Possible Amendments to H.R. 6056
(Technical Corrections Act of 1982)
to be considered during markup
by the
Committee on Ways and Means
on
May 11, 1982

Prepared by the Staff
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MINOR NONCONTROVERSIAL
CHANGES

The following is a list of minor, noncontroversial changes to the bill.

1. Clarify that the normalization provisions relating to the ESOP tax credits apply only to compensation paid which is subject to ratemaking.

2. Provide that the amendment in the bill (sec. 102(ℓ)(3)) allowing targeted jobs credit certifications to be made on the date employment starts will be effective for employees beginning work after May 11, 1982.

3. Clarify that the amendment in the bill relating to credit union share accounts applies only for purposes of computing the all-savers' limit applicable to credit unions (code sec. 128(d)(4)).

4. Provide that a taxpayer, who had an identified straddle consisting of all regulated futures contracts and takes delivery of a commodity on one or more positions of the straddle, shall treat all the contracts as terminated, so that the taxpayer may then elect to treat the straddle as a mixed straddle.

5. Allow special valuation property (Code sec. 2032A) purchased from an estate by a family member to be treated as meeting the long-term holding period requirement if the property is sold to another family member within a year of the decedent's death.

6. Clarify that certain pension plan limits may provide for deductible contributions (Code sec. 401(d)(5)).

7. Clarify that the 5-year amortization for low-income housing (under Code sec. 167(k)) remains a tax preference as under prior law.

8. Correct certain 50-cent rounding errors in the tax schedules for married filing separate returns, estates and trusts.

9. Clarify that the negligence penalty added by ERTA cannot apply to the period after the tax is paid.

10. Clarify language that the new research credit is incremental.

11. Add conforming changes to Code sections 584 and 702 regarding the net interest exclusion.

12. Delete a redundant reference in section 55 to section 44G.

13. Add a cross reference in section 671 to the new qualified subchapter S trusts.

14. Clarify that the penalty for overstated deposits does not apply where payment is made by the due date.

15. Correct typographical errors in Code sections 47, 402 and Act section 321.

16. Correct a cross reference in Code section 443 and delete an extraneous reference to stock in Code section 368(a)(2)(c), added by the Bankruptcy Tax Act.

17. Redesignate one of the two section 194's added to the Code.

18. Correct an erroneous reference in the effective date provision of Code section 404A.

19. Provide that royalty interests that produce qualified royalty production are not to be taken into account in determining whether a qualified family farm corporation satisfies the requirement that 80 percent of its assets be used in farming.

AMENDMENT #1
(Mr. Pickle, Mr. Jones, Mr. Archer)

Incentive Stock Option "Pyramiding"

ERTA added provisions to allow all income with respect to certain employee stock options ("incentive stock options") to be taxed at capital gains rates when the stock received on the exercise of the option is sold. The Act allows employees to pay for new incentive option stock with stock of their employer corporation.

H.R. 6056 provides that if stock which was acquired through the exercise of a statutory option is used to acquire new incentive stock, before the stock has met the minimum holding period requirements to obtain capital gain treatments (in the case of incentive stock, two years from the grant of the option and one year from the exercise of the option), income will be recognized with respect to the stock disposed of. Where the holding period was met, no income would be recognized.

Proposed amendment

The proposal would make the amendment apply only to exchanges after March 15, 1982.

AMENDMENT # 2
(Mr. Stark)

Stock Options -- Pre-ERTA Modifications

ERTA added provisions to allow all income with respect to certain employee stock options ("incentive stock options") to be taxed at capital gains rates when the stock received on the exercise of the option is sold. Under the stock option provisions, the modification of an existing option is treated as the grant of a new option, requiring the option price to be set at the then fair market value. Treasury regulations provide that, for purposes of this rule, modifications made before August 13, 1981, are ignored if the modification is rescinded.

Proposed amendment

The amendment would make the option modification rule inapplicable to modifications to incentive stock options (which are not also qualified stock options) made prior to August 13, 1981.

AMENDMENT #3
(Mr. Stark)

Bank Forward Contracts

ERTA requires that regulated futures contracts be "marked to market," i.e., gains or losses reflected in contracts held at the end of the taxable year are included in determining the taxpayer's taxable income for that year. Gains and losses are treated as 60 percent long-term and 40 percent short-term, resulting in a maximum tax rate of tax of 32 percent. The provision only applies to contracts which are traded on a system of marking to market.

Proposed amendment

The proposed amendment would extend the rules adopted by ERTA for regulated futures contracts to foreign currency contracts (i.e. bank forward contracts) entered into after May 11, 1982, where similar regulated future contracts are traded. The valuation of such contracts would be determined in accordance with regulations prescribed by the Treasury Department.

AMENDMENT # 4
(Mr. Jacobs)

Capital Gains

ERTA provided that the maximum long-term capital gains rate for individuals on sales or exchanges after June 9, 1981, is 20 percent.

