[JOINT COMMITTEE PRINT]

COMPARISON OF TAX REFORM PROVISIONS OF H.R. 3838 AS PASSED BY THE HOUSE AND THE SENATE

Prepared for Use by the House-Senate Conferees
by the
Staff of the Joint Committee on Taxation

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(A separate document indicates the *differing* provisions in the House bill and the Senate amendment.)

INTRODUCTION

This document [1] provides a comparative description of tax reform provisions in connection with the House-Senate conference on H.R 3838 (Tax Reform Act) as passed by the House and Senate

H R 3838 was passed by the House on December 17, 1985, and by the Senate as amended on June 24, 1986.

The document, in columnar form for each item, includes Present law (Col 2); the President's tax reform proposal [2] (Col. 3); the House-passed tax reform bill [3] (Col 4); and the Senate amendment to H R. 3838 [4] (Col. 5).

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[1] This document may be cited as follows Joint Committee on Taxation, *Comparison of Tax Reform Provisions of H R. 3838 as passed by the House and Senate* (JCS-15-86), July 15, 1986

[2] The White House, *The President's Tax Proposals to the Congress for Fairness, Growth, and Simplification*, May 1985

[3] See also report of the House Committee on Ways and Means, H Rept 99-426, December 7, 1985

[4] See also report of the Senate Committee on Finance, S Rept 99-313, May 29, 1986

Item	Present Law	President's Proposal	House Bill	Senate Amendment
A. Basic Rate Structure (secs. 101-103 and 131 of the House bill and secs. 101-104, 131, and 151 of the Senate amendment)				
1. Tax rate schedules				
a. Rates, brackets	(a) The present rate structure consists of up to 15 taxable income brackets and tax rates beginning above the zero bracket amount (ZBA). The following amounts apply for 1986 and reflect an adjustment for 1985 inflation.	(a) The tax structure would consist of three taxable income brackets and tax rates—15, 25, and 35 percent—above the ZBA.	(a) The tax structure consists of four brackets and tax rates—15, 25, 35, and 38 percent—beginning at zero taxable income, with a standard deduction replacing the ZBA.	(a) The tax structure consists of two brackets and tax rates—15 and 27 percent—beginning at zero taxable income, with a standard deduction replacing the ZBA.
	Married individuals filing jointly and surviving spouses	***Married individuals filing jointly and surviving spouses***	***Married individuals filing jointly and surviving spouses***	***Married individuals filing jointly and surviving spouses***
	14 taxable income brackets above the ZBA of $3,670, 11-percent tax rate starts at taxable income above $3,670, maximum 50-percent rate starts at taxable income above $175,250.	*Tax rate* — *Brackets* ZBA — $0 to 4,000 15% — $4,000 to 29,000 25% — $29,000 to 70,000 35% — Over $70,000	*Tax rate* — *Brackets* ZBA — Replaced by standard deduction 15% — $0 to $22,500 25% — $22,500 to $43,000 35% — $43,000 to $100,000 38% — Over $100,000	*Tax rate* — *Brackets* ZBA — Replaced by standard deduction 15% — 0 to $29,300 27% — Over $29,300
	(For married individuals filing separate returns, the ZBA is one-half the ZBA on joint returns, and the taxable income bracket amounts begin at one-half the amounts for joint returns.)	(For married individuals filing separate returns, the ZBA would be one-half the ZBA on joint returns, and the taxable income bracket amounts would begin at one-half the amounts for joint returns.)	(For married individuals filing separate returns, the taxable income bracket amounts begin at one-half the amounts for joint returns.)	(For married individuals filing separate returns, the 27-percent bracket begins at 14,650, i.e., one-half the taxable income amount for joint returns.)
	Heads of household	***Heads of household***	***Heads of household***	***Heads of household***
	14 taxable income brackets above the $2,480 ZBA; 11-percent tax rate starts at taxable income above $2,480, maximum 50 percent rate starts at taxable income above $116,870.	*Tax rate* — *Brackets* ZBA — $0 to 3,600 15% — $3,600 to 23,000 25% — $23,000 to 52,000 35% — Over $52,000	*Tax rate* — *Brackets* ZBA — Replaced by standard deduction 15% — $0 to $16,000 25% — $16,000 to $34,000 35% — $34,000 to $75,000 38% — Over $75,000	*Tax rate* — *Brackets* ZBA — Replaced by standard deduction 15% — 0 to $23,500 27% — Over $23,500
	Single individuals	***Single individuals***	***Single individuals***	***Single individuals***
	15 taxable income brackets above the $2,480 ZBA, 11-percent tax rate starts at taxable income above $2,480, maximum 50-percent rate starts at taxable income above $88,270.	*Tax rate* — *Brackets* ZBA — $0 to 2,900 15% — $2,900 to 18,000 25% — $18,000 to 42,000 35% — Over $42,000	*Tax rate* — *Brackets* ZBA — Replaced by standard deduction 15% — $0 to $12,500 25% — $12,500 to $30,000 35% — $30,000 to $60,000 38% — Over $60,000	*Tax rate* — *Brackets* ZBA — Replaced by standard deduction 15% — 0 to $17,600 27% — Over $17,600

Item	Present Law	President's Proposal	House Bill	Senate Amendment
1. Tax rate schedules (Cont.)				
b. Rate adjustment	(*b*) No provision	(*b*) No provision.	(*b*) No provision.	(*b*) The benefit of the 15-percent bracket is phased out for taxpayers above certain income levels, through a rate adjustment imposing additional tax liability equal to five percent of the income within a specified phase-out range. The rate adjustment applies over the following ranges of adjusted gross income (AGI) levels: *Filing status* — *AGI phase-out level* Joint returns or surviving spouses .... $75,000-$145,320 Heads of household ...... $55,000-$111,400 Single individuals ...... $45,000-$87,240 Married individuals filing separately .... $37,500-$72,660 The phase-out levels will be adjusted for inflation beginning in 1988. If resulting in less additional tax liability, the five-percent rate adjustment is computed with respect to the taxpayer's taxable income in the 27-percent bracket (For example, for joint returns with AGI exceeding $75,000, the rate adjustment applies over a taxable income range of $29,300 to $99,620, if that computation produces a lower additional tax liability than the computation based on AGI.) *Resolution.*—It is the sense of the Senate that the Senate conferees give the highest priority to the tax cut for all middle-income Americans (floor amendment by Senator Riegle, adopted by a vote of 94-1).
c. Effective date		(c) The changed tax rates and taxable income brackets would become effective on July 1, 1986. For 1986 returns, tax rate schedules would blend equally the present-law schedules (i.e., 1985 schedules as adjusted for inflation) with the new schedules.	(c) The changed tax rates and taxable income brackets become fully effective in 1987. For 1986 returns, tax rate schedules will blend equally the present-law schedules (i.e., 1985 schedules as adjusted for inflation) with the new schedules.	(*c*) The changed tax rates and taxable income brackets become fully effective in 1988. For 1987 returns, tax rate schedules will blend equally the present-law schedules (i.e., 1986 schedules as adjusted for inflation) with the new schedules.

Item	Present Law	President's Proposal	House Bill	Senate Amendment
2. Standard deduction (zero bracket amount)				
a. Increased standard deduction for all individuals	(*a*) The following zero bracket amounts apply for 1986 and reflect an adjustment for 1985 inflation. *Filing status* — *ZBA* Joint returns and surviving spouses — $3,670 Heads of household — 2,480 Single individuals — 2,480 Married individuals filing separately — 1,835 The ZBA is indexed annually for changes in the inflation rate.	(*a*) The following increased zero bracket amounts would apply for 1986. *Filing status* — *ZBA* Joint returns and surviving spouses — $4,000 Heads of household — 3,600 Single individuals — 2,900 Married individuals filing separately — 2,000 Indexing of the ZBA would be continued, as in present law, after 1986.	(*a*) Instead of the ZBA, individuals are allowed a standard deduction. In 1987, the standard deduction is increased to the following amounts: *Filing status* — *Standard deduction* Joint returns and surviving spouses — $4,800 Heads of household — $4,200 Single individuals — $2,950 Married individuals filing separately — $2,400 These increased standard deduction amounts are effective on January 1, 1987, and are indexed for inflation beginning in 1988. For 1986, the standard deduction is the same amount as the ZBA for 1986 under present law (i.e., the 1985 ZBA as adjusted for inflation in 1985).	(*a*) Instead of the ZBA, individuals are allowed a standard deduction. In 1988, the standard deduction is increased to the following amounts *Filing status* — *Standard deduction* Joint returns and surviving spouses — $5,000 Heads of household — $4,400 Single individuals — $3,000 Married individuals filing separately — $2,500 These increased standard deduction amounts are effective on January 1, 1988, and will be indexed for inflation beginning in 1989. For 1987, the standard deduction is the same amount as the ZBA that would have applied for 1987 under present law (i.e., the 1986 ZBA as adjusted for inflation in 1986).
b. Additional standard deduction amount for elderly or blind individuals	(*b*) No provision	(*b*) No provision.	(*b*) An additional standard deduction amount of $600 (indexed for inflation beginning in 1988) is allowed for an elderly or blind individual; $1,200 for a blind and elderly individual. For these taxpayers only, the new standard deduction amounts listed in (a) above (otherwise effective in 1987) and the additional $600 standard deduction amount are effective on January 1, 1986.	(*b*) An additional standard deduction amount of $600 (indexed for inflation beginning in 1989) is allowed for an elderly or blind individual; $1,200 for a blind and elderly individual. For these taxpayers only, the new standard deduction amounts listed in (a) above (otherwise effective in 1988) and the additional $600 standard deduction amount are effective on January 1, 1987
c. Floor under itemized deductions	(*c*) No provision	(*c*) No provision.	(*c*) Individuals who itemize their deductions must reduce their total itemized deductions by $500 times the number of personal exemptions claimed. The $500 floor will be adjusted for inflation beginning in 1987.	(*c*) No provision

Item	Present Law	President's Proposal	House Bill	Senate Amendment
3. Personal exemption				
a. Exemption amount	(*a*) The personal exemption amount for an individual, the individual's spouse, and each dependent is $1,080 for 1986 (reflecting an inflation adjustment for 1985). One additional personal exemption is provided for an individual who is age 65 or older, and for an individual who is blind	(*a*) The personal exemption amount for an individual, an individual's spouse, and each dependent would be increased to $2,000 for 1986; beginning in 1987, the $2,000 amount would be adjusted for inflation. The additional exemption for elderly or blind individuals would be repealed starting in 1986.	(*a*) Same as President's proposal. (As described above, an additional standard deduction amount is allowed for an elderly or blind individual.)	(*a*) The personal exemption amount is increased to $1,900 for 1987 and $2,000 for 1988; beginning in 1989, the $2,000 amount will be adjusted for inflation The additional exemption for elderly or blind individuals is repealed starting in 1987. (As described above, an additional standard deduction amount is allowed for an elderly or blind individual) *Phase-out*—All personal exemption amounts claimed by a taxpayer are reduced, at a five-percent rate, over a range of $40,000 (adjusted for inflation) starting at the AGI level at which the benefit of the 15-percent rate is totally phased out (see "Rate adjustment" under I.A.1, above). Thus, no personal exemption amounts are allowed for taxpayers with AGI exceeding the top of the exemption phase-out range (e g., for joint returns in 1988, for AGI above $185,320 as adjusted for inflation)
b. Rules for dependents	(*b*) Each taxpayer may claim a personal exemption for himself or herself and for any dependent whose gross income does not exceed the personal exemption amount. Also, parents may claim a full dependency exemption for their dependent child who has income above the personal exemption amount, if the dependent child is under age 19 or a full-time student, regardless of the child's income.	(*b*) No provision.	(*b*) In the case of an individual who is eligible to be claimed as a dependent on another taxpayer's return, no more than $1,000 of the personal exemption amount can be used to reduce the taxable amount of unearned income on the dependent's return.	(*b*) No personal exemption amount is allowable on the return of an individual who is eligible to be claimed as a dependent on another taxpayer's return; thus, an exemption amount cannot be claimed by a dependent child on the child's return if the child is eligible to be claimed as a dependent on the parents' return. If a child or other dependent who is not allowed a personal exemption under this provision has gross income of less than $100 per year, the individual is not subject to tax on that amount and is not required to file a Federal income tax return for that year
c. Effective date		(*c*) Taxable years beginning on or after January 1, 1986.	(*c*) Taxable years beginning on or after January 1, 1986.	(*c*) Taxable years beginning on or after January 1, 1987.

