

Joint Committee on Taxation  
June 8, 1984  
JCX-16-84

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Tentative Recommendations on Life Insurance

II. Life Insurance

A. Taxation of life insurance companies

133. Definition of life insurance companies.  
(p. 178)

(a) Deficiency reserves.

House recesses.

(b) Elec. to treat noncancellable A&H as cancellable.

House recesses, with amendment that the election must be made on the return filed for the first taxable year beginning after 1983.

134. General deductions.  
(p. 178)

(a) In general.

House and Senate the same.

(b) Dividends received from subsidiaries.

Open question.

135. Special deductions.  
(p. 180)

(a) Special life insurance company deduction.

Open question.

(b) Small life insurance company deduction.

Open question.

(c) Computation of tentative LICTI.

House recesses, with grandfather for certain current investments in minerals to be treated as insurance business.

(d) Tentative LICTI for a controlled group.

House recesses.

(e) Adjustments in

House recesses.

tentative LICTI.

(f) Alternative life insurance company deduction.

Open question.

136. Policy reserves.  
(p. 182)

(a) In general.

House and Senate the same.

(b) Net level reserves for noncancellable A&H.

Senate recedes.

(c) Term life and annuity benefits.

House recedes.

(d) States which determine annuity reserves without reduction for surrender charges.

Open question.

137. Special rules for variable contracts.  
(p. 184)

(a) In general.

Open question.

(b) Investment diversification.

Open question.

138. (a) Limitation on deduction for policyholder dividends paid by mutual companies.  
(p. 184)

House and Senate the same, with technical amendments to clarify the computation of equity and assets.

(b) Transition rule for high surplus mutuals.

Open question.

(c) Special rule for tax reserve equity adjustment for excess interest life contracts.

Open question.

(d) Reduction of equity for mutual successor of fraternal benefit society.

House recedes, with possible amendment.

139. Allocation authority over reinsurance agreements. (p. 186) House recedes, but (as part of compromise on item 141(b)(3)), with an amendment to extend authority to reinsurance transactions between unrelated companies generally.
140. Definition of policyholders' share and company's share. (p. 186) House recedes.
141. Effective dates and transition rules. (p. 186)
- (a) General effective date. House and Senate the same.
- (b)(1) Recomputation of reserves. House recedes.
- (b)(2) Fresh start for P&C's. Open question.
- (b)(3) Reinsurance transactions after 9/27/83. Senate recedes with the following modification: Adopt House anti-manipulation provision (without termination provisions), plus Senate provisions' denial of nonpar and group life and A&H deduction on contracts subject to reinsurance after 9/27/83. House recedes on sub-items (3)(ii), (3)(iii), and (3)(iv).
- (b)(4) Allocation of the fresh start benefit. House recedes.
- (b)(5) Election not to recompute reserves. House recedes, with amendment to substitute \$100 million for \$500 million asset limit.

(c)(1) Determination of tentative LICTI for companies of acquisitions in 1980, 1981, 1982, and 1983.

House recesses, with the addition of Arkansas and a technical amendment to clarify taxpayers affected; and an amendment for similar treatment for certain losses on pension business of certain companies.

(c)(2) Treatment of hybrid stock/mutual companies.

Open question.

(c)(3) Special rule to treat ownership of stock.

House recesses to Senate provision as corrected.

(c)(4) Forgiveness of Phase III tax.

Senate recesses.

142. Underpayments of estimated tax for 1984. (p. 190)

House recesses.

#### B. Taxation of life insurance products

143. Definition of life insurance. (p. 192)

(a) In general.

House recesses.

(b) Consequences of failure.

Senate recesses.

(c) Effective date and transition rules.

House recesses with the following amendment: The new definition to be effective for all contracts issued after 12/31/84, except for

increasing death benefit policies having a premium funding more rapid than 10-year level premiums, unless the policy meets one of the three transition rules in the House bill. Present law (with section 101(f) extended applies to all contracts sold before 7/1/84.

Grandfather for existing plans of insurance with a transition rule to allow contracts that credit excess interest monthly to be modified to credit it annually.

A transition rule for contracts issued before 10/1/84, if the initial cash value did not exceed the net single premium computed at 3 percent and 58 C.S.O. mortality.

