

[JOINT COMMITTEE PRINT]

**COMPARATIVE
SUMMARY**

OF

H.R. 4242

**TAX INCENTIVE ACT OF 1981
AS REPORTED BY THE
WAYS AND MEANS COMMITTEE
AND AS PROPOSED TO BE MODIFIED
BY THE
CONABLE-HANCE AND UDALL SUBSTITUTES**

PREPARED BY THE
STAFF OF THE
JOINT COMMITTEE ON TAXATION



JULY 27, 1981

CONTENTS

	Page
INTRODUCTION	1
COMPARATIVE SUMMARY OF PROVISIONS	3
A. Individual Income Tax Reductions	3
1. General rate reductions	3
2. Top marginal tax rate	3
3. Marriage penalty	4
4. Indexing	4
5. Zero bracket amount	4
6. Earned income credit	5
7. Child care credit	5
8. Foreign earned income	6
9. Capital gains on homes	6
10. Holding period for capital gains	6
11. Charitable contributions	7
B. Capital Cost Recovery Provisions	8
1. Underlying concept	8
2. Eligible property	8
3. Useful lives and methods of depreciation	8
4. Recapture of depreciation	10
5. Special depreciation for small business	10
6. Flexibility	10
7. Regular investment tax credit	11
8. At-risk limitation	11
9. Lease financing	11
10. Investment credit carryback	11
11. Construction period interest and taxes	12
12. Effective dates and phase in	12
C. Rehabilitation Expenditures	13
1. Investment tax credit	13
2. Demolition of historic structures	13
D. Incentives for Research and Experimentation	14
1. Tax credit for incremental expenditures	14
2. Charitable contributions	14
3. Allocation of research expenditures to foreign income	15
E. Small Business Provisions	16
1. Accumulated earnings credit	16
2. Subchapter S corporations	16
3. Loss on stock in small business corporations	16
4. Inventory accounting for small business	17
5. Investment credit for used property	17

COMPARATIVE SUMMARY OF PROVISIONS—Continued		Page
F. Windfall Profit Tax and Other Energy Tax Provisions		18
1. Royaltyowner credit or exemption		18
2. Newly discovered oil		18
3. Producer exemption		18
4. Front-end tertiary oil		19
5. Other windfall profit tax provisions		19
6. Percentage depletion		19
7. Foreign oil-related income		20
8. Residential energy credits		20
G. Corporate Tax Rate Reductions and Other Business Provisions		21
1. Top corporate tax rates		21
2. Graduated corporate tax rates		21
3. Stock options		21
4. Motor carrier operating rights		22
5. Targeted jobs credit		22
H. Savings Incentives		23
1. Individual retirement accounts		23
2. Self-employed retirement savings		23
3. Interest and dividend exclusion		23
4. Tax-exempt savings certificates		24
5. Dividend reinvestment		24
I. Estate and Gift Tax Provisions		25
J. Administrative Provisions		26
K. Commodity Straddles		27
L. Railroad Retirement Provisions		29
M. Other Provisions		30
1. Loss and credit carryovers		30
2. Unemployment compensation provisions		30
3. Fringe benefit and other regulations		30
4. Tax-exempt bond provisions		31
5. Payments to Guam and Virgin Islands		31
6. Tax treatment of State legislators		31
7. Mergers of savings and loan associations		32
8. Restricted property		32
COMPARATIVE REVENUE EFFECTS OF TAX PROPOSALS		33

INTRODUCTION

This pamphlet provides a brief, comparative summary of H.R. 4242, the Tax Incentive Act of 1981, as reported by the House Ways and Means Committee, as well as the proposed substitutes to be offered by Congressmen Conable and Hance and Congressman Udall. At the end of the comparative summary, there is a table comparing the revenue effects of the three proposals.

COMPARATIVE SUMMARY OF PROVISIONS

A. INDIVIDUAL INCOME TAX REDUCTIONS

1. General Rate Reductions

Present law

Individual income tax rates range from 14 to 70 percent.

Ways and Means Committee bill

The Ways and Means Committee bill provides rate reductions in all tax brackets but targets a more than proportionate rate cut to tax brackets affecting taxpayers whose income is between \$15,000 and \$50,000.

The rate cuts average 1 percent for 1981, 10 percent for 1982, and 16 percent for 1983. In addition, there will be a further rate reduction, which would provide a cumulative rate reduction of 22 percent, if certain economic and fiscal conditions for 1983 are met.

These reductions will be reflected in changes in taxes withheld from workers' paychecks on October 1, 1981, and July 1, 1982. The triggered tax reduction for 1984 would be reflected in withholding starting January 1, 1984.

The 1984 tax cuts will be triggered if the budget deficit for fiscal year 1983 is less than \$22.9 billion, the consumer price index for the third quarter of 1983 is 309 or less (1967=100), and 91-day Treasury bill rate 7.5 percent or less. These are consistent with the projections contained in the Administration's Mid-Session Review of the 1982 Budget.

Conable-Hance substitute

The substitute provides across-the-board rate reductions of 1¼ percent for 1981, 10 percent for 1982, 19 percent for 1983 and 23 percent for 1984. All tax rates will be reduced by approximately these percentages. Withholding changes will take place on October 1, 1981, July 1, 1982, and July 1, 1983.

Dodd substitute

The substitute provides a tax rate reduction of 3 percent in 1982 and 6 percent in 1983. The specific rate cuts are designed to provide tax cuts approximately large enough to offset the impact of one year's inflation in raising real tax burdens. Withholding changes will take place to reflect this rate reduction on July 1, 1982, and January 1, 1983.

2. Top Marginal Tax Rate

Present law

The top income tax rate is 70 percent. However, the top rate on earned income is limited to 50 percent. The top tax rate on long-term capital gains is 28 percent.

Ways and Means Committee bill

The bill reduces the top tax rate to 60 percent in 1982 and 50 percent in 1983. The top rate on long-term capital gains is reduced to 24 percent in 1982 and 20 percent thereafter.