Item	Present Law	President's Proposal	House Bill	Senate Amendment
4. Adjustments for inflation	The minimum and maximum tax rate bracket amounts, the ZBA (standard deduction), and the personal exemption amount are annually adjusted for inflation measured by 12-month periods ending September 30. If the inflation adjustment is not a multiple of $10, the increase is rounded to the nearest multiple of $10.	Same as present law.	Same as President's proposal, except that the 12-month periods end August 31.	Same as President's proposal and House bill, except that inflation adjustments to the rate brackets, standard deduction (and the $600 additional standard deduction for elderly or blind individuals), and personal exemption amounts are to be rounded down to the nearest multiple of $50.
5. Two-earner deduction	Under present law, differing rate schedules and zero bracket amounts contribute to an increased tax liability (marriage penalty) when two single taxpayers marry and file a joint return. Couples filing a joint return are allowed a tax deduction equal to 10 percent of the lesser of the earned income of the lower-earning spouse or $30,000; the maximum deduction thus is $3,000.	The two-earner deduction would be repealed. *Effective date.*—Taxable years beginning on or after January 1, 1986.	The two-earner deduction is repealed; marriage penalty relief is provided through standard deduction and rate schedules. *Effective date.*—Taxable years beginning on or after January 1, 1986.	Same as House bill. *Effective date.* Taxable years beginning on or after January 1, 1987.
6. Income averaging	An eligible individual (i.e., one who has been self-supporting and a U.S. citizen or resident during the past three years) can elect to have a lower marginal rate apply to the portion of income that is more than 40 percent higher than the average of his or her income for the prior three years.	Income averaging would be repealed. *Effective date.*—Taxable years beginning on or after January 1, 1986.	Same as President's proposal. *Effective date.*—Taxable years beginning on or after January 1, 1986.	Same as President's proposal and House bill, except that income averaging is retained for individuals who are actively engaged in the trade or business of farming during the taxable year if more than 50 percent of their average annual gross income during the three preceding years was attributable to such trade or business (See, also, IV.A.8.) (Provision for farmers added by floor amendments by Senator Metzenbaum, adopted by voice vote.) *Effective date.* Taxable years beginning on or after January 1, 1987.

Item	Present Law	President's Proposal	House Bill	Senate Amendment
B. Earned Income Credit (sec. 111 of the House bill and sec. 111 of the Senate amendment)	Eligible individuals with one or more children are allowed a credit of 11 percent of the first $5,000 of earned income (maximum credit of $550). The amount of the credit is reduced for income exceeding $6,500, and the credit is totally phased out at income of $11,000. The credit is refundable.	The earned income in credit would be increased to 14 percent of the first $5,000 of earned income (maximum credit of $700). The income level at which the phaseout begins would be raised to $6,500, with a total phaseout at $13,500. The maximum amount of the credit as well as the phaseout income levels would be adjusted for inflation occurring after 1984. *Effective date.*—Taxable years beginning on or after January 1, 1986.	Same as President's proposal, except that effective for taxable years beginning on or after January 1, 1987, the income phase-out levels are increased to $9,000/$16,000 (as adjusted for inflation after 1984). *Effective date.*—Taxable years beginning on or after January 1, 1986.	Same as President's proposal and the House bill, except that the income phase-out levels are increased to $10,000/$17,000 (as adjusted for inflation after 1984) effective for taxable years beginning on or after January 1, 1988. The Secretary of the Treasury is directed to require, under regulations, that employers must notify employees with no withholding that they may be eligible for the refundable earned income credit (Floor amendment by Senator Bradley, adopted by voice vote.) *Effective date.*—Taxable years beginning on or after January 1, 1987
C. Exclusions from Income **1. Unemployment compensation (sec. 122 of the House bill and sec. 121 of the Senate amendment)**	Present law provides a limited exclusion from gross income for unemployment compensation benefits received under a Federal or State program. If the sum of the taxpayer's unemployment compensation benefits and AGI does not exceed a base amount, then the entire benefit amount is excluded from income. The base amount is $12,000, in the case of an unmarried individual; $18,000, in the case of a married couple filing a joint return; and zero, in the case of a married couple filing separate returns. If the base amount is exceeded, then the amount of unemployment compensation benefits that is includible in income is equal to the lesser of (1) one-half of the excess of the taxpayer's combined income (modified AGI plus benefits) over the base amount, or (2) the amount of the unemployment compensation.	All unemployment compensation benefits would be includible in gross income. *Effective date.*—Taxable years beginning after December 31, 1986.	Same as President's proposal *Effective date.*—Taxable years beginning after December 31, 1986.	Same as President's proposal and House bill. *Effective date.*—Taxable years beginning after December 31, 1986.

Item	Present Law	President's Proposal	House Bill	Senate Amendment
2. Scholarships and fellowships (sec. 123 of the House bill)	*(a) In general.*—Degree candidates at an educational institution may exclude from income amounts received as a scholarship or fellowship grant, and also incidental amounts received for travel, research, clerical help, and equipment. Nondegree candidates may exclude only scholarships or fellowship grants from tax-exempt organizations or international or governmental agencies, limited to a maximum lifetime exclusion of $10,800. The exclusion for incidental amounts received by nondegree candidates is not limited.	*(a) In general.*—The exclusion for degree candidates would be limited to scholarship or fellowship grants up to the amount spent on tuition and course-required equipment; thus, amounts for room, board, or incidental expenses would not be excludable. The exclusion for nondegree candidates would be limited to reimbursements for incidental expenses (travel, research, clerical help, and equipment).	*(a) In general.*—Same as President's proposal, except that amounts received by nondegree candidates for incidental expenses are not excludable (although offsetting deductions are available if such costs qualify as business expenses under sec. 162).	*(a) In general.*—No provision.
	(b) Payments for services.—In general, amounts received by degree candidates are not eligible for exclusion if they represent payment for teaching or other services required as a condition of receiving the grant. However, an exception permits the exclusion for payments for services if all candidates for a particular degree must perform such services.	*(b) Payments for services.*—The exception allowing the exclusion for payments for services required of all candidates for a particular degree would be repealed.	*(b) Payments for services.*—Same as President's proposal.	*(b) Payments for services.*—No provision.
	(c) Federal grants.—Under another exception, grants received under a Federal program requiring the recipient to perform future services as a Federal employee are excludable to the extent used for tuition and required fees, books, supplies, and equipment.	*(c) Federal grants.*—The exception relating to certain Federal grants would be repealed.	*(c) Federal grants.*—Same as President's proposal.	*(c) Federal grants.*—No provision
		Effective date.—The proposal would be effective for scholarships and fellowships received in taxable years beginning on or after January 1, 1986, except that if a binding commitment to grant a scholarship for a degree candidate is made before January 1, 1986, amounts received would be excludable under present law through 1990.	*Effective date.*—The provision is effective for scholarships and fellowships granted after September 25, 1985.	

3. **Prizes and awards (sec. 123(b) of the House bill and sec. 122 of the Senate amendment)**	*(a) Scientific, etc. achievement awards.*—Prizes and awards received by the taxpayer, other than certain scholarships and fellowship grants, generally are taxable. However, an exclusion applies for awards received for achievements in fields such as charity, the arts, and the sciences, but only if the recipient (i) has not specifically applied for the prize or award (e.g., by entering a contest), and (ii) is not required to render services as a condition of receiving it.	*(a) Scientific, etc. achievement awards.* The present exclusion for awards for charitable, etc. achievement is repealed, except where the recipient assigns the prize or award to a tax-exempt charitable organization	*(a) Scientific, etc. achievement awards.*—Same as President's proposal	*(a) Scientific, etc achievement awards.*—Same as President's proposal and House bill
	(b) Employee awards.—Gifts are excludable from the income of recipients. To qualify as a gift, an item must be given out of detached generosity and not as compensation or to benefit the donor. If an item of tangible personal property awarded to an employee by reason of length of service, productivity, or safety achievement qualifies as a gift, the employer's deduction is limited to $400 ($1,600 under a qualified award plan).	*(b) Employee awards.*—Gift treatment would be denied for all employee awards given by reason of a work-related achievement. Since no employee awards would be both excludable and deductible, the deduction limits under present law would not be applicable.	*(b) Employee awards.*—Same as President's proposal, with clarification that employee awards of low value (such as certain traditional retirement gifts) may qualify as both deductible and excludable under the rules for de minimis fringe benefits enacted in 1984 (Code sec. 132).	*(b) Employee awards.*—Employee awards during a year for length of service or safety achievement are excludable by the employee, and deductible by the employer, to the extent not in excess of $1,600 for all awards and $400 for all awards that are not qualified plan awards. All other awards by employers to employees are includible in income (except, as under the House bill, awards excludable under sec. 132)
		Effective date.—Taxable years beginning after 1985.	*Effective date.*—Taxable years beginning after 1985.	*Effective date.*—Taxable years beginning after 1986.

D. Deductions for Personal Expenditures **1. Itemized deductions for certain State and local taxes (sec. 135 of the Senate amendment)**	Individuals may claim itemized deductions with respect to the following State and local taxes: income taxes, real property taxes, personal property taxes, and sales taxes. Other State and local taxes and foreign taxes are deductible by individuals if incurred in a business or in an income-producing (investment) activity, including such taxes that are allocable to a purchase of property and thus otherwise would have to be capitalized.	Itemized deductions for State and local taxes would be repealed. State and local taxes other than income taxes would be deductible if incurred in a business or, subject to the limitation in the following sentence, in an investment activity. When incurred by an individual in an investment activity, these taxes would be among the category of expenditures that would be deductible "above-the-line" to the extent exceeding one percent of adjusted gross income (see item E, below). *Effective date.*—Taxable years beginning after 1985.	Same as present law.	Same as House bill for State and local income, real property, and personsl property taxes. *Sales taxes.*—State and local general sales taxes are deductible to the extent of 60 percent of the excess of such taxes over State and local income taxes paid or accrued by the taxpayer during the year (floor amendment by Senator Evans, adopted by voice vote). *Resolution.*—It is the sense of the Senate that the bill adopted in conference retain present law regarding deductions for State and local taxes (floor amendment by Sens. Chiles and Domenici, adopted by a vote of 76-21). *Capitalization rule.*—State, local, and foreign taxes for which an itemized deduction is not allowed but which are allocable to a purchase of property are added to the basis of such property. *Effective date.*—Taxable years beginning on or after January 1, 1987.
2. Charitable deduction for nonitemizers (sec. 133 of the House bill)	Nonitemizers may deduct their charitable contributions in addition to taking the standard deduction (ZBA), subject to limitations for pre-1986 years. The maximum nonitemizer deduction was $25 for 1982 and 1983, and $75 for 1984. For 1985, 50 percent of the amount contributed was deductible, without a dollar cap. For 1986, the full amount of contributions is deductible. Under present law, no deduction (beyond the standard deduction) is provided for charitable contributions by nonitemizers made after 1986.	The nonitemizer charitable deduction would be repealed for contributions made after 1985, i.e., one year earlier than the scheduled termination of the nonitemizer deduction under present law.	The nonitemizer charitable deduction is made permanent. Also, the bill modifies the deduction by providing that, for taxable years beginning after 1985, the deduction is subject to a $100 floor.	No provision (thus, the nonitemizer charitable deduction terminates after 1986).