Proposed amendment

The amendment would apply the 20-percent rate to sales and exchanges on or after June 9, 1981.

AMENDMENT # 5
(Mr. Gephardt)

Rehabilitation Credit for Theme Park Structures

ERTA provided a 15-percent investment tax credit for the rehabilitation of nonresidential buildings at least 30 years old, a 20-percent credit for nonresidential buildings at least 40 years old, and a 25-percent credit for certified historic buildings.

The credit only is allowed for buildings which are 15-year recovery property under the new cost recovery provisions.

Under ERTA, theme-park structures have a 10-year recovery period, and therefore are not eligible for the credit.

Proposed amendment

The amendment would provide that a building which previously was treated as 15-year recovery property (or would have been so treated if ACRS had been in effect) could not be reclassified as 10-year property. Therefore, such a building could be eligible for the rehabilitation credit.

AMENDMENT #6
(Mr. Shannon)

Credit for Increasing Research Expenditures

ERTA added a 25-percent income tax credit based on the amount by which a taxpayer's qualified research expenditures for the taxable year exceed the average qualified research expenditures, in a base period (generally, the preceding three taxable years). Qualified research expenses include "in-house research expenses" and "contract research expenses." In-house research expenses means amounts paid or incurred for certain research wages, research supplies, or the right to use personal property in research.

H.R. 6056 would provide that in-house research expenses do not include payments for the right to use personal property in research paid or incurred after March 31, 1982, other than payments for the use of computer time by a person who is not the principal user of the computer.

Proposed amendment

The proposed amendment would retain the provisions of ERTA (allowing lease payments for the use of all personal property in research to be eligible as qualified research expenditures) except that no credit would be allowed to the extent the taxpayer was both the lessor and lessee of substantially identical property.

AMENDMENT #7
(Mr. Hance)

Depletion on Secondary and Tertiary Production after 1983

Section 613A(c)(6) provides for percentage depletion on up to 1,000 barrels a day or secondary or tertiary oil and gas production by an independent producer at the rate of 22 percent. This provision does not apply after 1983.

The general rule for percentage depletion by independent producers (section 613A(c)(3)) is coordinated with the special rule for secondary and tertiary production by reducing the depletable oil amount by any secondary or tertiary production.

Thus, there is no provision permitting percentage depletion on secondary and tertiary production after 1983. In addition, the depletable oil quantity of a producer who has both primary and secondary or tertiary production will be reduced by the secondary or tertiary production even though percentage depletion is not available on that production.

Proposed amendment

The amendment would eliminate any distinction between primary and secondary or tertiary production after 1983. Thus, independent producers could claim percentage depletion in 1984 at a rate of 15 percent on up to 1,000 barrels of all their production.

AMENDMENT # 8
(Mr. Matsui)

Effective Date of Net Profits Interest Amendment

Under present law, the right to depletion on oil produced under a net profits interest agreement and, therefore, the liability for windfall profit tax on that oil is determined by allocating cost recovery oil under the agreement to the working interest owner. Section 201(h) of H.R. 6056 would allocate cost recovery oil for windfall profit tax purposes in the same proportion as the net profits are shared under the agreement. This rule applies to net profits interest agreements entered into after March 31, 1982.

Proposed amendment

The proposal would amend the effective date of section 201(h) of the bill to make it apply to agreements entered into prior to April 1, 1982, if (1) the owner of the net profits'interest holds at least a 90 percent net profits interest, and (2) the holder is otherwise exempt from the windfall profits tax on crude oil.

AMENDMENT # 9
(Mr. Anthony)

Motor Carrier Operating Authorities

ERTA allowed taxpayers holding motor carrier operating authorities on July 1, 1980, to deduct the basis of the authorities over a 60-month period. ERTA also allowed corporations which held an authority on that date and whose stock which had been purchased (in a transaction meeting certain requirements) by a second corporation prior to that date, to adjust its basis in the operating authority by the portion of the purchase price of the stock attributable to the authority.

Proposed amendment

The amendment would allow an adjustment to the basis of a motor carrier operating authority held by a corporation whose stock had been purchased by individuals prior to July 1, 1980 (under requirements similar to those applying to corporate purchases).

AMENDMENT #10
(Mr. Conable)

At-Risk--Subchapter S and Partnerships

In the case of individuals, subchapter S corporations, and certain closely held corporations, ERTA denied the investment tax credit to the extent a taxpayer is not at risk. In the case of a subchapter S corporation or partnership, the shareholders or partners must be at risk in order to be eligible for their allowable share of the credit. A special exception applies to certain nonrecourse loans from certain third party lenders to subchapter S corporations and partnerships.

Proposed amendment

The amendment would provide that to the extent a subchapter S corporation or partnership is at risk, for purposes of the investment tax credit, the shareholders or partners will be treated at risk in order to be eligible for their allowable share of the credit.