Conable-Hance substitute

The substitute reduces the top tax rate to 50 percent in 1982. A 20 percent top tax rate on long-term capital gains applies to sales after June 9, 1981.

Udall substitute

The substitute reduces the top tax rate to 68 percent in 1982 and 6 percent in 1983.

3. Marriage Penalty**Present law**

When two persons with relatively equal incomes marry each other their tax is often higher than would be the case if they had remained single.

Ways and Means Committee bill

The bill provides a deduction for married couples equal to 10 percent of the first \$50,000 of earnings of the spouse with the lesser amount of earnings, effective in 1982.

Conable-Hance substitute

The substitute provides a similar marriage penalty deduction, but with a \$30,000 limit on the maximum amount of earnings eligible for the deduction. The deduction is phased in so that a 5-percent rate applies for 1982 and the permanent 10-percent rate takes effect in 1983.

Udall substitute

Same as Conable-Hance substitute.

4. Indexing**Present law**

Many of the numbers in the Internal Revenue Code which determine tax liability are fixed in terms of dollars. Thus, when inflation occurs, the value of these dollar amounts declines in relation to purchasing power.

Ways and Means Committee bill

No provision.

Conable-Hance substitute

Starting in 1985, the income tax brackets, the zero bracket amount and the personal exemption will be adjusted annually for inflation (as measured by the consumer price index).

Udall substitute

No provision.

5. Zero Bracket Amount**Present law**

There is no income tax on the first \$2,300 of taxable income for single return and \$3,400 for a joint return. This amount is referred to as the zero bracket amount and serves as a floor under allowable itemized deductions.

Ways and Means Committee bill

The bill increases the zero bracket amount for single returns by \$50 in 1981, \$200 in 1982 and, if additional tax cuts for 1984 are triggered, by a further \$100 in that year. For joint returns, the increase is \$100 for 1981, \$400 for 1982 and, if the additional tax cuts are triggered, a further \$200 in 1984.

Conable-Hance substitute

No provision.

Udall substitute

The zero bracket amount is increased by \$200 for single returns and \$400 for joint returns, starting in 1982.

6. Earned Income Credit**Present law**

Families with children are allowed a refundable tax credit (i.e., a credit that is refunded to the extent it exceeds tax liability) equal to 10 percent of the first \$5,000 of earned income. The credit phases out as income increases from \$6,000 to \$10,000.

Ways and Means Committee bill

The earned income credit is increased to 11 percent of the first \$5,000 of earnings, and the phaseout range is increased to between \$8,000 and \$12,000 of income. If the 1984 tax cuts are triggered, there would be a further increase in the credit to 11 percent of the first \$6,000 of earnings, phased out between \$9,000 and \$14,000 of income.

Conable-Hance substitute

No provision.

Udall substitute

The earned income credit is increased to 11 percent of the first \$5,000 of earnings, phased out between \$7,000 and \$11,000 of income.

7. Child Care Credit**Present law**

There is a tax credit for 20 percent of expenditures for the care of children and other dependents incurred in connection with the taxpayer's employment, up to a maximum of \$2,000 of expenditures for each of the taxpayer's first two dependents.

Ways and Means Committee bill

The rate of the child care credit is increased to 40 percent for taxpayers with income below \$11,000. This rate is then phased down to 20 percent as income rises from \$11,000 to \$30,000. The maximum amount of expenditures eligible for the credit is increased to \$2,400 for each of the first two dependents.

Conable-Hance substitute

No provision.

Udall substitute

Same as Ways and Means Committee bill.

8. Foreign Earned Income

Present law

A variety of deductions and exclusions are provided for income earned abroad, including deductions for excess cost-of-living, housing, education, and home leave and an exclusion for camps in hardship areas.

Ways and Means Committee bill

The bill replaces the existing provisions for income earned abroad with an exemption for the first \$95,000 of such income and an exclusion for excess housing costs. The maximum exclusion will be \$75,000 in 1982 and will be phased up to \$95,000 in \$5,000 increments.

Conable-Hance substitute

Same as Ways and Means Committee bill.

Udall substitute

No provision.

9. Capital Gains on Homes

Present law

The tax on the gain on the sale of a taxpayer's principal residence is deferred if the proceeds from the sale are reinvested in a new principal residence within 18 months. In addition, taxpayers age 55 or over may exclude up to \$100,000 of gain on the sale of a principal residence.

Ways and Means Committee bill

The bill increases the period in which gain must be reinvested under the rollover provision to 24 months, and increases the maximum exclusion for taxpayers age 55 or over to \$125,000.

Conable-Hance substitute

Same as Ways and Means Committee bill.

Udall substitute

No provision.

10. Holding Period for Capital Gains

Present law

With some exceptions, an asset must be held for more than 1 year in order for gain on the sale of that asset to qualify as a long-term capital gain and be eligible for the exclusion for 60 percent of long-term capital gains.

Ways and Means Committee bill

No provision.

Conable-Hance substitute

The holding period is reduced to 6 months for all assets.

Udall substitute

No provision.

11. Charitable Contributions***Present law***

A deduction for charitable contributions is allowed only for a taxpayer who itemizes his deductions.

Ways and Means Committee bill

No provision.

Conable-Hance substitute

The substitute permits taxpayers to deduct a percentage of their charitable contributions even if they do not itemize the rest of their deductions. For 1982-84, the percentage is 25 percent; for 1985, it is 50 percent; and for 1986, it is 100 percent. For 1982-84, the maximum deduction is \$25. The provisions terminate after 1986.

Udall substitute

No provision.

B. CAPITAL COST RECOVERY PROVISIONS

1. Underlying Concept

Present law

The present system is designed to spread depreciation deductions over the useful life of an asset so that deductions for the cost of the asset are matched with the income produced by the asset. The key determinants of the depreciation deduction are the useful life over which the property is depreciated and the method used to allocate deductions over that life.

Ways and Means Committee bill

The present system is phased out and replaced by a system of expensing for personal property (i.e., machinery and equipment). Under expensing, the cost of eligible property will be deducted in the year the property is placed in service.