3. **Medical expense deduction** (sec. 134 of the Senate amendment)	Itemizers may deduct unreimbursed medical care expenses to the extent the total of such expenses exceeds five percent of the taxpayer's AGI	No provision.	No provision.	The floor under the itemized medical expense deduction is increased from 5 to approximately 9 percent (substituted for 10-percent floor of committee amendment by floor amendment by Sen Metzenbaum, adopted by vote of 80-18) *Effective date.*—Taxable years beginning on or after January 1, 1987.
4. **Adoption expenses** (secs. 134 and 1407 of the House bill)	An itemized deduction is allowed for up to $1,500 of adoption fees and expenses (such as court costs and attorneys' fees) for the adoption of a child with special needs, i.e., a handicapped or other child eligible for adoption assistance payments under the Social Security Act.	The itemized adoption expense deduction would be repealed in anticipation that a direct expenditure program would be enacted to continue Federal support for families adopting children with special needs. *Effective date.*—Generally January 1, 1987, except that present law would apply for pre-1986 adoptions and special phaseout rules would apply for adoptions during 1986.	(*a*) The itemized adoption expense deduction is repealed. (*b*) The adoption assistance program in Title IV-E of the Social Security Act is amended to provide matching funds as an administrative expense for adoption expenses for any child with special needs who has been placed for adoption in accordance with applicable State and local law. Such expenses include all qualified adoption expenses included in the current tax deduction provision. *Effective date.*—The deduction repeal generally is effective for adoption expenses paid after 1986; present law continues to apply in 1987 for adoptions as to which deductible expenses were incurred in 1986. The effective date of amending the adoption assistance program is coordinated with repeal of the deduction.	Same as present law.
5. **Deductibility of mortgage interest and taxes allocable to tax-free allowances for ministers and military personnel** (sec. 144 of the House bill and sec. 144 of the Senate amendment)	The IRS has ruled that a minister may not deduct mortgage interest and property taxes allocable to a tax-free parsonage allowance. This ruling was based on Code section 265(1), which disallows deductions for expenses allocable to tax-exempt income. This ruling applied effective July 1, 1983, subject to transitional relief (extended through 1986) for ministers owning homes before 1983.	No provision.	The bill provides a permanent rule (effective retroactively) that ministers receiving tax-free parsonage allowances, as well as military personnel receiving tax-free military housing allowances, are not precluded by Code section 265 from deducting mortgage interest or real property taxes on the taxpayer's residence.	Same as House bill

Item	Present Law	President's Proposal	House Bill	Senate Amendment
E. Expenses for Business or Investment 1. Meals, travel, and entertainment expenses (sec. 142 of the House bill and sec. 142 of the Senate amendment)				
a. Meal expenses	*(a)* Meal expenses that constitute ordinary and necessary business expenses generally are deductible if the meal takes place in an atmosphere conducive to business discussion, whether or not business is discussed before, during, or after the meal. Unlike the substantiation rules for deducting other entertainment expenses (see below), the taxpayer need not show that such meal expenses are either directly related to or associated with the active conduct of business.	*(a)* Allowable deductions for a business meal would be limited to $25 times the number of participants in the meal, plus one-half of tha excess. This limit would apply to a taxpayer's meals while away from home on business, but not to meals furnished on the premises of the taxpayer primarily for its employees.	*(a)* The bill generally reduces to 80 percent the amount of deductions otherwise allowable for business meal expenses (including meals away from home and meals furnished on an employer's premises to its employees). Exceptions allowing full deductibility include (i) employee meal expenses reimbursed by the employer (in which case the employer is subject to the 80-percent rule); (ii) employer-furnished meals that are excludible from the employee's income as de minimis fringes under code sec. 132 (including subsidized eating facilities); (iii) meals taxed to employees as compensation; and (iv) items sold to the public (such as the cost of food to restaurants) or furnished to the public as samples or for promotion. The bill also provides that deductions for business meals are subject to the same requirement as for other entertainment expenses (see item (b), below). Thus, no deduction is allowed unless business is discussed during, or directly before or after, the meal (except for an individual eating alone while away from home on business). As an additional requirement not applicable to other entertainment expense, no deduction for business meals is allowable unless the meal has a clear business purpose presently related to the active conduct of the taxpayer's business. The Treasury is instructed to tighten substantiation requirements; special fraud and negligence penalties apply to certain improper deductions	*(a)* Same as House bill, except that full deductibility is allowed in 1987 and 1988 for costs of meals (if not separately stated) that are provided as an integral part of a qualified banquet meeting (i.e., a convention, seminar, annual meeting, or similar business meeting where the program includes the meal, more than 50 percent of the participants are away from home, there are at least 40 attendees, and the meal event includes a speaker).

Item	Present Law	President's Proposal	House Bill	Senate Amendment
b. Entertainment expenses other than for meals	*(b)(1)* Entertainment expenses generally are deductible only if, in addition to constituting ordinary and necessary business expenses, they are either (i) directly related to the active conduct of the taxpayer's business, or (ii) if directly preceding or following a substantial and bona fide business discussion, associated with the active conduct of the taxpayer's business.	*(b)(1)* Deductions for entertainment expenses would be denied, with the following exceptions: (i) expenses paid under a reimbursement arrangement (in which case the deduction would be denied to the party making the reimbursement); (ii) items taxed as compensation to the beneficiaries; (iii) recreational expenses for employees (e.g., Christmas parties); and (iv) items made available to the general public (e.g., samples and promotional activities).	*(b)(1)* The bill generally reduces to 80 percent the amount of deductions otherwise allowable for business entertainment expenses. Exceptions allowing full deductibility include (i) expenses reimbursed by an employer (in which case the employer is subject to the 80 percent rule); (ii) traditional employer-paid recreational expenses for employees (e.g., holiday parties); (iii) items taxed as compensation to the recipient, or excludable from income as section 132 de minimis fringe benefits; (iv) items made available to the general public (e.g., as promotional activities); and (v) tickets to certain charitable fundraising sports events. Ticket costs in excess of face value are not deductible, except with regard to tickets for charitable fundraising sports events.	*(b)(1)* Same as House bill
	(b)(2) No deduction or credit is allowed for the cost of purchasing or constructing certain entertainment facilities (e.g., skyboxes). This deduction disallowance rule does not apply to the rental of such a facility or the costs of box seats or season tickets.	*(b)(2)* No special rule for skyboxes.	*(b)(2)* In addition to the present-law entertainment facility rules, deductions for the rental or other use of a luxury skybox at a sports arena are disallowed, to the extent in excess of the cost of regular tickets, if used by the taxpayer for more than one event.	*(b)(2)* No special rule for skyboxes (general entertainment facility rules continue to apply).
c. Travel expenses (other than for attending conventions)	*(c)(1) Luxury water transportation.*—Travel expenses incurred by a taxpayer while away from home in the conduct of a business generally are deductible. However, the cost of commuting to and from work is not deductible	*(c)(1) Luxury water transportation.*—No deduction would be allowed for the cost of luxury water transportation to the extent in excess of the cost of otherwise available business transportation.	*(c)(1) Luxury water transportation.*—Deductions for cruise ship or other luxury water transportation are limited (subject to certain exceptions) to twice the highest Federal per diem for travel in the U.S., times the number of days in transit. This limitation does not apply to deductions for cruise ship conventions, which remain subject to present-law limitations, or where an exception to the 80-percent deduction rule (above) applies.	*(c)(1) Luxury water transportation.*—Same as House bill.
	(c)(2) Educational travel.—Traveling expenses may be deductible as business expenses if the travel (i) maintains or improves existing employment skills and (ii) is directly related to the taxpayer's duties in his or her employment or trade or business	*(c)(2) Educational travel.*—No deduction would be allowed for costs of travel that would be deductible only on the ground that the travel constitutes a form of education.	*(c)(2) Educational travel.*—Same as President's proposal.	*(c)(2) Educational travel.*—Same as President's proposal and House bill.
	(c)(3) Charitable travel.—Travel away from home may give rise to a charitable deduction if travel expenses (whether paid directly by the individual or indirectly through a contribution by the individual to the charity, which then pays for the individual's travel) are deemed to be incurred in performing services on behalf of the charity.	*(c)(3) Charitable travel.*—No provision.	*(c)(3) Charitable travel.*—The present-law rule applicable to medical deductions for lodging costs away from home (sec. 213(d)(2)(B)) is extended to charitable deductions claimed for transportation and other travel expenses incurred in performing services away from home for a charitable organization. Thus, no deduction is allowed for such expenses (whether paid directly by the individual or indirectly through a contribution to the organization) unless there is no significant element of personal pleasure, recreation, or vacation in the travel away from home.	*(c)(3) Charitable travel.*—No provision.

Item	Present Law	President's Proposal	House Bill	Senate Amendment
d. Travel expenses for attending conventions	*(d)(1) In general.*—The costs of attending a convention or seminar, either for business or for investment purposes, generally are deductible	*(d)(1) In general.*—No special rule (see meal and entertainment limitations described above).	*(d)(1) In general.*—The travel and other costs of attending a convention or seminar for investment purposes (i.e., not for trade or business purposes) are not deductible.	*(d)(1) In general.*—Same as House bill
	(d)(2) Foreign conventions.—No deduction is allowed for the cost of attending a convention outside of the North American area (i.e., not in the U.S., Canada, Mexico, or certain Carribbean countries) unless the taxpayer can show that it was as reasonable to hold the convention there as in the North American areas. Certain Caribbean countries, including Bermuda, are treated as in the North American area if they make available certain tax information to U.S. authorities and certain other requirements are met.	*(d)(2) Foreign conventions.*—No special provision. Under S. 1718 (introduced at the request of the Administration), Bermuda would qualify as in the North American area even if it does not make available tax information, subject to President certification.	*(d)(2) Foreign conventions.*—No special provision.	*(d)(2) Foreign conventions.*—Same as S 1718 (see President's proposal). Thus, Bermuda will be treated as within the North American area for purposes of the foreign convention deductibility rules if the President certifies that such treatment is in the U.S. national security interest and that Bermuda's information exchange programs do not materially impede U.S. tax laws.
e. Effective date (all travel and entertainment provisions)		(e) Taxable years beginning after December 31, 1985.	*(e)* Taxable years beginning after December 31, 1985.	(e) Taxable years beginning after December 31, 1986.

2. Employee business expenses, investment expenses, and other miscellaneous itemized deductions (sec. 132 of the House bill and secs. 132-133 of the Senate amendment)				
a. In general	*(a)* Five types of employee business expenses are allowed "above-the-line" in calculating adjusted gross income under present law: (1) expenses reimbursed by the employer; (2) employee travel expenses; (3) employee transportation expenses; (4) business expenses of employees who are outside salespersons; and (5) employee moving expenses. In addition to the itemized deductions for medical expenses, charitable donations, interest, taxes, and casualty losses, itemizers may deduct certain "miscellaneous deductions." This category includes (1) unreimbursed employee business expenses (other than those deductible above-the-line), including home office expenses of employees; (2) certain expenses related to investment income (such as investment counsel fees); (3) tax return preparation costs; (4) gambling or hobby losses up to the amounts, respectively, of gambling or hobby income; (5) certain adjustments where a taxpayer restores amounts held under claim of right (sec. 1341); (6) amortizable bond premiums (sec. 171); and (7) certain costs of cooperative housing corporations (sec. 216). (The miscellaneous itemized deduction for certain costs of adopting children with special needs is discussed in I.D.4., above.)	(a) The miscellaneous itemized deductions would become deductible "above-the-line", but, along with deductions for unreimbursed employee business expenses (other than moving expenses) currently allowed above-the-line, would be allowed only to the extent that the total of such deductions exceeded one percent of the taxpayer's adjusted gross income. In addition, State and local taxes (other than income taxes) that related to an investment activity of the taxpayer (other than one involving the production of rental or royalty income) would be aggregated with the miscellaneous deductions for purposes of the one-percent floor.	*(a)* Employee business expenses, other than reimbursements and moving expenses, are to be allowed only as itemized deductions, and are subject to the floor described below. The miscellaneous itemized deductions, including the employee business expenses described above, are subject to a floor of one percent of the taxpayer's adjusted gross income (AGI), except that the floor does not apply to gambling losses up to, but not exceeding, gambling income (sec. 165(d)) or estate tax in the case of income in respect of a decedent (sec. 691(c)).	*(a)* Same as House bill with regard to certain employee business expenses currently allowed above-the-line. The miscellaneous itemized deductions allowable under present law are repealed, except for (1) impairment-related work expenses of handicapped employees (floor amendment by Sen. Dole, adopted by voice vote); (2) certain costs of adopting children with special needs (sec. 222); (3) estate tax in the case of income in respect of a decedent (sec. 691(c)); (4) gambling losses up to, but not exceeding, gambling income (sec. 165(d)); (5) certain adjustments where a taxpayer restores amounts held under claim of right (sec. 1341); (6) amortizable bond premiums (sec. 171); (7) certain terminated annuity payments (new sec. 72(b)(3)); and (8) certain costs of cooperative housing corporations (sec. 216).
b. Home office expenses	*(b)* Expenses attributable to use of a part of one's home as an office are deductible subject to the following restrictions: (1) use of the home office must be for the convenience of the employer, (2) the home office must be used regularly and exclusively either as the taxpayer's principal place of business, or to meet patients, clients, or customers, and (3) the deduction cannot exceed the taxpayer's gross income from the business. A recent case held that these limits do not apply when the taxpayer leases a portion of the home to his or her employer.	(*b*) No provision.	*(b)* The present-law limits are to apply when an employee leases a portion of the home to his or her employer. In addition, the home office deduction is limited to the taxpayer's net income from the business (i.e., gross income minus deductions attributable to the business). Disallowed home office deductions may be carried forward to later years.	(*b*) Same as House bill.

