DESCRIPTION OF AN AMENDMENT IN THE NATURE OF A SUBSTITUTE TO THE CHAIRMAN'S MARK RELATING TO ADDITIONAL TECHNICAL CORRECTIONS

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HOUSE COMMITTEE ON WAYS AND MEANS

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INTRODUCTION

The House Committee on Ways and Means has scheduled a markup on additional technical corrections on September 18, 1995. This document, prepared by the staff of the Joint Committee on Taxation, provides a description of the proposed additional technical corrections.[1] (Other technical corrections are included in H.R. 1215 as passed by the House of Representatives.)

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[1] This document may be cited as follows: Joint Committee on Taxation, *Description of an Amendment in the Nature of a Substitute to the Chairman's Mark Relating to Additional Technical Corrections* (JCX-37-95), September 18, 1995.

DESCRIPTION OF ADDITIONAL TECHNICAL CORRECTIONS

A. Technical Correction to the Technical and Miscellaneous Revenue Act of 1988-- Reporting of Real Estate Transactions

Present Law

It is unlawful for any real estate reporting person to charge separately any customer for complying with the information reporting requirements with respect to real estate transactions.

Description of Proposal

The proposal would clarify that real estate reporting persons may take into account the cost of complying with the reporting requirements of Code section 6045 to establishing charges for their services, so long as a separately listed charge for such costs is not made.

Effective Date

The proposal would be effective on November 11, 1988 (as if originally enacted as part of the amendment to the Code relating to separate changes).

B. Technical Correction to the Tax Reform Act of 1986-- Clarification of Denial of Deductions for Stock Redemption Expenses

Present Law

Section 162(k), added by the Tax Reform Act of 1986, denies a deduction for any amount paid or incurred by a corporation in connection with the redemption of its stock. An exception is provided for any deduction allowable under section 163 (relating to interest). The Internal Revenue Service has taken the position that costs properly allocable to a borrowing, the interest on which is deductible under the exception, may not be amortized over the period of the loan, due to section 162(k). Different courts have reached differing conclusions when taxpayers have litigated the question.[2]

Description of Proposal

The proposal clarifies that amounts properly allocable to indebtedness on which interest is deductible and properly amortized over the term of that indebtedness are not subject to the provision of section 162(k) denying a deduction for any amount paid or incurred by a corporation in connection with the redemption of its stock.

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[2] See, e.g., Fort Howard Corp. v. Commissioner, 103 T.C. 345 (1994) upholding the IRS position; compare U.S. v. Kroy (Europe) Limited, 27 F.3d 367 (9th Cir. 1994) (to the contrary).

In addition, the proposal clarifies that the rules of section 162(k) apply to any acquisition of its stock by a corporation or by a party that has a relationship to the corporation described in section 465(b)(3)(C) (which applies a more than 10 percent relationship test in certain cases).

Thus, for example, it is clarified that the denial of a deduction applies to any reacquisition (i.e., any transaction that is in effect an acquisition of previously outstanding stock) regardless of whether the transaction is treated as a redemption for purposes of subchapter C of the Code, regardless of whether it is treated for tax purposes as a sale of the stock or as a dividend, and regardless of whether the transaction is a recapitalization or other reorganization.

Effective Date

The proposal clarifying that amounts properly allocable to indebtedness and amortized over the term of that indebtedness are not subject to the denial under section 162(k), would be effective as if included in the Tax Reform Act of 1986.

The other clarifications would apply to amounts paid or incurred after September 13, 1995. No inference is intended that any amounts described in this clarification, or any other amounts paid or incurred to acquire stock are deductible under present law.

C. Technical Correction to the Omnibus Budget Reconciliation Act of 1990--Clarification of Depreciation Class for Certain Energy Property

Present Law

Section 168(e)(3)(B)(vi)(I) provides that "solar and wind energy property" is 5-year property for purposes of the Modified Accelerated Cost Recovery System ("MACRS"). "Solar and wind energy property" is defined by a cross-reference to section 48(a)(3)(A). Section 48(a)(3) contains flush language that provides that "energy property" does not include any public utility property. It is unclear whether this language applies to section 48(a)(3)(A) to deny the characterization of solar and wind energy property that is also public utility property as 5-year property.

Description of Proposal

The proposed technical correction would clarify that solar or wind energy property that is also public utility property qualifies as 5-year MACRS property.

Effective Date

The proposal would be effective as if included in the Omnibus Budget Reconciliation Act of 1990.

D. Technical Correction to the Deficit Reduction Act of 1984--Cross Reference Relating to Limitations on Benefits and Contributions

Present Law

Section 404(j)(1) requires the application of the limits on contributions and benefits under section 415 in determining deductions under certain listed paragraphs of subsection 404(a). Included in this list is paragraph (10) which no longer exists.

Section 713(d)(4)(A) of the Deficit Reduction Act of 1984 ("DEFRA") removed the prior section 404(a)(9), which referred to plans benefiting self-employed, and redesignated 404(a)(10) as 404 (a)(9). However, this cross reference in 404(j)(1) was not changed.

Description of Proposal

Section 404(j)(1) would be amended to refer to section 404(a)(9) instead of section 404(a)(10).

Effective Date

The proposal would be effective as if included in DEFRA.