For real estate, costs will be recovered over 15 years. The costs of long-lived public utility property and certain other kinds of property costs will be recovered over recovery periods of 10 or 15 years.

Conable-Hance substitute

The costs of eligible property will be recovered over recovery periods of 3, 5, 10 and 15 years.

Udall substitute

The Udall substitute is the same as the Ways and Means Committee bill with the exception of a longer recovery period for structures. Thus, in the following comparison, it is not listed separately except in items 3b, 10 and 11.

2. Eligible Property

Ways and Means Committee bill

Property eligible for the new system is essentially all depreciable property other than certain property not eligible for the investment tax credit.

Conable-Hance substitute

Essentially the same as the Ways and Means Committee bill.

3. Useful Lives and Methods

a. Personal property (i.e., equipment)

Present law

Useful lives are determined under the Asset Depreciation Range (ADR) system by the Treasury. Taxpayers may elect a life 20 percent longer or shorter than the Treasury's ADR class life.

Taxpayers may use the straight-line method, the 200-percent declining balance method or the sum-of-the-year's digits method for new personal property and the 150-percent declining balance method or the straight-line method for used personal property.

Ways and Means Committee bill

General rule.—The cost of personal property is written off in the year placed in service.

10-year class.—Railroad tank cars, oil pipelines, mobile homes, theme park structures and public utility property with an ADR life between 18 and 25 years are put in a 10-year class and depreciated under a 150-percent declining balance method.

15-year class.—Public utility property with an ADR life above 25 years is depreciated using the 150-percent declining balance method with a 15-year life.

Conable-Hance substitute

Personal property is put into one of four classes. In each class there is a statutory method of cost recovery which, in the years 1981 through 1984, approximates the 150-percent declining balance method, with a switch to the straight-line method. In 1984, the method is accelerated to approximate the 175-percent declining balance method, with a switch to the sum-of-the-years-digits method, and in 1986 there is a further acceleration to an approximation of the 200-percent declining balance method, with a switch to SYD.

3-year class.—This class includes autos, light duty trucks, R&D equipment, and any other property with an ADR life of 4 years or less.

5-year class.—This class includes most other equipment and single-purpose agricultural structures.

10-year class.—This class includes railroad tank cars, theme park structures, and public utility property with an ADR class life of 18 to 25 years.

15-year class.—This class includes public utility property with an ADR class life exceeding 25 years.

b. Real Property

Present law

Taxpayers use lives which are based on the facts and circumstances pertaining to each structure.

New residential structures are depreciated under the straight-line method, the 200-percent declining balance method or the sum-of-the-years-digits method. New nonresidential property is depreciated under the 150-percent declining balance method or the straight-line method. Used residential property is depreciated under the 125-percent declining balance method or the straight-line method. Used nonresidential property is limited to the straight-line method.

Ways and Means Committee bill

All structures are depreciated over a 15-year recovery period unless the taxpayer elects a longer recovery period. Taxpayers may use either the straight-line method or the 150-percent declining balance method (200 percent for low-income housing or nonresidential structures in targeted areas).

Conable-Hance substitute

Essentially the same as the Ways and Means Committee bill, except that all structures are eligible for the 200-percent declining balance method.

Udall substitute

Same as Ways and Means Committee bill, except that the recovery period is 20 years.

4. Recapture of Depreciation**Present law**

When a taxpayer sells a structure, gain is treated as ordinary income to the extent of the excess of accelerated depreciation previously taken over what would have been straight-line depreciation.

Ways and Means Committee bill

If a taxpayer uses straight-line depreciation on a structure, all gain is capital gain. If a taxpayer elects accelerated depreciation on a non-residential structure, all depreciation is recaptured as ordinary income. If a taxpayer elects accelerated depreciation on a residential structure, only the excess of accelerated over straight-line depreciation is recaptured as ordinary income.

Conable-Hance substitute

Same as Ways and Means Committee bill.

5. Special Depreciation for Small Business**Present law**

A taxpayer may deduct in the year property is placed in service "bonus" depreciation equal to 20 percent of up to \$10,000 of the cost of certain depreciable equipment.

Ways and Means Committee bill

Up to \$25,000 of eligible property is eligible for immediate expensing, starting in 1981 regardless of the other phase-in rules.

Conable-Hance substitute

There is an election to expense up to \$5,000 in 1982 and 1983, \$7,500 in 1984 and 1985, and \$10,000 in 1986 and thereafter.

6. Flexibility**Present law**

Taxpayers may vary their useful lives under the ADR system by 20 percent and may elect a variety of different methods of depreciation.

Ways and Means Committee bill

Taxpayers are allowed to expense less than the full amount eligible for expensing. Unexpensed costs are recovered under the straight-line method over the ADR class life. For real property, taxpayers may elect the straight-line method over a 25-, 35- or 45-year recovery period, instead of the 15-year recovery period.

Conable-Hance substitute

Taxpayers are allowed to use the straight-line method and to elect two longer recovery periods for each class of property.

7. Regular Investment Tax Credit**Present law**

Taxpayers who purchase eligible equipment are allowed an investment tax credit of 3 $\frac{1}{3}$ percent for property with a useful life of 3 or 4 years, 6 $\frac{2}{3}$ percent for property with a useful life of 5 or 6 years, and 10 percent for property with a useful life of 7 or more years.

Ways and Means Committee bill

The investment tax credit is phased out between 1981 and 1985 as the expensing system is phased in.

Conable-Hance substitute

The investment tax credit is 6 percent for eligible property in the 3-year class and 10 percent for property in the other classes.

8. At-Risk Limitation**Present law**

For individuals and closely held corporations, certain tax losses are limited to the extent to which the taxpayer is "at risk" (i.e., is investing his own money or is personally liable for loans) with respect to the activity producing the loss.

Ways and Means Committee bill

No provision.