2. Employee business expenses, investment expenses, and other miscellaneous itemized deductions (sec. 132 of the House bill and secs. 132-133 of the Senate amendment) (Cont.)				
c. Hobby losses	*(c)* Hobby losses are deductible up to the amount of hobby income. An activity is presumed not to be a hobby, and therefore expenses incurred in the activity generally are not subject to this deduction limitation, if it is profitable in 2 out of 5 consecutive years, or 2 out of 7 years for horse breeding or racing (However, an activity need not meet this standard in order to avoid treatment as a hobby.)	(c) No provision.	*(c)* An activity (other than horse breeding or racing) is presumed not to be a hobby if it is profitable in 3 out of 5 consecutive years. The present-law presumption rules are retained for horse activities.	(c) Same as House bill
d. Effective date		*(d) Effective date* (employee business expenses, etc.).—Taxable years beginning after 1985.	*(d) Effective date* (employee business expenses, etc.).—Taxable years beginning on or after January 1, 1986.	*(d) Effective date* (employee business expenses, etc.).—Taxable years beginning on or after January 1, 1987.
F. Political Contributions Tax Credit (sec. 112 of the House bill)	Individual taxpayers may claim a nonrefundable income tax credit equal to one-half the amount of their contributions to political candidates and certain political campaign organizations during the taxable year. The maximum allowable credit is $50 for an individual and $100 for a married couple filing a joint return.	The political contributions credit would be repealed. *Effective date.*—Taxable years beginning on or after January 1, 1986.	A tax credit is allowed to individuals for the full amount of political contributions, up to a maximum of $100 ($200 for a joint return), made to a Congressional candidate for election in the State in which the taxpayer resides. (Floor amendment by Mr McHugh, adopted by a vote of 230-196. *Effective date.*—Taxable years beginning on or after January 1, 1986.	Same as President's proposal. *Effective date.*—Taxable years beginning on or after January 1, 1987.

A. Cost Recovery: Depreciation; ITC; Finance Leases (secs. 201, 202, 203, and 211 of the House bill and secs. 201, 202, 211, and 212 of the Senate amendment) **1. Accelerated depreciation**				
a. Cost recovery classes	(a) *Cost recovery classes* Under the Accelerated Cost Recovery System ("ACRS"), recovery deductions are determined by applying a statutory percentage to an asset's original cost (adjusted for allowable investment tax credit). The classification of assets under ACRS generally is based on the Asset Depreciation Range ("ADR") system of prior law Under the ADR system, a present class life ("midpoint") was provided for all assets used in the same activity, other than certain assets with common characteristics (e g., cars):	(a) *Cost recovery classes* ACRS would be replaced by the Capital Cost Recovery System ("CCRS"). Under CCRS, a recovery percentage would be applied to an asset's inflation-adjusted basis. Asset classifications under CCRS would not be based on ACRS or ADR; rather assets would be identified by descriptions drawn from the U.S. National Income and Products Account prepared by the Commerce Department	(a) *Cost recovery classes* ACRS is replaced by the Incentive Depreciation System ("IDS"). Under IDS, assets are grouped according to present class lives (or ADR midpoint lives). IDS deductions are subject to increases for inflation adjustments, beginning in 1988.	(a) *Cost recovery classes* ACRS is modified by (1) prescribing depreciation methods for each ACRS class (in lieu of providing statutory tables), (2) reclassifying certain assets, including the creation of a second three-year class to which the straight-line method of depreciation applies, (3) providing more accelerated depreciation for the five- and ten-year ACRS classes (as revised by the bill), and (4) requiring the cost of real property to be recovered using the straight-line method over extended recovery periods
	3-year class: Property with an ADR midpoint of 4 years or less (such as cars and light-duty trucks), *plus* property used in connection with research & experimentation and certain horses. Method is 150 percent declining balance, switching to straight line, over 3 years.	*CCRS Class 1:* 3-year ACRS property Method is equivalent to 220 percent declining balance method, switching to straight line, over 4 years	*Class 1.* Property with ADR midpoints under 5 years, *excluding* cars and light general purpose trucks, and *adding* clothing held for rental Includes motor vehicle special tools and over-the-road tractor units. Method is 200 percent declining balance, switching to straight line, over 3 years	*3-year class.* Same as present law, but *excluding* automobiles, light general purpose trucks, and over-the-road tractor units In addition, property used in connection with research and experimentation is excluded if placed in service before January 1, 1990. Method is 150% declining balance, switching to straight-line, over 3 years.
				Straight-line 3-year class: A new class, including automobiles, light general purpose trucks, and property used to manufacture semiconductors Method is straight-line over 3 years
	5-year class: All tangible personal property not included in any other class Method is 150 percent declining balance, switching to straight line, over 10 years.	*CCRS Class 2:* Trucks, buses, trailers, and office, computing, and accounting equipment. Method is equivalent to 220 percent declining balance method, switching to straight line, over 5 years.	*Class 2.* Property with ADR midpoints of at least 5 but less than 7 years, and *adding* cars and light general purpose trucks, qualified technological equipment, computer-based telephone central office switching equipment, and race horses. Includes trailers, computers, heavy trucks, electronics manufacturing assets, and oil and gas drilling assets. Method is 200 percent declining balance, switching to straight line, over 5 years.	*5-year class:* Same as present law, *adding* research and experimentation property placed in service before January 1, 1990, and *excluding* property with ADR midpoint lives of 16 years and greater (other than computer-based telephone central office switching equipment). Also includes geothermal, ocean thermal, solar and wind energy property, and property that has no ADR midpoint Method is 200% declining balance, switching to straight-line over 5 years
		CCRS Class 3: Construction machinery, tractors, aircraft, mining & oil field machinery, and instruments. Method is equivalent to 198 percent declining balance method, switching to straight line, over 6 years.	*Class 3.* Property with ADR midpoints of at least 7 but less than 10 years Includes offshore drilling, chemicals manufacturing, and distributive trades and services assets. Method is 200 percent declining balance, switching to straight line, over 7 years.	

Item	Present Law	President's Proposal	House Bill	Senate Amendment
1. Accelerated depreciation (cont.) *a. Cost recovery classes (cont.)*		*CCRS Class 4.* All tangible personal property not included in any other class. Includes railroad track and furniture and fixtures. Method is 154 percent declining balance method, switching to straight line, over 7 years.	*Class 4:* Property with ADR midpoints of at least 10 but less than 13 years, and *adding* horses other than race horses, and property that has no ADR midpoint and is not classified otherwise. Includes commercial passenger aircraft, railroad track, agriculture, mining, aerospace manufacturing, and motor vehicle manufacturing assets Method is 200 percent declining balance, switching to straight line, over 10 years.	
		CCRS Class 5: Railroad structures, ships & boats, engines & turbines, plant & equipment for generation, transmission, and distribution of electricity and other power, and distribution plant for communication services. Method is equivalent to 170 percent declining balance method, switching to straight line, over ten years.	*Class 5:* Property with ADR midpoints of at least 13 but less than 16 years, plus single-purpose argicultural or horticultural structures. Includes assets used in pulp manufacturing, primary steel manufacturing, and railroad machinery and equipment. Method is 200 percent declining balance switching to straight line, over 13 years.	
	10-year class: Public utility property with an ADR midpoint of 18.5 to 25 years, certain burners and boilers with an ADR midpoint of 25 years, amusement park structures, railroad tank cars, and manufactured homes Method is 150 percent declining balance, switching to straight line, over 10 years		*Class 6:* Property with ADR midpoints of at least 16 but less than 20 years. Includes vessels and barges Method is 200 percent declining balance, switching to straight line, over 16 years.	*10-year class:* Same as present law, *adding* property with an ADR midpoint of 16 years or more (other than computer-based telephone central office switching equipment), and *excluding* utility property with an ADR midpoint of 20 years or more. Method is 200% declining balance, switching to straight-line, over 10 years.
	15-year public utility class: Other public utility property with an ADR midpoint of more than 25 years. Method is 150 percent declining balance, switching to straight line, over 15 years.		*Class 7:* Property with ADR midpoints of at least 20 but less than 25 years, *plus* very low-income housing Includes cement manufacturing, pipeline transportation, and nuclear production of electricity Method is 200 percent declining balance, switching to straight line, over 20 years.	*15-year class:* Utility property (whether the property is used by a public utility or an unregulated company) with ADR midpoints of 20 years or more and industrial steam and electric generation or distribution equipment described in ADR class 00.4 Method is 150% declining balance, switching to straight-line, over 15 years
			Class 8: Property with ADR midpoints of at least 25 but less than 30 years, *plus* telephone distribution plant and comparable equipment used by other transmitters of information Includes electric utility steam power production. Method is 200 percent declining balance, switching to straight line, over 25 years.	

1. Accelerated depreciation (cont.) a. *Cost recovery classes (cont.)*	*15-year real property class:* Low-income housing. Method is 200 percent declining balance, switching to straight line, over 15 years.		*Class 9:* Property with ADR midpoints of at least 30 but less than 36 years, *plus* low-income housing (other than very low-income housing). Includes railroad structures, electric transmission and distribution plant, and gas distribution facilities. Method is 200 percent declining balance, switching to straight line, over 30 years.	
	19-year real property class: Buildings and structures. With relatively few exceptions, ADR lives were not assigned to buildings. Method is 175 percent declining balance, switching to straight line, over 19 years.	*CCRS Class 6:* ACRS 19-year real property and low-income housing. Method is equivalent to 112 percent declining balance method, switching to straight line, over 28 years.	*Class 10:* Property with ADR midpoints of at least 36 years, *plus* all other real property. Method is straight line over 30 years.	*Residential rental property class:* Real property that is residential rental property. Method is straight-line over 27.5 years. *Nonresidential real property class:* Real property (that is not 10-year property or residential rental property). Method is straight-line over 31.5 years.