E. Treatment of Certain Veterans' Reemployment Rights

Present Law

Under the Uniformed Services Employment and Reemployment Rights Act of 1994 ("USERRA"), Pub. L. No. 103-353, 38 U.S.C. §§ 4301, ff., which revised and restated the Federal law protecting veterans' reemployment rights, an employee who leaves a civilian job for qualified military service (including National Guard and certain Public Health Service duty) generally is entitled to be reemployed by the civilian employer if the individual returns to employment within a specified time period. In addition to reemployment rights, a returning veteran also is entitled to the restoration of certain pension, profit sharing and similar benefits that would have accrued, but for the employee's absence due to the qualified military service.

USERRA generally provides that for a reemployed veteran service in the uniformed services is considered service with the employer for retirement plan benefit accrual purposes, and the employer that reemploys the returning veteran is liable for funding any resulting obligation. USERRA also provides that the reemployed veteran is entitled to any accrued benefits that are contingent on the making of, or derived from, employee contributions or elective deferrals only to the extent the reemployed veteran makes payment to the plan with respect to such contributions or deferrals. No such payment may exceed the amount the reemployed veteran would have been permitted or required to contribute had the person remained continuously employed by the

employer throughout the period of uniformed service. Under USERRA, any such payment to the plan must be made during the period beginning with the date of reemployment and whose duration is three times the reemployed veteran's period of uniform service, not to exceed five years.

Under the Internal Revenue Code, overall limits are provided on contributions and benefits under certain retirement plans. For example, the maximum amount of elective deferrals that can be made by an individual into a qualified cash or deferred arrangement in any taxable year is limited to $9,240 for 1995 (sec. 402(g)). Annual additions with respect to each participant under a qualified defined contribution plan generally are limited to the lesser of $30,000 (for 1995) or 25 percent of compensation (sec 415(c)). Annual deferrals with respect to each participant under an eligible deferred compensation plan (sec. 457) generally are limited to the lesser of $7,500 or 33-1/3 of includible compensation. There is no provision under present law that permits contributions or deferrals to exceed these and other annual limits in the case of contributions with respect to a reemployed member of the uniformed services.

Other requirements for which there is no special provision for contributions with respect to a reemployed member of the uniformed services include the limit on deductible contributions and the qualified plan nondiscrimination, coverage, minimum participation, and top heavy rules.

Description of Proposal

The proposal would provide special rules in the case of certain contributions ("make-up contributions") with respect to a reemployed member of the uniformed services that are required or authorized under USERRA. The proposal would apply with respect to contributions made by an employer or elective deferrals made by an employee to an individual account plan or to contributions made by an employee to a defined benefit pension plan that provides for employee contributions

Under the proposal, if any make-up contribution is made by an employer with respect to a reemployed member of the uniformed services, then such contribution would not be subject to the generally applicable plan contribution limits (i.e., secs. 402(g), 403(b), 408, 415, or 457) or the limit on deductible contributions (i.e., sec. 404(a)) as applied with respect to the year in which the contribution is made. In addition, the make-up contribution will not be taken into account in applying the plan contribution or deductible contribution limits to any other contribution made during the year. However, the amount of any make-up contribution cannot exceed the aggregate amount of contributions that would have been permitted under the plan contribution and deductible contribution limits had the individual continued to be employed by the employer during the period of uniformed service.

The proposal also provides that a plan under which a make-up contribution is made on account of a reemployed member of the uniformed services would not be treated as failing to meet the qualified plan nondiscrimination, coverage, minimum participation, and top heavy rules

(i.e., secs. 401(a)(4), 401(a)(26), 401(k)(3), 401(m), 403(b)(12), 410(b), 416) by reason of the making of such contribution. Consequently, for purposes of applying the tests associated with these rules make-up contributions will not be taken into account. Further, the proposal provides that the requirements of an eligible deferred compensation plan (sec. 457) would not be violated as a result of a make-up contribution to such plan.

Under the proposal, a special rule would apply in the case of make-up contributions of salary reduction and employer matching amounts. A plan that provides for elective deferrals would be treated as meeting the requirements of USERRA if the employer permits reemployed service persons to make additional elective deferrals under the plan during the period which begins on the date of reemployment and has the same length as the lesser of (1) the period of the individual's absence due to uniformed service multiplied by three or (2) five years. The amount of the additional deferrals could not exceed the amount of deferrals that the individual would have been permitted to make under the plan and in accordance with the plan contribution limits described above had the individual continued to be employed by the employer during the period of uniformed service and received compensation at the same rate as received from the employer immediately before such service.

The employer would be required to match any additional elective deferrals at the same rate that would have been required had the deferrals actually been made during the period of uniformed service. Additional elective deferrals and employer matching contributions would be treated as make-up contributions for purposes of the rule exempting such contributions from qualified plan nondiscrimination, coverage, minimum participation, and top heavy rules as described above.

The proposal would clarify that USERRA does not require (1) any earnings to be credited to an employee with respect to any contribution before such contribution is actually made or (2) any make-up allocation of any forfeiture that occurred during the period of uniformed service.

The proposal would also provides that a plan may suspend repayment of a plan loan for the period of uniformed service without adverse consequences to the individual or the plan.

The proposal would also define compensation to be used for purposes of determining make-up contributions and would conform the rules contained in the Code with certain rights of reemployed veterans contained in USERRA pertaining to employee benefit plans.

Effective Date

The proposal would be effective as of December 12, 1994, the effective date of the benefits-related provisions of USERRA.