Conable-Hance substitute

The investment tax credit is limited to that portion of the investment with respect to which a taxpayer is at risk. There are exceptions for amounts borrowed from certain kinds of financial institutions.

9. Lease Financing**Present law**

Under certain circumstances, a lease will not be recognized as such for tax purposes; that is, the lessor will not be eligible for depreciation, the investment credit and any other tax benefits which result from placing an asset in service.

Ways and Means Committee bill

No provision.

Conable-Hance substitute

The rules on recognition of leases of corporate lessors for tax purposes are considerably liberalized.

10. Investment Credit Carryback**Present law**

Taxpayers may carry back unused investment tax credits and use them against tax liability incurred in up to 3 prior years, subject to whatever limitations on use of the investment credit applied in those years (e.g., the limitation on the credit to a percentage of tax liability).

Ways and Means Committee bill

Taxpayers in six distressed industries—autos, steel, paper, railroads, mining, and airlines—are allowed to carry back unused investment credits to 1962 and use them against all regular tax liability incurred in those activities in those years.

Conable-Hance substitute

No provision.

Udall substitute

No provision.

11. Construction Period Interest and Taxes**Present law**

Taxpayers must generally capitalize interest and taxes paid during the construction period of a building and amortize those costs over a 10-year period. However, the effective date of this rule was postponed for low-income housing until 1982.

Ways and Means Committee bill

The bill postpones the effective date of the amortization of construction period interest and taxes for low-income housing for 5 more years. As a result, these expenses will continue to be deducted in the year incurred until 1987.

Conable-Hance substitute

The substitute provides a one-year postponement.

Udall substitute

No provision.

12. Effective Dates and Phase-in**Ways and Means Committee bill**

The present depreciation rules and the investment credit are phased out between 1981 and 1985. For property placed in service in 1981, 20 percent will be eligible for the new system. The percentage will be 40 percent in 1982, 60 percent in 1983, and so forth.

Initially the new system will consist of a 2-year write-off. However, between 1985 and 1990, this 2-year writeoff will be phased in to a full expensing system. A special rule for small businesses permits taxpayers to expense fully up to \$25,000 of investment starting in 1981.

Conable-Hance substitute

The new rules are effective for property placed in service in 1981 and future years. However, there is an acceleration of the method of depreciation for personal property in 1985, and the permanent rule for personal property takes effect in 1986.

C. REHABILITATION EXPENDITURES

1. Investment Tax Credit

Present law

There is a 10-percent investment tax credit for expenditures to rehabilitate nonresidential structures more than 19 years old.

Ways and Means Committee bill

The bill replaces the present investment tax credit for rehabilitations with a new graduated tax credit. The credit will be 15 percent for nonresidential buildings 30 to 39 years old, 20 percent for nonresidential buildings more than 39 years old and 25 percent for certified historic structures. For the 15-percent and 20-percent credits, the basis for recovery allowances will be reduced by the amount of the credit.

Conable-Hance substitute

Essentially the same as Ways and Means Committee bill.

Udall substitute

Same as Ways and Means Committee bill.

2. Demolition of Historic Structures

Present law

Buildings constructed at the site of a demolished historic structure must be depreciated under the straight-line method, and demolition costs may not be deducted.

Ways and Means Committee bill

The two demolition penalties of present law are repealed.

Conable-Hance substitute

Only the straight-line requirement is repealed.

Udall substitute

Same as Ways and Means Committee bill.

**D. INCENTIVES FOR RESEARCH AND
EXPERIMENTATION**

1. Tax Credit for Incremental Expenditures

Present law

A taxpayer may expense research and experimental expenditures.

Ways and Means Committee bill

The bill provides a 25-percent tax credit for expenditures on research and experimentation in excess of a 3-year moving average base period. All such expenditures, other than overhead and depreciation, are taken into account. Amounts contributed to a university or certain other tax-exempt institutions for research are eligible for the credit but are excluded from the base. The credit sunsets after 1985.

Conable-Hance substitute

Same as Ways and Means Committee bill, except that contributions to a university or other tax exempt institution are included in the base.

Udall substitute

Same as Ways and Means Committee bill.

2. Charitable Contributions

Present law

When the sale of property would generate ordinary income to the taxpayer, charitable contributions of that property are generally limited to the taxpayer's cost or other basis in the property. There is an exception to this rule for contributions of property for use in the care of the needy, the ill or infants, in which case a deduction is allowed for the lesser of (1) the basis plus 50 percent of the depreciation or (2) twice the basis.

Ways and Means Committee bill

The rule that now applies for property used to care for the needy, the ill or infants is extended to contributions of research equipment made by a corporation to a college or university.

Conable-Hance substitute

Same as Ways and Means Committee bill.

Udall substitute

No provision.

3. Allocation of Research Expenditures to Foreign Income

Present law

Taxpayers must allocate research expenditures between their domestic and foreign source income. To the extent that such expenditures are allocated to foreign source income, the taxpayer's foreign tax credit limitation is reduced, which may reduce his utilization of foreign tax credits.

Ways and Means Committee bill

For one year, taxpayers must allocate all research expenditures on activities conducted in the United States to U.S.-source income. The Treasury is required to study the impact of its allocation regulations.

Conable-Hance substitute

Same as Ways and Means Committee bill, except the rule requiring U.S. allocation is permanent.

Udall substitute

No provision.

E. SMALL BUSINESS PROVISIONS

1. Accumulated Earnings Credit

Present law

There is a tax on earnings accumulated in a corporation beyond the reasonable needs of the business. However, there is a credit against this tax of \$150,000.

Ways and Means Committee bill

The accumulated earnings credit is generally increased to \$250,000.

Conable-Hance substitute

Essentially the same as Ways and Means Committee bill.

Udall substitute

No provision.

2. Subchapter S Corporations

Present law

Small business corporations meeting certain conditions are taxed essentially as partnerships. These subchapter S corporations may not have more than 15 shareholders.

Ways and Means Committee bill

The maximum number of shareholders is increased to 25, and certain kind of trusts are made eligible shareholders.