Item	Present Law	President's Proposal	House Bill	Senate Amendment
1. Accelerated depreciation (cont.) *b. Classification of special types of property*		No special provisions		
(i) Automobiles (ADR midpoint of 3 years) and light trucks (ADR midpoint of 4 years)	3-year class		Class 2 (5 years)	Straight-line 3-year class
(ii) Research and experimentation property (various ADR midpoints)	3-year class		No special provision.	5-year class if placed in service before January 1, 1990 (the expiration date of the incremental research credit), and 3-year class if placed in service thereafter
(iii) Over-the-road tractor units (ADR midpoint of 4 years)	3-year class.		Class 1 (3 years).	5-year class
(iv) Race horses	3-year class.		Class 2 (5 years)	3-year class.
(v) Horses over 12 years old	3-year class		Class 4 (10 years).	3-year class.
(vi) Property with no ADR midpoint (other than real property), e.g., railroad track	Generally, 5-year class.		Class 4 (10 years) (treated as if property had an ADR midpoint of 12 years).	5-year class (treated as if property had an ADR midpoint of 12 years)
(vii) Semi-conductor manufacturing equipment (ADR midpoint of 6 years)	5-year class.		Class 2 (5 years)	Straight-line 3-year class.
(viii) Retail rental clothing (ADR midpoint of 9 years)	5-year class		Class 1 (3 years).	5-year class
(ix) Computer-based central office switching equipment (ADR midpoint of 18 years)	5-year class		Class 2 (5 years).	5-year class
(x) Single-purpose agricultural or horticultural structures (ADR midpoint of 25 years)	5-year class		Class 5 (13 years).	10-year class
(xi) Railroad tank cars (ADR midpoints of 14 years and 15 years)	10-year class.		Class 5 (13 years).	10-year class
(xii) Qualified coal utilization property (various ADR midpoints)	10-year class.		No special provision	10-year class
(xiii) Manufactured homes	10-year class		Class 10 (30 years)	10-year class

Item	Present Law	President's Proposal	House Bill	Senate Amendment
I. Accelerated depreciation (cont.) *b. Classification of special types of property (cont.)*				
(xiv) Geothermal, ocean thermal, solar, and wind energy property (various ADR midpoints and no ADR midpoints)	5-year class, if not owned by a regulated utility Certain assets may be 15-year class property if owned by a regulated utility		No special provision.	5-year class
(xv) Telephone distribution plant (ADR midpoint of 35 years)	5-year class if not owned by a regulated utility; 15-year class otherwise.		Telephone distribution plant and comparable equipment used by other transmitters of information (e.g., cable television operators) is class 8 property (25 years).	15-year class.
(xvi) Low-income housing	Generally, rental housing where at least 85 percent of the tenants have incomes of 80 percent or less of area median income may be depreciated over 15 years.		Rental housing where at least 40% of the tenants have incomes of 60% or less of area median income is Class 7 property (20 years). Rental housing where either (a) at least 20% of the tenants have incomes of 70% or less of area median income or (b) at least 25% of the tenants have incomes of 80% or less of area median income is Class 9 property (30 years accelerated).	No special provision, but see low-income housing credit (item II E.3, below).
(xvii) Qualified technological equipment, as defined in the tax-exempt entity leasing rules	5-year class		Class 2 (5 years).	5-year class
c. Luxury cars	(c) Recovery deductions for automobiles are subject to the following dollar limitations: $3,200 for the first recovery year; $4,800 for each succeeding taxable year in the recovery period	(c) Retain present law.	(c) Same as President's proposal	(c) Conforms the fixed limitations on deductions so that the price range of affected cars is unchanged Depreciation deductions are limited to $2,133 for the first year in the recovery period, and $4,210 for each succeeding year In addition, clarifies that the fixed limitations apply to all deductions claimed for depreciation of automobiles, not just ACRS deductions
d. Changes in classification	(d) Under ACRS, recovery periods are fixed	(d) Treasury would monitor and analyze actual experience with all tangible depreciable assets so that changes could be made.	(d) As under the President's proposal, Treasury has authority to adjust class lives based on actual experience with certain depreciable assets (other than 30-year real property or low-income housing) and any new class life will be used for determining the class of such property and in applying the alternative depreciation system	(d) Same as President's proposal and House bill, except the lives of certain other property in addition to residential rental property and nonresidential real property may not be changed

Item	Present Law	President's Proposal	House Bill	Senate Amendment
2. Alternative cost recovery system *a. In general*	(a)(i) ACRS deductions are reduced for property that is (1) used predominantly outside the United States or (2) leased to a tax-exempt entity Different depreciation methods are also used for purposes of (1) computing earnings and profits of a domestic corporation, and (2) applying the minimum tax provisions.	(a) A system intended to allow depreciation deductions that approximate the assumed decline in an asset's value would apply for certain purposes. Although no specific system is recommended, the Administration proposal indicates that the depreciation system set forth in the 1984 Treasury report ("RCRS") would serve as the model. Under RCRS, the inflation-adjusted basis of property would be recovered over periods ranging from 5 years for short-lived property to 63 years for real property.	(a)(i)(A) An alternative cost recovery system is provided for the following purposes: (1) property used predominantly outside the United States, (2) property leased to a tax-exempt entity, (3) for computing earnings and profits of a domestic corporation, and (4) for applying the minimum tax provisions. Depreciation deductions are computed under the method that is used under present law for property that is leased to a tax-exempt entity, which is generally straight-line over the ADR midpoint life. The cost of qualified technological equipment is recovered over 5 years and real property over 40 years.	(a)(i)(A) Same as House bill
			(B) Property which is classified for the incentive system on a basis other than ADR midpoint is treated as having the same recovery period as for the incentive system (e.g., automobiles and computer-based central office switching equipment are recovered over 5 years).	(B) The recovery period for automobiles, light trucks, and over-the-road tractor units is 5-years.
	(ii) Property, other than low-income housing, to the extent it is financed with industrial development bonds, the interest on which is tax-exempt, is depreciated using the straight-line method over the ACRS recovery period		(ii) If all or part of property, other than low-income housing, is financed with bonds, the interest on which is tax-exempt, it is depreciated using the straight-line method over the naxt longest IDS class (40 years for real property).	(ii) Generally, property to the extent it is financed with bonds, the interest on which is tax-exempt, is depreciated using the same method as in (i). The recovery period for solid waste disposal facilities and hazardous waste treatment facilities is 8 years, and for low-income housing is 27.5 years.
	(iii) Taxpayers can elect to use the straight-line method over the applicable ACRS recovery period (or over a longer recovery period) with respect to one or more classes of ACRS property placed in service during a taxable year.		(iii) Taxpayers may elect the alternative cost recovery system described in (i) for property that is otherwise eligible for incentive depreciation on a class-by-class, year-by-year basis.	(iii) Taxpayers may elect either the alternative cost recovery system or the straight-line method over the ACRS recovery period for property that is otherwise eligible for ACRS on a class-by-class, year-by-year basis
b. Property predominantly of foreign origin	(b) There is Presidential authority to deny the investment tax credit, but not accelerated depreciation	(b) No provision	(b) Provides Presidential authority to deny accelerated depreciation to property produced abroad, similar to present-law rules applicable to the investment tax credit.	(b) Same as House bill.
c. Property used in outer space	(c) No provision.	(c) No provision	(c) Property launched by a U.S. person from the United States and used in outer space is not treated as foreign use property.	(c) Same as House bill
3. Indexing	The basis of depreciable property is not adjusted for inflation; however, depreciation allowances are accelerated, in part, to compensate for inflation	Beginning with the second year an asset is in service, the asset's unrecovered basis would be adjusted upwards for inflation.	Beginning in 1988, IDS deductions are increased for half the annual inflation in excess of 5 percent since the second year an asset is placed in service.	Retains present law

Item	Present Law	President's Proposal	House Bill	Senate Amendment
4. Accounting conventions				
a. Half-year convention	(a) The statutory schedules for personal property reflect a half-year convention that results in a half-year depreciation allowance for the first recovery year, regardless of when property is placed in service during the year	(a) The depreciation allowance for the first year would be based on the number of months the asset was in service	(a) For personal property, both the first and last depreciation allowances for an asset reflect the half-year convention	(a) Same as House bill.
b. Mid-month convention	(b) Under a mid-month convention, real property (other than low-income housing) placed in service or disposed of at anytime during a month is treated as having been placed in service or disposed of in the middle of the month.	(b) The same mid-month convention that applies to most real property under present law would apply to all property.	(b)(i) For Class 10 property and low-income housing, apply the present-law mid-month convention. (ii) For other property, apply the mid-month convention to taxpayers who place more then 40 percent of property in service during the last quarter of the taxable year	(b)(i) The present-law mid-month convention applies to residential rental property and nonresidential real property. (ii) Same as House bill.
5. Gain on disposition				
a. In general	(a) With limited exceptions, gain is "recaptured" as ordinary income to the extent of previously allowed depreciation deductions. Gain in excess of amounts subject to recapture is treated as capital gain. These rules have no application to nondepreciable property used in a trade or business (such as land).	(a) All gain on disposition of depreciable property would be taxed as ordinary income.	(a) Retains present law	(a) Same as House bill (retains present law).
b. Residential real property	(b) For residential real property held for more than one year, gain is recaptured only to the extent that accelerated depreciation deductions exceed straight-line deductions. Recapture for low-income housing is phased out after property has been held for a prescribed period.	(b) No special provision.	(b) For low-income housing, only the excess of IDS deductions over straight line deductions (over the applicable recovery period) is recaptured, and the phaseout of recapture is repealed. For property that ceases to qualify as low-income housing after a sale-leaseback, Treasury is granted regulatory authority to determine the recapture amount by reference to straight line depreciation over 30 years. For other residential real property that is 30-year property, there is no recapture.	(b) For all residential rental property, there is no recapture.
c. Nonresidential real property	(c) There is no recapture if the taxpayer elected to recover the property's cost using the straight-line method. Otherwise, the full amount of depreciation—to extent of gain—is recaptured.	(c) No special provision.	(c) For nonresidential (30-year) real property, there is no recapture.	(c) Same as House bill.

Item	Present Law	President's Proposal	House Bill	Senate Amendment
6. Lessee leasehold improvements	A lessee recovers the cost of leasehold improvements over the shorter of the property's ACRS recovery period or the portion of the lease term remaining on the date the property is acquired. Under statutory rules provided for use in determining the term of a lease, in certain cases, a lease term includes periods during which the lease may be renewed pursuant to an option held by the lessee, unless the lessee establishes that it is more probable than not that the lease will not be renewed. In other cases, the statute provides that a lease term is determined by excluding renewal options held by the lessee, unless the facts show with reasonable certainty that the lease will be renewed. These rules also apply in determining the amortization period for lease acquisition costs.	The cost of leasehold improvements made by a lessee would be recovered under the general rules, without regard to the lease term, except where the improvement is reasonably expected to have no residual value on expiration of the lease.	A lessee recovers capital costs under the general rules in every case.	Same as House bill. The statutory rules for determining the term of a lease—the only future relevance of which would be in determining the amortization period for lease acquisition costs—is amended to provide that the term of a lease is determined by including all renewal options as well as any period for which the parties reasonably expect the lease to be renewed.
7. Repair allowances	Expenditures that prolong the life of an asset are recoverable in the same manner as the cost of a capital asset. Other expenditures for repair or maintenance are expensed. The characterization of an expense as a capital expenditure or a deductible repair requires a factual determination.	Each asset class would be assigned a safe-harbor repair allowance factor. A taxpayer would automatically deduct expenses to the extent the expenses do not exceed the product of the asset's inflation-adjusted basis multiplied by the repair allowance factor.	Retains present law.	Same as House bill (retains present law).
8. Expensing	Taxpayers can elect to expense up to $5,000 of the cost of personal property that is purchased and used in a trade or business. The $5,000 ceiling is scheduled to increase to $7,500 for taxable years beginning in 1988 and 1989, and to $10,000 for years beginning after 1989. The dollar limitation is subject to apportionment among certain related entities. If expensed property is converted to nonbusiness use within two years of the time the property was placed in service, the difference between the amount expensed and the ACRS deductions that would have been allowed for the period of business use is recaptured as ordinary income.	The scheduled increases in the ceiling would be repealed.	Provides a $10,000 ceiling and limits eligibility for expensing to taxpayer whose total investment in tangible personal property for taxable year is $200,000 or less.	Provides a $10,000 ceiling for expensing to taxpayers whose total investment in tangible personal property is $200,000 or less. For other taxpayers, for every dollar of investment in excess of $200,000, the $10,000 ceiling is reduced by one dollar. The amount eligible to be expensed is limited to the taxable income derived from the active trade or business in which the property is used. The difference between expensing and ACRS deductions is recaptured if property is converted to nonbusiness use at any time before the end of the property's recovery period.
9. Vintage accounts	Taxpayers generally compute depreciation deductions on an asset-by-asset basis. There is an election to establish mass asset vintage accounts for assets in the same recovery class and placed in service in the same year. The definition of assets eligible for inclusion in mass asset accounts is limited, primarily because of concern about the mechanics of recapturing investment tax credit.	Mass asset vintage accounts would be retained for property qualifying for such treatment under ACRS.	With repeal of the investment tax credit, the definition of eligible property is expanded to include all property.	Same as House bill.