144. Annuity contracts.  
(p. 194)

(a) In general.

House and Senate the same.

(b) Treatment of annuity contract at death.

House recedes with amendment to adopt a substitute for the Senate provision conforming to IRA and pension rules for distribution at death.

145. Policyholder loans.  
(p. 194)

Open question.

146. Group-term insurance.  
(p. 196)

House recedes with the modification that the grandfather in the Senate amendment applies only

with respect to employees employed under the grandfathered plan on 1/1/84; existing plans have to conform the nondiscrimination rules by 1/1/87.

147. Treatment of certain exchanges of insurance policies. (p. 196)

House recesses.

148. Studies. (p. 196)

Senate recesses with modification that the consultation on studies be with the House Ways and Means and Senate Finance Committees.

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TENTATIVE RECOMMENDATIONS -- CONFERENCE ISSUES

I. TAX FREEZE; TAX REFORMS GENERALLY

H. Pension and Welfare Benefit Plan Provisions

62. Deduction limits for qualified pension plans. (p. 86)
- |   |                     |
|---|---------------------|
| (a) 25-percent deduction limit.                   | (a) Senate recedes. |
| (b) Overall deduction limit.                      | (b) Senate recedes. |
| (c) Combined limit on contributions and benefits. | (c) Senate recedes. |
63. Provisions relating to top-heavy pension plans. (p. 86)
- |                                    |  |
|------------------------------------|--|
| (a) Super top-heavy plans.         | (a) Senate recedes.  |
| (b) Definition of key employee     | (b) House recedes with amendment to exclude officers who earn less than 1.5 times the limit on contributions to a defined contribution plan (\$45,000 for 1984). |
| (c) Separated employees.           | (c) House recedes.   |
| (d) Salary reduction arrangements. | (d) House recedes.   |
| (e) Governmental plans.            | (e) House recedes.   |
| (f) Simplified amendments.         | (f) House recedes.   |
- Effective dates - House recedes.
64. Distribution rules for qualified pension plans.

(p. 90)

(a) Pre 59 1/2 distributions.

(a) House recesses.

(b) Before death distributions.

(b) House recesses.

(c) After death distributions.

(c) House recesses with amendments to clarify that (1) surviving spouse is not subject to the benefit commencement rule and (2) the immediate annuity requirement can be satisfied with distributions directly from an IRA or qualified plan provided the distributions meet the usual requirements.

(d) Qualifying rollover distributions.

(d) House recesses.

Effective dates - House recesses.

65. Pension plans with substantially all benefits derived from employee contributions. (p. 92)

House recesses with amendment to define "substantially all" to mean 85 percent of benefits.

66. Repeal of estate tax exclusion for qualified pension plan benefits. (p. 92)

House recesses with amendment to provide that the present law rule excluding from the gross estate a community property interest in pension benefits is retained.

70. Medical benefits provided by pension plans. (p. 104)

Senate recesses.

#### I. Foreign Provisions

73. Original issue discount in the case of foreign investors. (p. 110)

House recesses with modification that denies deduction to U.S. borrower that accrues interest on original issue discount

debt to related foreign lender until the related lender includes (or would include) the interest in income.

79. Definition of resident alien. (p. 116)

Senate recedes with language (i) clarifying that days in transit without clearing customs are not days present in the U.S., and (ii) with a modification that will tax aliens resident for three consecutive years or more who cease residence for up to two years on U.S. source income and sales of U.S. assets (the same taxation as U.S. citizens who renounce citizenship for tax purposes).

M. Miscellaneous Reform Provisions

124. Section 267. (p. 164)

(a) Same.

(b) House recedes on low-income housing and adds a general rule to prevent partnership-partner status from arising out of the partner owning a de minimis amount of corporate stock.

(c) House recedes but adds an exception for sales of inventory to foreign affiliates in the ordinary course of business of both the seller and the purchaser.

Effective date.--House recedes on Senate partnership provision. Senate recedes on House foreign corporation rule.

127. Capital gains on coal royalties from related parties. (p. 168)

House recedes.

Effective date.--Same.