Conable-Hance substitute

Same as Ways and Means Committee bill.

Udall substitute

No provision.

3. Losses on Stock of Small Business Corporations

Present law

An individual may treat up to \$50,000 of loss on small business corporation stock as ordinary (rather than capital) loss.

Ways and Means Committee bill

The bill extends ordinary loss treatment to preferred stock.

Conable-Hance substitute

No provision.

Udall substitute

No provision.

4. Inventory Accounting for Small Businesses

Present law

Taxpayers with inventories must use the accrual method of accounting rather than the cash method.

Ways and Means Committee bill

The Treasury Department is required to study LIFO accounting and cash accounting.

Conable-Hance substitute

The substitute provides for certain simplifying changes in the LIFO inventory accounting method. These are (1) permitting the income from the increase in inventory value required when LIFO is elected to be spread over 3 years; (2) permitting small businesses (\$1 million of gross revenue) to use one inventory pool; (3) requiring the Treasury Department to prescribe regulations providing for the use of published government indexes. In addition, the Treasury Department is required to study LIFO accounting and cash accounting.

Udall substitute

No provision.

5. Investment Credit for Used Property

Present law

The investment tax credit may be claimed on up to \$100,000 of used property each year.

Ways and Means Committee bill

The bill phases out the regular investment credit. During the phase-out period, the limit on the credit for used property is increased to \$150,000 in 1981, \$191,667 in 1982, \$275,000 in 1983, and \$525,000 in 1984.

Conable-Hance substitute

The used property limitation is increased to \$125,000 in 1982 through 1984 and \$150,000 thereafter.

Udall substitute

Same as Ways and Means Committee bill.

F. WINDFALL PROFIT TAX AND OTHER ENERGY TAX PROVISIONS

1. Royaltyowner Credit or Exemption

Present law

Under the windfall profit tax, royaltyowners are treated essentially as major oil companies. However, for 1980, there was a credit against the first \$1,000 of windfall profit tax paid by a royaltyowner.

Ways and Means Committee bill

The bill provides a \$2,500 royaltyowner credit for 1981 and an exemption for royaltyowners from the windfall profit tax of up to 1 barrel per day from 1982 through 1984, 2 barrels a day in 1985 and 3½ barrels a day in subsequent years.

Conable-Hance substitute

There is a royaltyowner credit for 1981 of \$2,500 and an exemption for 2 barrels per day in 1982 through 1984 and 4 barrels per day thereafter.

Udall substitute

No provision.

2. Newly Discovered Oil

Present law

The windfall profit tax rate on newly discovered oil (i.e., oil produced on properties not in production in 1978) is presently 30 percent.

Ways and Means Committee bill

No provision.

Conable-Hance substitute

The tax rate on newly discovered oil is reduced to 15 percent over a 5-year period. Specifically, the rates will be 27½ percent in 1982, 25 percent in 1983, 22½ percent in 1984, 20 percent in 1985 and 15 percent after 1985.

Udall substitute

No provision.

3. Producer Exemption

Present law

Independent producers are allowed reduced tax rates on up to 1,000 barrels per day of old and stripper oil (tiers 1 and 2 of the tax, respectively). For old oil, the rate reduced from 70 percent to 50 percent. For stripper oil, the rate is reduced from 60 percent to 30 percent.

Ways and Means Committee bill

All producers are allowed an exemption for up to 500 barrels per day for new, heavy and tertiary oil (tier 3 of the tax). In addition, there is an exemption for old and stripper oil of up to 100 barrels per day in 1982 through 1984, 200 barrels per day in 1985 and 350 barrels per day in 1986 and subsequent years. The aggregate exemption under these two provisions is limited to 500 barrels per day.

Conable-Hance substitute

There is an exemption for an unlimited amount of stripper oil produced by independent producers after 1982.

Udall substitute

No provision.

4. Front-end Tertiary Oil**Present law**

There is a windfall profit tax exemption for oil which is deregulated under the Department of Energy's front-end tertiary provision if that oil would not have been deregulated under any other pricing provisions. As a result, this exemption expired when President Reagan decontrolled oil prices on January 28, 1981.

Ways and Means Committee bill

The bill extends the front-end tertiary exemption to provide independent producers with benefits approximately equivalent to what they lost when the front-end tertiary tax exemption expired after decontrol.

Conable-Hance substitute

No provision.

Udall substitute

No provision.

5. Other Windfall Profit Tax Provisions**Ways and Means Committee bill**

The bill exempts oil owned by residential child care agencies and treats natural gas retailers as nonintegrated producers for purposes of the special tax rates for independent producers.

Conable-Hance substitute

The substitute includes the exemption for child care agencies but not the provision for natural gas retailers.

Udall substitute

No provision.

6. Percentage Depletion**Present law**

Taxpayers other than integrated companies are allowed a percentage depletion deduction of up to 1,000 barrels of oil or the equivalent amount of gas per day. Until recently, this was 22 percent of gross income from a property. However, pursuant to changes enacted in 1975,

the rate of percentage depletion phased down to 20 percent in 1981, and will continue to phase down to a permanent level of 15 percent in 1984.

Ways and Means Committee bill

No provision.

Conable-Hance substitute

The substitute continues percentage depletion for oil and gas at a 22-percent rate.

Udall substitute

The substitute repeals percentage depletion for oil and gas, starting in 1982.

7. Foreign Oil-Related Income

Present law

Treasury collects relatively little tax on foreign oil-related income because of the use of the foreign tax credit and losses on foreign exploration.

Ways and Means Committee bill

The bill exempts foreign oil extraction income from tax, denies deductions and credits attributable to that income, and currently taxes oil companies on certain foreign oil related income.

Conable-Hance substitute

No provision.

Udall substitute

Same as Ways and Means Committee bill.

8. Residential Energy Credits

Present law

There is a 15-percent tax credit for expenditures for insulation and certain other energy conserving items and a 40-percent credit for solar and other renewable energy expenditures incurred in connection with a taxpayer's residence.