Item	Present Law	President's Proposal	House Bill	Senate Amendment
10. Public utility property	The benefits of accelerated depreciation must be normalized.	Same as present law	Same as present law; also, special normalization rules are applied to excess deferred tax reserves resulting from the reduction of corporate income tax rates	Same as House bill
11. Effective dates for depreciation				
a. In general		(a) CCRS would be effective for property placed in service on or after January 1, 1986.	(a) Effective for property placed in service on or after January 1, 1986.	(a) Effective for property placed in service on or after January 1, 1987.
b. Anti-churning rules		(b) Under rules similar to those enacted as part of ACRS, taxpayers would be prevented from bringing property placed in service before the effective date under CCRS by certain post-effective date transactions among related parties.	(b) No provision.	(b) Under rules similar to those enacted as part of ACRS, taxpayers are prevented from bringing property placed in service before the effective date under the revised ACRS by certain post-effective date transactions among related parties.
c. Transition rules		(c) No provision.	(c) ACRS would apply to: (1) property that is constructed, reconstructed, or acquired pursuant to a written contract that was binding as of September 25, 1985, or (2) property constructed or reconstructed by the taxpayer, if the lesser of $1 million or 5 percent of cost has been incurred or committed by September 25, 1985, if construction commenced by that date, or (3) an equipped building or a plant facility, if construction has commenced as of September 25, 1985, pursuant to a written specific plan, and more than half of the cost has been incurred or committed by that date, and if property or project is placed in service by July 1, 1986, in the case of Class 1 property, cars, and light general purpose trucks; by January 1, 1987, in the case of Class 2 property; by January 1, 1989, in the case of Class 3–6 property; and by January 1, 1991, in the case of Class 7–10 property. ACRS would apply to property that qualifies under (1), (2), or (3) which is sold and leased back by the person initially committed to acquire the property within a 3-month window. Special transitional rules are provided	(c) Present law ACRS would apply to property with an ADR midpoint of 7 years or greater (other than computer-based telephone central office switching equipment) that is: (1) constructed, reconstructed, or acquired pursuant to a written contract that was binding as of March 1, 1986, or (2) constructed or reconstructed by the taxpayer, if the lesser of $1 million or 5 percent of cost has been incurred or committed by March 1, 1986, if construction commenced by that date, or (3) an equipped building or a plant facility, if construction has commenced as of March 1, 1986, pursuant to a written specific plan, and more than half of the cost has been incurred or committed by that date, and if such property or project is placed in service by January 1, 1989 in the case of property with an ADR midpoint less than 20 years; and by January 1, 1991 in the case of property with an ADR midpoint of 20 years and greater and residential rental and nonresidential real property. Present law ACRS would apply to property that qualifies under (1), (2), or (3) which is sold and leased back by the person initially committed to acquire the property within a 3-month window Special transitional rules are provided

Item	Present Law	President's Proposal	House Bill	Senate Amendment
12. Regular investment tax credit				
a. Allowable credit	A credit against income tax liability is allowed for up to ten percent of a taxpayer's investment in tangible personal property (six percent for property in the three-year ACRS class).	The regular investment tax credit would be repealed	Same as President's proposal	Same as President's proposal and House bill
b. Public utility property	For public utility property, the tax benefits of the credit must be normalized	Normalization rules would be retained for the unamortized portion of investment tax credits allowed to public utilities.	Same as President's proposal.	Same as President's proposal and House bill.
c. Effective dates				
i. General		(i) Repeal would be effective for property placed in service on or after January 1, 1986	(i) Repeal is effective for property placed in service on or after January 1, 1986.	(i) Same as House bill
ii Transition rules		(ii) No provision	(ii) The credit is available under the same circumstances in which present-law depreciation rules would continue to apply Special transition rules are provided	(ii) The credit is available under transitional rules for property that is: (1) constructed, reconstructed, or acquired pursuant to a written contract that was binding as of December 31, 1985, or (2) constructed or reconstructed by the taxpayer, if the lesser of $1 million of 5 percent of cost has been incurred or committed by December 31, 1985, if construction commenced by that date, or (3) an equipped building or a plant facility, if construction has commenced as of December 31, 1985, pursuant to a written specific plan, and more than half of the cost has been incurred or committed by that date, and if such property is placed in service by July 1, 1986, in the case of property with an ADR midpoint less than 5 years, by January 1, 1987, in the case of property with an ADR midpoint of at least 5 but less than 7 years and including computer-based central office switching equipment; by January 1, 1989, in the case of property with an ADR midpoint of at least 7 but less than 20 years; and by January 1, 1991, in the case of property with an ADR midpoint of 20 years and greater, residential rental property, and nonresidential real property. The credit is available for property that qualifies under (1), (2), or (3) which is sold and leased back by the person initially committed to acquire the property within a 3-month window Special transitional rules are provided

Item	Present Law	President's Proposal	House Bill	Senate Amendment
d. Mandatory reduction of ITC carryovers	Unused investment tax credits are allowed a three-year carryback and a 15-year carryforward Credits that are not used before the end of the carryforward period expire	No provision	No provision	For taxable years beginning after December 31, 1986, the ITC amount allowable for carryovers is reduced by 30 percent (15 percent in the case of credits allowable for a taxable year beginning in 1987).
e. Reduction of credits claimed under transition rules	No provision.	No provision.	A taxpayer must spread the credit earned on transition property ratably over 5 years. A basis adjustment is required for the full investment credit in the first taxable year	The same reduction that would apply to carryovers would also apply to credits earned under transition rules
13. Finance leases	Under the finance lease rules, the fact that a lessee has a fixed-price option to purchase the property or the leased property is limited use property is not taken into account in determining whether the aggreement is a lease. The finance lease rules are scheduled to go into effect after December 31 1987, although the rules are available currently for limited categories of property.	No provision.	Repeals the finance lease rules. *Effective date.*—Agreements entered into on or after January 1, 1986 (for property that qualifies for finance lease transition rules under prior tax acts, January 1, 1988).	Same as House bill. *Effective date.*—Agreements entered into on or after January 1, 1987 (for property that qualifies for finance lease transition rules under prior tax acts, January 1, 1988)
B. Limitation on Business Tax Credits (sec. 501(c)(4) of the House bill and sec. 631 of the Senate amendment)	The business tax credits earned by a taxpayer can be used to reduce up to 85 percent of tax liability in excess of $25,000.	No provision	The limitation on the amount of income tax liability (in excess of $25,000) is reduced from 85 percent to 75 percent. *Effective date.*—Taxable years beginning after December 31, 1985.	Same as House bill. *Effective date.*—Taxable years beginning after December 31, 1986

Item	Present Law	President's Proposal	House Bill	Senate Amendment
C. Research and Development				
1. Tax credit for increasing research expenditures (sec. 231 of the House bill and sec. 1301 of the Senate amendment)	*(a) Expiration date.*—The research tax credit does not apply to expenses paid or incurred after December 31, 1985.	*(a) Expiration date.*—The research tax credit would be extended for an additional three years, through December 31, 1988.	*(a) Expiration date.*—Same as President's proposal (three-year extension through December 31, 1988).	*(a) Expiration date.*—The research tax credit is extended for an additional four years, through December 31, 1989.
	(b) Rate.—The taxpayer may claim a 25-percent tax credit for excess of (1) qualified research expenditures for the taxable year incurred in carrying on a business over (2) the average amount of the taxpayer's yearly qualified research expenditures in the preceding three taxable years.	*(b) Rate.*—Same as present law (25-percent incremental credit).	*(b) Rate.*—Credit rate is reduced to 20 percent.	*(b) Rate.*—Same as President's proposal (25-percent incremental credit).
	(c) Research definition.—The credit provision adopts the deduction definition of research (in sec. 174), but subject to three exclusions: (1) research conducted outside the U.S.; (2) research in the social sciences or humanities; and (3) research to the extent funded, through grant or contract, by another person or governmental entity.	*(c) Research definition.*—The definition of qualified research (for purposes of the credit) would be revised to limit the credit to research activities involving a process of experimentation intended to result in technological innovations in products and production processes.	*(c) Research definition.*—The committee report clarifies that the credit does not apply to expenditures for certain nonresearch activities (activities occurring after the beginning of production; adaptation of an existing product; and studies and surveys). In addition, the report modifies the definition of credit-eligible research (effective for taxable years beginning after 1985) to target the credit to research undertaken to discover information that is technological in nature and that pertains to functional aspects of products.	*(c) Research definition.*—Same general approach as under the House bill, except that the definitional rules (effective for taxable years beginning after 1985) are set forth in statutory language. Thus, the credit is targeted to research undertaken to discover information that is technological in nature and that pertains to functional aspects of products. Also, the bill expands the present-law list of credit exclusions to include expenditures for the types of nonresearch activities excluded under the House bill.
	(d) Qualified expenditures.—Research expenditures eligible for the credit consist of (a) in-house expenditures for research wages and supplies; (b) rental or user fees for research use of laboratory equipment, computers, or other personal property; (c) 65 percent of amounts paid by the taxpayer for contract research conducted on the taxpayer's behalf; and (d) 65 percent of a corporate taxpayer's expenditures (including grants or contributions) for basic research performed by universities or certain scientific research organizations.	*(d) Qualified expenditures.*—No provision.	*(d) Qualified expenditures.*—Leased research equipment is treated the same as purchased equipment; i.e., rental and similar payments for personal property (other than payments to others for use of computer time) are ineligible for the credit.	*(d) Qualified expenditures.*—No provision (i.e., rental or user fees for research use of laboratory equipment, computers, or other personal property remain eligible for the credit).
	(e) University credit.—Expenditures eligible for the 25-percent incremental research credit include 65 percent of a corporate taxpayer's expenditures (including grants or contributions) for basic research performed by universities or certain scientific research organizations.	*(e) University credit.*—No provision.	*(e) University credit.*—A 20-percent tax credit applies to the *excess* of (1) 100 percent of corporate cash expenditures for university basic research *over* (2) the sum of (a) the greater of two fixed research floors plus (b) an amount reflecting any decrease in nonresearch giving to universities by the corporation as compared to such giving during a fixed base period, as adjusted for inflation.	*(e) University credit.*—Same as House bill.

Item	Present Law	President's Proposal	House Bill	Senate Amendment
1. Tax credit for increasing research expenditures (Cont.)	*(f) Credit use limitation.*—The research credit is not subject to the general limitation on use of business credits (under present law, 85 percent to tax liability over $25,000).	*(f) Credit use limitation.*—No provision	*(f) Credit use limitation.*—The general limitation on business credits applies to the research credit. *Effective date.*—Taxable years beginning after 1985	*(f) Credit use limitation.*—Same as the House bill. *Effective date.*—The provision extending the credit applies to taxable years beginning after December 31, 1985. The provisions relating to the research definition, university credit, and credit use limitation apply for taxable years beginning after December 31, 1985.
2. Augmented charitable deduction for certain donations of scientific equipment (sec. 231(f) of the House bill)	Under a special rule, corporations are allowed an augmented charitable deduction for donations of newly manufactured scientific equipment to a college or university for research use in the physical or biological sciences	No provision.	The category of eligible donees under the special rule is expanded to include certain tax-exempt scientific research organizations. *Effective date.*—Taxable years beginning after December 31, 1985.	No provision.
3. Tax credit for orphan drug clinical testing (sec. 283 of the House bill and sec. 1709 of the Senate amendment)	A 50-percent tax credit is allowed for a taxpayer's expenses of clinical testing of certain drugs for rare diseases or conditions The credit is scheduled to expire after 1987.	Same as present law (i.e., credit expires after 1987).	The tax credit for clinical testing of orphan drugs is extended for one additional year (i.e., through December 31, 1988).	The credit is made permanent. (Floor amendment by Sen. Metzenbaum, agreed to voice vote.)