X. MISCELLANEOUS REVENUE PROVISIONS

E. Employee Benefits

222. Extension of time for                    House recedes.  
repayment of quali-  
fied refunding loans.  
(p. 316)

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TENTATIVE RECOMMENDATIONS -- CONFERENCE ISSUES

I. TAX FREEZE; TAX REFORMS GENERALLY

F. Accounting Changes

46. Premature accruals.  
(p. 66)

(a) General rule.

(a) Same.

(b) Employee benefits:

(b) Consideration of this item is deferred until other employee benefit issues are resolved.

(c) Exceptions:

(i) Clarify economic performance test for certain recurring items. Item treated as incurred in a taxable year if--

(1) all events test is met;

(2) economic performance occurs within a reasonable period but limited to 8-1/2 months after end of year;

(3) item is recurring and tax treatment is consistent; and

(4) either (a) item is not a material item, or (b) accrual in year results in better matching against income.

(ii) Contested liabilities. House recedes to Senate amendment that requires economic performance before deduction for payment to sec. 461(f) trust. Clarify that payment to a sec. 461(f)

trust is not a payment to a person for purposes of the economic performance test.

(iv) Nuclear waste disposal. Clarify that amounts required to be paid to the Federal Government's Nuclear Waste Fund are deductible when paid.

(d) NOL carrybacks:

(d) Same.

Effective date.--Same, but allow taxpayers to elect House provision (cut-off method) or Senate (481 change of accounting method rules) with a 3-year spread.

47. Nuclear power plant decommissioning  
(p. 68)

House recedes.

48. Mine reclamation and similar costs  
(p. 68)

(a) General.

(a) House recedes.

(b) Site reclamation costs

(b) House recedes with 2 amendments:

1. Taxpayers will not be required to discount (by 2 percent per year) deductions for the current cost of future reclamation expense.

2. Taxpayers will not be required to recapture amounts deducted for reclamation, but not spent, on a parcel by parcel basis.

(c) Site closing costs

(c) House recedes with an amendment eliminating the

requirement to discount (by 2 percent per year) deductions for the current cost of future site closing expense.

(d) Sinking funds

(d) House recedes with 2 amendments:

1. Amounts deducted for site reclamation and site closing costs are deemed to earn interest at 110 percent of the current applicable short-term Federal rate.

2. The sinking fund balance is limited to the current cost of: (i) reclaiming disturbed, unreclaimed land (in the case of reclamation costs), (ii) closing the mined portion of the site on a units of production basis (in the case of mine closing costs), and (iii) closing the utilized portion of the site on a units of capacity basis (in the case of waste disposal site closing costs). Any amount in excess of this limit at the end of each tax year is recaptured.

(e) Transition rules.

(e) House recedes.

Effective date.--Same.

51. Deferred payment transactions  
(p. 74)

(a) Time for inclusion or deletion of deferred interest.

House recedes with an amendment exempting loans of \$10,000 or less between natural persons and provides that, for deferred payment transactions entered into

after the date of conference action and before January 1, 1985, interest may be deducted only as it economically accrues.

Effective date--Same.

(b) Measurement of interest and principal

House recedes.

Effective date--House recedes.

52. Deferred payments for use of property or services (p. 76)

House recedes with an amendment requiring both lessor and lessee to account for rent on the accrual method based on the amount allocable to each year under the terms of the lease. When no annual rent is stated in the lease, level rents will be assumed. In addition, in the case of sale-leasebacks and long-term leases where the rent is stepped for tax avoidance purposes, both the lessor and lessee must account for rent on a level amount basis. Rents which increase pursuant to the following terms would not be tax motivated--

- (1) percentage rents
- (2) increases in CPI
- (3) reasonable rent holidays
- (4) increases in amounts paid to third parties
- (5) rents which fluctuate by less than 10% above or below the average rent.

Finally, in the case of the sale of property subject to a long-term lease or a sale leaseback, any gain on the sale would be treated as ordinary income to the extent of

the excess of the remaining rents under the lease over what would be level rents.

Effective date.--Leases entered into after the date of conference action except for--

- (1) leases entered into pursuant to binding agreements on that date and
- (2) leases covered under the transitional rules of the Senate bill

53. Capitalization of construction period interest and taxes (p. 78)

House recedes.

Effective date.--Same.