Ways and Means Committee bill

The bill provides a tax credit of up to \$2,000 for builders of homes embodying passive solar energy systems.

Conable-Hance substitute

The substitute extends the 15-percent residential energy credit to woodburning stoves.

Udall substitute

No provision.

**G. CORPORATE TAX REDUCTIONS AND OTHER
BUSINESS PROVISIONS**

1. Top Corporate Tax Rate

Ways and Means Committee bill

The bill reduces the top corporate tax rate from 46 percent to 43 percent in 1984, 40 percent in 1985, 37 percent in 1986 and 34 percent in 1987 and subsequent years.

Conable-Hance substitute

No provision.

Udall substitute

No provision.

2. Graduated Corporate Tax Rates

Present law

The corporate tax rate is 17 percent on the first \$25,000 of taxable income, 20 percent on the next \$25,000, 30 percent on taxable income between \$50,000 and \$75,000, and 40 percent on taxable income between \$75,000 and \$100,000.

Ways and Means Committee bill

The bill phases in a reduction in the graduated corporated tax rates and a widening of the brackets starting January 1, 1982. The permanent rates, to take effect in 1984, are 15 percent on the first \$50,000 of taxable income, 20 percent on the next \$50,000 of taxable income, 25 percent of taxable income between \$100,000 and \$150,000 and 30 percent of taxable income between \$150,000 and \$200,000 of taxable income.

Conable-Hance substitute

The substitute reduces the tax rate in the bottom two corporate brackets (those applying to taxable income below \$50,000) by one percentage point in 1982 and by one additional point in 1983 and subsequent years.

Udall substitute

The Udall substitute is the same as the Ways and Means Committee bill, except that the first stage of rate reductions takes effect on July 1, 1982.

3. Stock Options

Present law

When an employee exercises stock options, the difference between the option price and the fair market value of the stock at the time of exercise is generally taxed at ordinary income rates, and the employer is allowed a deduction for that amount.

Ways and Means Committee bill

The bill provides for restricted stock options under which there will be no tax consequences when the option is granted or exercised, and the difference between the exercise price and the sales price of the stock will be taxed as a capital gain when the stock is sold by the employee. Only options (including options granted since 1976) to purchase up to \$75,000 of stock per year will qualify.

Conable-Hance substitute

Similar to Ways and Means Committee bill except (1) options must be exercised in the order granted, and (2) the application of the new rule to options granted during the years 1976-1980 is limited to a total of \$150,000.

Udall substitute

No provision.

4. Motor Carrier Operating Rights**Present law**

No deduction is allowed for the decline in value of property unless there is a sale or other disposition.

Ways and Means Committee bill

The bill permits 60-month amortization for the basis of motor carriers' operating rights held on July 1, 1980.

Conable-Hance substitute

Same as Ways and Means Committee bill.

Udall substitute

No provision.

5. Targeted Jobs Credit**Present law**

There is a tax credit for hiring individuals from one of seven targeted groups. The credit is equal to 50 percent of the first \$6,000 of first-year wages and 25 percent of the first \$6,000 of second year wages. This credit expires after 1981.

Ways and Means Committee bill

The bill extends the credit through 1984 and increases the amount of eligible wages to \$10,000 per year. It merges the targeted jobs credit with the existing credits for hiring AFDC recipients and WIN registrants. It also limits the credit for cooperative education students and largely eliminates retroactive certifications.

Conable-Hance substitute

The substitute extends the credit through 1983, expands it to include WIN registrants and people involuntarily terminated from CETA jobs and eliminates cooperative education students and retroactive certifications.

Udall substitute

No provision.

H. SAVINGS INCENTIVES

1. Individual Retirement Accounts

Present law

Individuals not participating in tax qualified pension plans may deduct contributions to individual retirement accounts (IRAs) up to the lesser of \$1,500 or 15 percent of compensation. The limit is increased to \$1,750 where a nonearning spouse is a beneficiary (a spousal IRA).

Ways and Means Committee bill

The bill increases the limit on IRA contributions to the lesser of 100 percent of compensation or \$2,000. In addition, the bill allows active participants in tax qualified plans to be eligible for IRA deductions.

Conable-Hance substitute

Same as Ways and Means Committee bill except that the contribution limit is \$2,250 for a spousal IRA.

Udall substitute

No provision.

2. Self-employed Retirement Savings

Present law

Self-employed individuals may deduct contributions to a self-employed retirement plan up to the lesser of \$7,500 or 15 percent of self-employment earnings.

Ways and Means Committee bill

The bill increases the contribution limit to \$15,000.

Conable-Hance substitute

Same as Ways and Means Committee bill.

Udall substitute

No provision.

3. Interest and Dividend Exclusion

Present law

For the years 1981 and 1982, there is an exclusion for up to \$200 of interest and dividends (\$400 for a joint return). After 1982, the law reverts to the pre-1981 dividend exclusion of up to \$100 per taxpayer.

Ways and Means Committee bill

The bill terminates the \$200 interest and dividend exclusion after 1981, when the law will revert to the prior \$100 dividend exclusion.

Conable-Hance substitute

Like the Ways and Means Committee bill, the substitute terminates the \$200 interest and dividend exclusion after 1981. However, beginning in 1985 it introduces a new interest exclusion for 15 percent of interest received in excess of interest deducted other than business and home mortgage interest. This net interest exclusion is limited to \$3,000 of net interest per year (\$6,000 for joint returns).

Udall substitute

No provision.

4. Tax-Exempt Savings Certificates**Present law**

No provision.

Ways and Means Committee bill

There is an exclusion for up to \$1,000 (\$2,000 for a joint return) of interest on "all savers" certificates. These certificates must have an interest yield no greater than 70 percent of the Treasury bill rate, and institutions issuing these certificates must invest certain amounts in residential financing or agricultural loans.

Conable-Hance substitute

Essentially the same as Ways and Means Committee bill.

Udall substitute

No provision.

5. Dividend Reinvestment**Present law**

No provision.