Item	Present Law	President's Proposal	House Bill	Senate Amendment
D. Rapid Amortization Provisions				
1. Five-year amortization of trademark and trade name expenditures (sec. 221 of the House bill and sec. 634 of the Senate amendment)	Taxpayers may elect to amortize over a period of at least 60 months expenditures for the acquisition, protection, expansion, registration, or defense of a trademark or trade name, other than an expenditure which is part of the consideration for an existing trademark or trade name.	The election would be repealed. Trademark and trade name expenditures would therefore generally be capitalized and recovered on a disposition of the asset. *Effective date.*—The repeal would be effective for expenditures paid or incurred on or after January 1, 1986.	Same as President's proposal. *Effective date.*—Expenditures paid or incurred on or after January 1, 1986. *Transition rule.*—Present law applies to expenditures incurred: (i) pursuant to a written contract that was binding as of September 25, 1985; or (ii) with respect to development, protection, expansion, registration or defense commenced as of September 25, 1985, if the lesser of \$1 million or 5 percent of cost has been incurred or committed by that date; provided in each case the trademark or trade name is placed in service before January 1, 1988.	Same as President's proposal and House bill. *Effective date.*—Expenditures paid or incurred after December 31, 1986 *Transition rate.*—Present law applies to expenditures incurred: (i) pursuant to a written contract that was binding as of March 1, 1986; or (ii) with respect to development, protection, expansion, registration or defense commenced as of March 1, 1986, if the lesser of \$1 million or 5 percent of cost has been incurred or committed by the date, provided in each case the trademark or tradename is placed in service before January 1, 1988.
2. Five-year amortization of pollution control facilities (sec. 222 of the House bill)	Taxpayers may elect to amortize over a 60-month period the cost of a qualifying certified pollution control facility used in connection with a plant that was in operation before 1976. To the extent that a pollution control facility has a useful life in excess of 15 years, a portion of the facility's cost is not eligible for 60-month amortization, but must be recovered through depreciation.	The election would be repealed. Expenditures for pollution control facilities would therefore be recovered in accordance with the applicable depreciation schedules. *Effective date.*—The repeal would be effective for expenditures paid or incurred on or after January 1, 1986.	Same as President's proposal. *Effective date.*—Expenditures paid or incurred on or after January 1, 1986 *Transition rule.*—Present law applies to expenditures incurred: (i) pursuant to a written contract that was binding as of September 25, 1985; or (ii) with respect to facilities, construction of which is commenced as of September 25, 1985, if the lesser of \$1 million or 5 percent of cost has been incurred or committed by that date; provided in each case the facility is placed in service before January 1, 1988.	Same as present law.

Item	Present Law	President's Proposal	House Bill	Senate Amendment
3. Fifty-year amortization of qualified railroad grading and tunnel bores (sec. 224 of the House bill)	Domestic railroad common carriers may elect to amortize the cost of qualified railroad grading and tunnel bores over a 50-year period. "Qualified railroad grading and tunnel bores" include all land improvements (including tunneling) necessary to provide, construct, reconstruct, alter, protect, improve, replace, or restore a roadbed or right-of-way for railroad track.	The election would be repealed. Expenditures for railroad grading and tunnel bores would therefore be capitalized and recovered on disposition of the asset. *Effective date.*—The repeal would be effective for expenses paid or incurred on or after January 1, 1986.	Same as President's proposal. In addition, special ACRS treatment is provided for a particular railroad disaster and involuntary conversion treatment of insurance proceeds in that case is specified. *Effective date.*—Expenses paid or incurred on or after January 1, 1986. *Transition rule.*—Present law continues to apply to expenditures incurred: (i) pursuant to a written contract that was binding as of September 25, 1985; or (ii) with respect to construction, reconstructioo, alteration, improvement, replacement or restoration commenced as of September 25, 1985, if the lesser of $1 million or 5 percent of cost has been incurred or committed by that date, provided in each case the improvements are placed in service before January 1, 1988.	Same as present law. However, the treatment provided for a particular railroad disaster is the same as the House bill.
4. Deduction for loss in value of bus operating authorities (sec. 635 of the Senate amendment)	Generally, no deduction is allowed for a decline in value of property absent a sale or other disposition. The courts have denied a loss deduction where the value of an operating permit or license decreased as the result of legislation that expanded the number of permits or licenses issued, on the grounds that the permit or license continued to have value as a right to carry on a business.	No provision	No provision.	Taxpayers are allowed an ordinary deduction ratably over a 60-month period for the adjusted bases of bus-operating authorities held on November 19, 1982, (the date of enactment of the Bus Regulatory Reform Act) or acquired after that date under a written contract that was binding on that date. *Effective date.*—The provision is effective retroactively for taxable years ending after November 18, 1982.
5. Expensing for costs of removing architectural barriers to the handicapped and elderly (sec. 225 of the House bill and sec. 1707 of the Senate amendment)	Taxpayers may elect to deduct up to $35,000 of qualifying expenses for the removal of architectural and transportation barriers to the handicapped and elderly in the year paid or incurred, instead of capitalizing them. The election is not available in taxable years beginning after December 31, 1985.	No provision.	The election to deduct qualifying expenditures is extended for two years, to taxable years beginning before January 1, 1988.	The election to deduct qualifying expenditures is extended permanently, effective for taxable years beginning after December 31, 1985.

Item	Present Law	President's Proposal	House Bill	Senate Amendment
E. Real Estate Provisions				
1. Tax credit for rehabilitation expenditures (sec. 232 of the House bill and sec. 1412 of the Senate amendment)				
a. Nonhistoric structures	The credit is 15 percent for nonresidential buildings at least 30 years old, and 20 percent for nonresidential buildings at least 40 years old. If the 15- or 20-percent credit is allowed, depreciable basis is reduced by the amount of credit earned. The credit is available only if the taxpayer elects to use the straight-line method of cost recovery with respect to rehabilitation expenditures. Rehabilitation expenditures are eligible for the credit only if incurred in connection with a substantial rehabilitation in which either (i) 75 percent of external walls are retained in place as external walls, or (ii) 75 percent of external walls are retained in place as internal or external walls; 50 percent of external walls are retained in place as external walls; and 75 percent of the building's internal structural framework is retained in place.	The 15- and 20-percent credits would be repealed. *Effective date.*—January 1, 1986.	Provides one 10-percent credit. Limits credit to buildings placed in service before 1936, and deletes the alternative test that only looks to 75 percent of walls. *Effective date.*—Property placed in service on or after January 1, 1986.	Same as House bill. *Effective date.*—Property placed in service on or after January 1, 1987.
b. Certified historic structures	The credit is 25 percent for certified historic structures. If the 25-percent credit is allowed, depreciable basis is reduced by 50 percent of the amount of credit earned. The credit is available only if the taxpayer elects to use the straight-line method of cost recovery with respect to rehabilitation expenditures. The external-walls test of the substantial rehabilitation requirement applies (as described above).	The credit for rehabilitations of certified historic structures would be repealed. *Effective date.*—January 1, 1986.	Reduce credit to 20 percent, require a full-basis adjustment, and delete the external-walls tests. *Effective date.*—Property placed in service on or after January 1, 1986.	Same as House bill. *Effective date.*—Property placed in service on or after January 1, 1987.

Item	Present Law	President's Proposal	House Bill	Senate Amendment
1. Tax credit for rehabilitation expenditures—Cont.				
c. Transition rules	No provision	Credits would be allowed with respect to pre-effective date expenditures if pre-effective date expenditures plus post-effective date expenditures qualify under test of a substantial rehabilitation.	(i) Credits would be available to buildings placed in service before January 1, 1994, if: (1) rehabilitation completed pursuant to a written contract that was binding on September 25, 1985, or (2) the building is acquired on or before September 25, 1985 (or subject to a binding contract as of that date to be acquired) and either Part 1 or 2 of the Historic Preservation Certification Application has been submitted to the Interior Department or its designate as of November 22, 1985, or the lesser of $1 million or 5 percent of rehabilitation's cost was incurred or required to be incurred pursuant to a binding contract entered into as of November 22, 1985, or the rehabilitation was completed pursuant to a written contract that was binding as of November 22, 1985. If a rehabilitation qualifies under (1) or (2), present law depreciation rules continue to apply (except full basis adjustment required for historic structures) and the credits are reduced from 15 percent to 10 percent, from 20 percent to 13 percent, or from 24 percent to 20 percent. (ii) Special transitional rules are provided for five projects.	(i) Same as House bill, except substitutes March 1, 1986 for September 25, 1985 and November 22, 1985. (ii) Special transitional rules are provided for 15 projects.

Item	Present Law			
2. Five-year amortization of expenditures to rehabilitate low-income housing (sec. 223 of the House bill)	Taxpayers may elect to amortize over a 60 month period certain qualifying expenditures for additions or improvements to low-income rental housing with a useful life of at least five years (other than hotels or other similar facilities primarily serving transients). Expenditures in any year for any dwelling unit are eligible only if the aggregate amount of expenditures for each unit exceeds $3,000 over two consecutive taxable years. Expenditures for any dwelling unit are not generally eligible to the extent that they aggregate more than $20,000 (in certain cases, $40,000). The election is scheduled to expire for expenditures incurred after December 31, 1986 (except in cases where rehabilitation began, or a binding contract for such expenditures was entered into, before January 1, 1987).	The election would be repealed. Expenditures for low-income housing would therefore be recovered in accordance with the applicable depreciation schedules. *Effective date.*—The repeal would be effective for expenditures paid or incurred on or after January 1, 1986.	Eliminates scheduled expiration and replaces $20,000 and $40,000 aggregate expenditure limits with a single $30,000 limit. *Effective date.*—The modification to the aggregate limit permits additional expenditures over the present $20,000 limit, in the case of expenditures paid or incurred on or after January 1, 1986 *Transitional rule.*—The $40,000 limit continues for expenses incurred (i) pursuant to a written contract that was binding as of September 25, 1985; or (ii) with respect to rehabilitation commenced as of September 25, 1985; if 5 percent of the cost has been incurred or committed by that date; provided in each case the additions or improvements are placed in service before January 1, 1988. It also continues in certain other circumstances	Provision expires in accordance with present law (However, see tax credit for low-income rental housing, item 3., below.)
3. Tax credit for low-income rental housing (sec. 1413 of the Senate amendment as modified by floor amendment by Sen. Mitchell, adopted by voice vote)	No low-income rental credit is provided but other special provisions are available: *Tax-exempt bond financing* Tax-exempt bonds may be used to finance multifamily rental housing if at least 20 percent (15% in targeted areas) of the housing units are occupied by individuals whose income does not exceed 80 percent of the area median income when they first occupy the unit. Proposed Treasury regulations require adjustments for family size in determining tenant income Multifamily rental housing bonds are exempt from volume caps and certain other requirements applicable to other IDBs. (See Part XII, below, for a discussion of rental housing bonds.)	No special provisions are available. *Tax-exempt bond financing* Tax-exempt bonds for multifamily rental housing would not be permitted.	No low-income rental housing credit is provided but other special provisions are available: *Tax-exempt bond financing* Tax-exempt bonds may be used to finance multifamily rental housing satisfying the following set-aside requirements on a continuous basis— (1) At least 25 percent of the housing units are occupied by persons whose income does not exceed 80 percent of the area median income, or (2) At least 20 percent of the housing units are occupied by persons whose income does not exceed 70 percent of the area median income. Multifamily rental housing bonds are subject to the new unified volume cap and other requirements applicable to nonessential function bonds.	As an alternative to tax-exempt bond financing and in lieu of preferential depreciation, five-year amortization, and special treatment of construction period interest and taxes, a new tax credit is provided that may be claimed by owners of residential rental projects providing low-income housing. The credit is claimed annually for a period of 10 years. The credit rate is set so that the annualized credit amounts have a present value of 60% or 30% of the basis attributable to qualifying low-income units, depending on the income of the tenants qualifying the unit for the credit. For projects on which construction commences prior to 1988, the annual credit rate is 8% (80% over 10 years) for units occupied by individuals with incomes of 50% or less of area median (as adjusted for family size) and 4% (40% over 10 years) for a maximum of 30% of the units occupied by individuals with incomes of between 50% and 70% of area median. For projects on which construction begins after 1987, Treasury is directed to adjust the credit rates to maintain the present values of the annualized credit amounts of 60% and 30%. Newly constructed buildings and newly acquired existing structures that are sub-