Proposed alternative amendment

The proposed alternative amendment would make the investment tax credit "at risk" rules inapplicable to normal commercial transactions of nontax shelter businesses. Nontax shelter businesses would be businesses that have a certain number of employees, a certain level of business activity, and a certain level of receipts from active business operations. This exception is modeled on the exception for closely-held leasing corporations under section 465.

AMENDMENT #11
(Mr. Archer)

Foreign Refiner Exclusions

Under present law, retailers and refiners are, in general, excluded from independent producer status. A retailer is, generally, a person who sells oil, natural gas, or any product derived therefrom, through any retail outlet operated by the taxpayer or a related person. The retailer exception does not apply, however, if the combined gross receipts from the sale of oil, natural gas, or any product derived therefrom do not exceed $5,000,000. In determining whether the $5,000,000 threshold has been crossed, such sales do not include sales made outside the United States if no domestic production of the taxpayer or a related person is exported during the year or the preceding taxable year.

A refiner is any person who refines 50,000 barrels or more of crude oil a day. Currently, refinery runs of related foreign refineries are taken into account in determining this 50,000 barrel amount.

Proposed Amendment

The proposal would allow United States refiners to exclude refinery runs of related foreign refineries in determining whether or not the United States producer or refiner was entitled to independent producer status.

This rule will only apply if (1) there were no exports of United States oil by the United States producer and (2) no refinery products (in excess of a de minimis amount of $5,000,000), were imported into the United States by the U.S. producer or refiner.

AMENDMENT #12
(Mr. Moore)

Royalty Owners Exemption

Under present law, up to two barrels of oil per day attributable to the economic interest of a royalty owner is exempt from the windfall profit tax. This exemption will be increased to 3 barrels per day starting in 1985 and thereafter. Prior to 1982, the royalty owner exemption was fixed in terms of a dollar credit, up to $1,000 for 1980 and up to $2,500 for 1981.

Proposed amendment

The proposal would amend the royalty owner credit to provide a dollar credit, in lieu of the exemption, equal to the value which an average royalty owner would derive from the 2-3 barrel exemption.

OTHER ISSUES
A.

Condensate

The windfall profit tax was designed to tax price increases resulting from OPEC price increases and decontrol. To accomplish this, the tax is imposed on all production which is other than exempt oil. The term "crude oil" is defined in the Internal Revenue Code with reference to the definition of that term in the June 1979 regulation of the Department of Energy. The June 1979 energy regulations, in turn, define oil as including, "condensate recovered in associated or nonassociated production by mechanical separators, whether located on the lease, at central field facilities, or at the inlet side of a gas processing plant."

Proposed admendment

The amendment would treat as "removed" and, therefore, taxable, all oil actually recovered (by mechanical separation), at or before the inlet side of the gas processing plan. Such crude oil would be "removed" when actually recovered, even if recovery actually occurred after the gas left the lease. Thus, the time at which condensate becomes taxable would be clarified.

Second, the definition of the term "domestic" would be amended to remove a reference to "oil" thus clarifying the taxability of oil received in association with gas production.

Safe Harbor Leasing for ITC Strips

The safe harbor leasing provisions under ERTA guarantee lease treatment for transactions that are intended only to transfer the tax benefits of ownership from the user of the property (seller/lessee) to a person with a sufficient tax base to fully utilize those benefits (buyer/lessor). By virtue of the transaction, the buyer/lessor is treated as the owner of the property for Federal tax purposes and is entitled to claim the depreciation deductions and investment tax credits allowed to owners of property.

In a colloquy between Senators Dole and Danforth (127 Cong. Rec. S. 8644 (daily ed. July 28, 1981)) that occurred at the time the full Senate considered the safe harbor leasing provisions as part of the Economic Recovery Tax Act of 1981, Senator Dole stated that the safe harbor provisions would permit so-called ITC strips or credit pass-through leases. The purpose of these credit pass-through leases is to permit the state law owner of the property to sell the investment tax credit and retain the depreciation deductions normally allowed owners of property. In a credit pass-through lease, the owner leases the property to a lessee who then subleases the property back for the same term to the owner or an affiliate. Pursuant to a section 48(d) election, the owner passes through the investment credit to the lessee/sublessor, who is treated as the lessee for Federal tax purposes.

Proposed amendment

The amendment would clarify that the safe harbor leasing provisions apply to "ITC strips" (i.e., credit pass through leases) entered into before October 20, 1981.

Powerhouse Fuel

Generally, oil that is used to power production equipment for the property from which it is produced is not subject to depletion or the windfall profit tax. This result is non-statutory. The conference report on the windfall profit tax adopted an expansive definition of use on the same property. In the conference report, there is a reference to a hypothetical case in which contiguous properties that are not even divided by a public road are treated as one property for purposes of the powerhouse exception.

Proposed colloquies

(1) Mr. Jones would clarify that the presence or absence of a road on the surface would not affect the treatment of otherwise contiguous mineral estates.

(2) Mr. Archer would clarify that the premises on which oil is both produced and used for powerhouse fuel need not be directly above the mineral deposit.