Ways and Means Committee bill

The bill permits taxpayers to exclude up to \$1,500 a year (\$3,000 for a joint return) of dividends received from public utility corporations if the dividends are reinvested in stock in the utility. The dividends excluded under this provision will reduce the taxpayer's basis in the stock and thus will increase the taxpayer's capital gain when he sells the stock.

Conable-Hance substitute

Same as Ways and Means Committee bill.

Udall substitute

No provision.

I. ESTATE AND GIFT TAX PROVISIONS

The Ways and Means Committee bill and the Conable-Hance substitute contain the same provisions with respect to estate and gift taxes. The most important of these provisions are the following:

(1) An increase in the level of transfers at which the estate and gift tax rates begin from \$175,625 to \$600,000, phased in over a 6-year period.

(2) Elimination of the estate and gift tax on all gifts and bequests between spouses.

(3) An increase in the gift tax exclusion for gifts in any single year to any one person from \$3,000 to \$10,000 plus an unlimited exclusion for gifts paid for medical expenses and school tuition.

(4) Liberalization of the provision for current use valuation of farms and real estate, including an increase in the maximum reduction in the taxable estate resulting from this provision from \$500,000 to \$1 million.

(5) Liberalization of the provisions of present law permitting deferred payment of estate tax when the estate consists largely of a closely held business.

The Udall substitute includes only the provision for an unlimited marital deduction and increases the level of taxable transfers at which the estate and gift tax rate begins only for farms and small businesses and only to \$350,000.

J. ADMINISTRATIVE PROVISIONS

The Ways and Means Committee bill and the Conable-Hance substitute make similar changes in administrative provisions. With one exception, noted below, the Udall substitute does not contain these changes. The most significant of the administrative provisions included in the bills are the following:

(1) Requirement that large corporations cover 80 percent of their current year's tax liability with estimated tax payments. (This is in the Udall substitute as well.)

(2) More current adjustment of the interest rate on tax overpayments and deficiencies to 100 percent of the prime interest rate.

(3) Additional civil and criminal penalties for filing of false W-4 forms.

(4) A new "no fault" penalty in cases where tax is assessed because the taxpayer overvalued certain property, and an increase in the negligence penalty in certain cases.

(5) An increase in the exemption from the estimated tax penalty for individuals from \$100 to \$500, phased in over a 4-year period.

K. COMMODITY STRADDLES

Present law

Under present law, taxpayers may avail themselves of a number of provisions in the law which may permit the use of commodity straddles and related transactions to defer tax and convert ordinary income and short-term capital gains into long-term capital gains. (A straddle exists when an investor holds equivalent long and short positions in assets whose price movements are likely to be closely correlated.)

Ways and Means Committee bill

Loss limitation.—The bill limits the deduction for losses from commodity-related straddle transactions to the amount of gains from commodity-related transactions, reduced by losses on non-straddle commodity-related transactions. This loss limitation rule applies to straddles in futures contracts, commodities, Treasury bills, other debt instruments, options and other interests in Treasury bills and debt instruments, forward contracts and currency. There is an exemption for hedging transactions.

Capitalization of interest and carrying charges.—The bill requires that interest and carrying charges incurred to purchase or carry a commodity held as part of a straddle be capitalized, rather than expensed. However, there is an exemption from this rule for hedging transactions and a special rule for traders of commodity futures contracts.

Treasury bills.—The bill treats Treasury bills as capital assets, so that gain or loss on their sale is treated as capital gain or loss, not ordinary gain or loss. The determination of how much of the appreciation of a Treasury bill sold before maturity is capital gain and how much is interest income is based on the market discount on the bill at the time of its acquisition by the taxpayer. Thus, if a bill is purchased six months before maturity and held for three months, one-half of the market discount is treated as interest and taxed as ordinary income and any additional difference between the sales price and the purchase price is treated as capital gain or loss.

Dealer designation rule.—The bill requires dealers in securities to identify a security as being held for investment (and thereby eligible for capital gain treatment) on the day of acquisition rather than 30 days after acquisition, as is the case under present law.

Sale or exchange requirement.—The bill requires that all taxable dispositions of capital assets which are actively traded or which are commodity related assets be treated as sales or exchanges, thereby producing capital gain or loss.

Conable-Hance substitute

Same as Ways and Means Committee bill.

Udall substitute

Mark-to-market.—Under the substitute, regulated futures contracts are marked to market at the earlier of disposition or the end of the tax year. Under this rule, gains and losses in a taxpayer's futures account are treated as recognized at the close of the year. Net gains on regulated futures contracts are treated as if 50 percent of the gain were short-term gain and 50 percent of the gain were long-term gain, thus providing a maximum tax rate of 35 percent on gains on regulated futures contracts after 1981. Furthermore, the substitute provides a 3-year capital loss carryback for losses on regulated futures contracts. These losses can be deducted against gains from regulated futures contracts in the three prior years.

Loss deferral.—In the case of straddles which do not involve positions in regulated futures contracts, losses are deferred to the extent there are unrealized gains in offsetting positions. However, in the case of straddles which consist of one or more positions in regulated futures contracts, the taxpayer may elect either to have all positions marked to market, or alternatively, have the leg that is a regulated futures contract exempted from the mark-to-market rule and treated, along with the other positions making up the straddle, under the general loss deferral rule. The substitute also authorizes regulations extending present law wash-sale and short-sale principles to straddle positions.

Capitalization of interest and carrying charges.—Same as Ways and Means Committee bill, except no exception for traders.

Hedging exception.—The substitute exempts hedging transactions from the mark-to-market, loss deferral and capitalization rules.

Treasury bills.—Same as Ways and Means Committee bill.

Dealer identification of securities.—Same as Ways and Means Committee bill.

Sale or exchange.—Same as Ways and Means Committee bill.

L. RAILROAD RETIREMENT TAXES

Present law

The railroad retirement tax on employers is 9.5 percent of covered payroll.

