	......	−0.1	−0.3	−0.4	−0.4	−0.4	−1.5
4. Extend targeted jobs tax credit (1 year)	......	−0.1	−0.1	−0.1	(1)	(1)	−0.4
5. Extend business energy tax credits (1 year)	......	(1)	(1)	......	......	......	(1)
6. Extend health insurance deduction for self-employed (1 year)	......	−0.3	−0.1	......	......	......	−0.4
C. Compliance Provisions							
1. Increase IRS enforcement funding [3]	......	......	......	......	......	......	......
2. Improve retail compliance with alcohol special occupational taxes [4]	......	(5)	(5)	(5)	(5)	(5)	0.1

D. Other Tax Provisions							
1. Extend Highway Trust Fund excise taxes (1 year)[4,6]	......					−2.8	−2.8
2. Extend Medicare (HI) coverage to all State and local employees[3,4]	......	1.1	1.5	1.5	1.5	1.5	7.2
3. Extend railroad unemployment insurance (UI) reimbursable status[3,4]	(1)	(5)	(5)	(5)	(1)	(1)	(5)
E. Certain User Fees							
1. Extend abandoned mine reclamation fees[3]	......					0.3	0.3
2. Increase HUD interstate land sales fee[3]	(7)	(7)	(7)	(7)	(7)	(7)	(5)
Grand Total[8]	**0.8**	**2.8**	**−4.2**	**−5.8**	**−6.1**	**−8.5**	**−20.8**

[1] Loss of $50 million or less.

[2] Uncertainty about the size, location, and economic characteristics of enterprise zones to be designated makes the proposal difficult to estimate at this time.

[3] Estimate for this provision provided by the Congressional Budget Office (CBO).

[4] Net of income tax offsets.

[5] Gain of $50 million or less.

[6] Extend existing Trust Fund taxes from October 1, 1995, through September 30, 1996, but a 9 cents per gallon for gasoline and 15 cents per gallon for diesel fuel for the one-year extension period. Estimate is relative to the CBO baseline, which assumes extension of these motor fuels taxes at 11.5 cents per gallon for gasoline and 17.5 cents per gallon for diesel fuel (the Highway Trust Fund financing rates).

[7] Gain of less than $1 million.

[8] Not including the enterprise zones proposal (A. 5.).

Source: Joint Committee on Taxation; Congressional Budget Office (Items C.1., D.2., D.3., E.1., and E.2.)

PRELIMINARY

Table 2.—Estimated Revenue Effects of the President's Capital Gains Tax Reduction Proposal

Fiscal Years 1991–1996

[Billions of Dollars]

Item [1]	1991	1992	1993	1994	1995	1996	1991–96
1. Static effect of the 30% exclusion [2]	−2.1	−14.5	−16.3	−17.6	−19.1	−20.7	−90.4
2. Effect of induced realizations [3]	2.7	17.1	13.4	12.6	13.7	14.8	74.3
3. Effect of full depreciation recapture	0.1	0.7	0.8	0.9	0.9	1.0	4.5
4. Effect of phase-in of the 3-year holding period	......	−0.2	−1.5	−0.7	−0.1	1.0	−1.5
5. Effect of treating excluded portion of gains as a preference item for AMT purposes	0.1	0.4	0.4	0.4	0.4	0.4	2.1
6. Effective date of the proposal [4]	0.1	0.2	......	......	......	......	0.3
Total, Revenue Effect of the Proposal	**0.8**	**3.7**	**−3.2**	**−4.4**	**−4.1**	**−3.4**	**−10.6**

[1] All estimates in this table are done incrementally; that is, assuming provisions described on preceding lines of the table have been enacted.

[2] This line reflects an estimate of the proposed 30% exclusion for assets held at least one year, assuming no change in taxpayer behavior.

[3] This line reflects an estimate of the increase in budget receipts attributable to taxpayer decisions to realize more capital gains as a result of the lower tax rate.

[4] Lines 1–5, above, reflect a January 1, 1991, effective date; line 6 represents an adjustment to these lines to reflect an assumed effective date of March 15, 1991.

Note: Details may not add to totals due to rounding.

Source: Joint Committee on Taxation.