Ways and Means Committee bill

The bill increases the tax on employers to 11.75 percent and provides a new tax of 2 percent on the compensation of employees.

Conable-Hance substitute

Essentially the same as Ways and Means Committee bill.

Udall substitute

Same as Ways and Means Committee bill.

M. MISCELLANEOUS PROVISIONS

1. Loss and Credit Carryovers

Present law

Generally, unused investment credits and net operating losses can be carried forward for 7 years.

Ways and Means Committee bill

The bill extends the investment credit and the net operating loss carryover periods to 20 years.

Conable-Hance substitute

Same as Ways and Means Committee bill.

Udall substitute

No provision.

2. Unemployment Compensation Provisions

Ways and Means Committee bill

The bill begins to charge interest on new loans to State unemployment compensation trust funds. In addition, for those States with outstanding debt which meets certain solvency conditions, it freezes the net Federal unemployment tax at the higher of 0.6 percent or the previous year's tax.

Conable-Hance substitute

No provision.

Udall substitute

No provision.

3. Fringe Benefits and Other Regulations

Present law

Congress has enacted moratoriums on the issuance of Treasury regulations on fringe benefits and commuting expenses to temporary job sites. These expired on May 31, 1981.

Ways and Means Committee bill

The bill extends these moratoriums for 2 years.

Conable-Hance substitute

Same as Ways and Means Committee bill.

Udall substitute

No provision.

4. Tax-Exempt Bond Provisions

Present law

Interest on obligations of State and local government is exempt from tax. However, there are restrictions on the exemption for industrial development bonds; that is, bonds whose proceeds are used for the benefit of the private sector.

Ways and Means Committee bill

The bill exempts interest on industrial development bonds used to finance buses, subways cars and similar equipment leased to publicly owned mass transit system. It also exempts interest on obligations of volunteer fire departments.

Conable-Hance substitute

Same as Ways and Means Committee bill except the provision for volunteer fire departments is prospective.

Udall substitute

No provision.

5. Payments to Guam and the Virgin Islands

Present law

Guam and the Virgin Islands have "mirror image" tax systems to that of the United States. Thus, whenever the U.S. tax law changes, the tax law of these possessions automatically changes as well.

Ways and Means Committee bill

The bill authorizes an appropriation to the governments of Guam and the Virgin Islands to compensate them for the revenue lost as a result of the tax reductions in this bill.

Conable-Hance substitute

No provision.

Udall substitute

No provision.

6. Tax Treatment of State Legislators

Present law

Under present law, it is unclear how the business expenses for away-from-home travel expenses of State legislators are to be treated. Legislation attempting to clarify those rules on a temporary basis expired at the end of 1980.

Ways and Means Committee bill

The bill extends through 1982 a modified version of the recently expired treatment of the business expenses of State legislators.

Conable-Hance substitute

Same as Ways and Means Committee bill, except that the extension is permanent.

Udall substitute

Same as Ways and Means Committee bill.

7. Mergers of Savings and Loans***Present law***

Present law imposes a number of restrictions on tax-free corporate reorganizations and "trafficking" in loss carryovers through such reorganizations.

Ways and Means Committee bill

No provision.

Conable-Hance substitute

The substitute provides special rules which allow tax-free reorganizations of mutually-owned savings and loan associations, cooperative banks and mutual savings banks and the carryover of tax attributes in such reorganizations. In addition, the substitute exempts these institutions from the normal rules relating to contributions to capital by nonshareholders and rules relating to recapture of bad debt deductions upon distributions out of bad debt or supplemental reserves in the case of payment and repayments of financial assistance by Federal Savings and Loan Insurance Corporation.

Udall substitute

No provision.

8. Restricted Property***Present law***

Property transferred in connection with the performance of services is not taxed if it is subject to a substantial risk of forfeiture or to a restriction on transferability. However, restrictions arising from securities laws or certain accounting rules are not considered sufficient to prevent inclusion in income.

Ways and Means bill

The bill will permit a taxpayer who receives stock subject to Federal securities law restrictions or the "pooling-of-interests" accounting rules to include the value of the stock in income when these restrictions terminate.

Conable-Hance substitute

Same as Ways and Means bill, but with prospective application only.

Udall substitute

No provision.

Comparative Revenue Effects

[Billions of dollars]

	Fiscal year—					
	1981	1982	1983	1984	1985	1986
Ways and Means Committee bill without 1984 cuts ² -----	-1.5	-37.8	-98.4	-128.9	-159.5	-193.9
Ways and Means Committee bill with 1984 cuts ² -----	-1.5	-37.8	-98.4	-148.6	-190.3	-229.5
Conable-Hance substitute ³ -----	-1.7	-36.3	-95.2	-152.9	¹ -200.5	¹ -267.8
Udall substitute-----	-1.2	-12.7	-50.0	-66.4	-81.5	-98.9

¹ The revenue estimates for fiscal years 1985 and 1986 are extremely sensitive to the assumed rates of inflation, owing to the indexing provision. The staff estimates are based on inflation rates which lead to an indexing adjustment of 8.5 percent for 1985 and 7.9 percent for 1986.

² The Ways and Means Committee bill includes additional tax cuts in 1984 if certain economic and fiscal conditions are met in 1983.

³ The Treasury Department estimates the revenue loss of the Conable-Hance substitute to be: \$2.0 billion in FY 1981, \$35.8 billion in FY 1982, \$97.2 billion in FY 1983, \$152.9 billion in FY 1984, \$193.9 billion in FY 1985 and \$251.0 billion in FY 1986. These estimates

were prepared before the cap was removed from the charitable contributions provision. Staff estimates of this provision, as introduced, are \$1.3 billion higher in FY 1985 and \$3.6 billion higher in FY 1986 than those of the Treasury Department. Additionally, due to the difference in inflation assumptions, staff estimates of the revenue loss associated with indexation of the individual income tax are \$4.3 billion higher in FY 1985 and \$13.1 billion higher in FY 1986 than those of the Treasury Department.

NOTE: These numbers are preliminary estimates.