Item	Present Law	President's Proposal	House Bill	Senate Amendment
3. Tax credit for low-income rental housing (cont.)	*Depreciation* Low-income housing (generally, at least 85% of the units occupied by tenants with incomes of 80% or less of area median income) may be depreciated over 15 years using the 200% declining balance method; other housing is limited to a 19-year recovery period and the 175% declining balance method. (See A 1 b.xvi, above for depreciation provisions.)	*Depreciation* Buildings, including low-income housing, would be depreciated over 28 years using a method equivalent to 112 percent declining balance.	*Depreciation* Very low-income housing (at least 40% of the units occupied by tenants with incomes of 60% or less of area median income) may be depreciated over 20 years using the 200% declining balance method. Other low-income housing ((a) either at least 20% of the units occupied by tenants with incomes of 70% or less of area median income, or (b) at least 25% of the units occupied by tenants with incomes of 80% or less of area median income) may be depreciated over 30 years using the 200% declining balance method. Housing other than low-income housing is depreciated over 30 years using the straight-line method.	stantially rehabilitated are eligible for the credit. Substantial rehabilitation is defined as rehabilitation expenditures made over a two-year period (or five-year period in the case of rehabilitation conducted subject to a comprehensive plan) of at least 22.5% of the acquisition cost of the project (other than for the cost of land). The cost of rehabilitation and acquisition allocable to low-income units is eligible for the credit. Comparable to the treatment of multifamily rental housing bonds, there is no volume limitation or "trade-in" requirement for low-income housing credits.
	5-year amortization of rehabilitation expenditures Taxpayers may elect to amortize over a 60-month period certain qualifying expenditures for additions or improvements to low-income rental housing with a useful life of at least five years (other than hotels or other similar facilities primarily serving transients). Expenditures for any dwelling unit generally are not eligible to the extent that they aggregate more than $20,000 (in certain cases, $40,000). The election is scheduled to expire for expenditures incurred after December 31, 1986 (except in cases where rehabilitation began, or a binding contract for such expenditures was entered into, before January 1, 1987). (See item 2., above, for further details of 5-year amortization provisions.)	*5-year amortization of rehabilitation expenditures* The election would be repealed. Expenditures for low-income housing would be recovered in accordance with the applicable depreciation schedules.	*5-year amortization of rehabilitation expenditures* Eliminates scheduled expiration and replaces $20,000 and $40,000 aggregate expenditure limits with a single $30,000 limit.	*Definition of low-income housing* Low-income housing eligible for the credit is defined as follows: (i) At least 20 percent of the housing units in each project is occupied by individuals having incomes of less than 50 percent of the area median income. (ii) Income determinations are made with adjustments for family size. (iii) Qualification as a low-income tenant is determined on a continuing basis. (iv) The gross rent paid by families in units qualifying for the credit may not exceed 30% of the applicable qualifying income for a family of its size. *Restriction on tax-exempt financing* A project is not eligible for the credit if any part of the project is financed with obligations on which the interest is exempt from tax under Code section 103. This restriction applies as long as any of those obligations remain outstanding. A limited exception is made for certain existing federally assisted projects on which tax-exempt bonds remain outstanding. *Federally assisted housing* Unless otherwise specifically provided, projects receiving Federal grants, loans, or rental assistance are not eligible for the credit. A Federal guarantee does not constitute Federal assistance that would preclude a project from credit eligibility. (i) An exception to the Federal assistance restriction is provided for new construction or substantial rehabilitation of properties receiving assistance under the Urban Development Block Grant program, the Com-

Item	Present Law	President's Proposal	House Bill	Senate Amendment
3. Tax credit for low-income rental housing (cont.)				munity Development Block Grant program, and Housing Development or Rental Rehabilitation programs. Projects receiving assistance under these programs must exclude such assistance from the basis on which the low-income credit is allowable. (ii) Another exception is provided for new construction or substantial rehabilitation of properties receiving assistance under the HUD section 8 moderate rehabilitation program or the FmHA section 515 program. Projects receiving assistance under these programs, however, are only eligible for credits on units occupied by tenants with incomes of 50 percent or less of area median. Section 8 payments may not exceed certain specified amounts on all property eligible for the credit. (iii)(A) A final exception to the Federal assistance restriction is provided for newly acquired existing property receiving assistance under HUD's section 8, section 221(d)(3) or, section 236 programs, or FmHA's section 515 program. Such property must have 50 percent or more of the units occupied by tenants with incomes of 50 percent or less of area median income. All residential rental units in such projects are eligible to be included in the basis on which the credit is allowed. The credit rate is one-half the rate otherwise applicable to units occupied by tenants with incomes of 50 percent or less of area median income. Generally, a project eligible for this exception may not be placed in service within 15 years of its having last been placed in service, and section 8 payments may not exceed certain specified amounts on property eligible for the credit. (B) *Exception to substantial rehabilitation requirement.*—Existing property receiving assistance under HUD section 8, section 221(d)(3), section 236, or FmHA section 515 and described in (iii)(A), above, is excepted from the substantial rehabilitation requirement. (Generally, existing property (and the acquisition cost of existing property) is only eligible for the credit if substantial rehabilitation is performed after acquisition.) *At-risk limitation* The amount of the credit is subject to an at-risk limitation similar to the investment tax credit at risk rules in the case of nonrecourse financing.

Item	Present Law	President's Proposal	House Bill	Senate Amendment
3. Tax credit for low-income rental housing (cont.)				An exception is provided for certain lenders related to the buyer of the low income housing property. Another exception is provided for financing (including seller financing) not in excess of 60 percent of the basis of the property that is lent by charitable and social welfare organizations whose exempt purpose includes fostering low income housing. The credit is recaptured if the financing provided by such organizations is not repaid with interest by the end of the 15-year credit compliance period (described below). *Compliance requirements* Projects are required to comply with the low-income occupancy requirement for at least 15 years. Failure to meet the minimum low-income occupancy requirement during the 15-year period triggers a recapture of the credit. The credit is recaptured fully for violations during the first ten years, and recaptured partially for violations in years 11–15. Failure to meet the low-income occupancy requirement upon which the maximum credit is based (while still satisfying the minimum low-income occupancy requirement) results in a reduction of the credit for the year of the violation. *Transferability* Credits may be transferred to new purchasers of a project during the period for which the property is eligible to receive the credit, with the new purchaser "stepping into the shoes" of the seller, both as to credit percentage, basis, and liability for compliance and recapture. *Coordination with other provisions* The credit is subject to the rules of the general business credit, including the maximum amount of income tax liability that may be reduced by a general business tax credit in any year. Unused credits for any taxable year may be carried back to each of the three preceding taxable years and then carried forward to each of the 15 following taxable years. For purposes of the rules in the amendment limiting passive loss deductions, the credit (but not other losses from the project) is treated as arising from rental real estate activities in which the taxpayer actively

Item	Present Law	President's Proposal	House Bill	Senate Amendment
3. Tax credit for low-income rental housing (cont.)				participates, and is subject to the limitations imposed on tax credits from such activities. The basis with respect to which credits are allowed is reduced to reflect any rehabilitation credit for which the project is eligible. The basis of a project for depreciation is not reduced by the amount of low-income housing credits claimed. A more generous low-income housing credit is provided for one specific project (Columbia Point, Boston, Massachusetts). *Effective date.*—Effective for property placed in service after December 31, 1986.
F. Merchant Marine Capital Construction Fund (sec. 233 of the House bill)	Taxpayers are entitled to deduct certain amounts deposited in a capital construction fund. Earnings from the investment or reinvestment of amounts in a capital construction fund are excluded from income. A nonqualified withdrawal generates income to the taxpayer, subject to interest payable from the time the amount withdrawn was reported.	The rule providing special tax treatment for capital construction funds would be repealed. *Effective date.*—No tax-free contributions to capital construction funds could be made after December 31, 1985, except with respect to vessels the taxpayer owned on January 1, 1986, or vessels with respect to which the taxpayer performs a substantial amount of construction or reconstruction before January 1, 1986. Amounts remaining in a capital construction fund on January 1, 1996, would be treated as withdrawn at that time.	The rules providing special tax treatment for capital construction funds are retained, but modified to coordinate the application of the Internal Revenue Code with the Merchant Marine Act: the maximum rate of tax is imposed on nonqualified withdrawals, the Secretaries of Transportation and Commerce are required to make reports to the Secretary of Treasury regarding monies in funds. A taxpayer whose fund balance exceeds the amount appropriate for the vessel construction program that was determined when the fund was established must develop appropriate program objectives within 3 years or treat the excess as a nonqualified withdrawal. A ten-year limit is imposed on the amount of time monies can remain in a fund; monies not withdrawn after a ten-year period are treated as nonqualified withdrawals according to a schedule, beginning with 20 percent in the 11th year and ending with 100 percent in the 15th year. *Effective date.*—Taxable years beginning after December 31, 1985.	Same as present law.

Item	Present Law	President's Proposal	House Bill	Senate Amendment
A. Individual Capital Gains (sec. 241 of the House bill and secs. 401 and 402 of the Senate amendment)	An individual may deduct from gross income 60 percent of net capital gain (the excess of net long-term capital gain over any net short-term capital loss). Since the maximum regular individual tax rate is 50 percent, the deduction means that net capital gain is taxed at a maximum rate of 20 percent. The alternative minimum tax, which applies only if greater than the regular tax, is also 20 percent. Thus, although the deducted portion of capital gains is a preference item, the alternative minimum tax does not increase the maximum rate on net capital gain.	50 percent of an individual's net capital gain would be deductible. Since the highest regular tax rate for individuals would be 35 percent, the highest rate applicable to such net capital gain would be 17.5 percent. However, taxpayers subject to the alternative minimum tax would be potentially subject to a 20 percent rate on net capital gain. *Effective date.*—July 1, 1986. A taxpayer with a fiscal year that includes but does not begin on July 1, 1986 would use a blended percentage deduction for sales at any time during the year 1986.	42 percent (50 percent in 1986) of an individual's net capital gain is deductible. Since the highest regular rate for the individuals is 38 percent, the highest rate applicable to such net capital gain is 22.04 percent. The alternative minimum tax does not increase the maximum rate on net capital gain. *Effective date.*—Taxable years beginning after December 31, 1985.	The capital gains deduction is repealed. The maximum rate on long-term capital gains of individuals (including all long-term capital gains recognized at any time during calendar year 1987) will not exceed the maximum individual rates that become effective July 1, 1987. (See Part I. A. 1., above). *Effective date.*—Taxable years beginning after December 31, 1986. A targeted transition rule is provided.
B. Corporate Capital Gains (sec. 302 of the House bill)	An alternative tax rate of 28 percent applies to a corporation's net capital gain if the tax would be lower than the tax using the regular graduated rates.	Same as present law.	The alternative tax on corporate net capital gain is repealed. Thus, corporate net capital gain is taxed at regular corporate rates (i.e., a maximum of 36 percent). *Effective date.*—The change in the alternative tax for corporate capital gain generally applies to gain properly taken into account on or after January 1, 1986, unless pursuant to a sale that was made on or before September 25, 1985, or that was pursuant to a written binding contract in effect on that date.	Same as present law.
C. Incentive Stock Options (sec. 411 of the Senate amendment)	An employee is not taxed on the exercise of an incentive stock option and is entitled to capital gains when the stock is sold. In order for options to qualify as incentive stock options, among other requirements, the options must be exercisable in the order they are granted. Also, the employer may not in any one year grant the employee such options to acquire stock with a value (at the time the option is granted) of more than $100,000 (increased by certain carryover amounts).	No provision.	No provision.	The requirement that the options be exercisable in the order granted is repealed. The $100,000 limitation is modified so that an employer may not, in the aggregate, grant an employee incentive stock options that are first exercisable during any one calendar year to the extent the aggregate fair market value of the stock (at the time the options are granted) exceeds $100,000. *Effective date.*—Options issued after 1986.

*See also Part IV for certain agriculture, timber, energy and natural resources provisions.

Item	Present Law	President's Proposal	House Bill	Senate Amendment
. Straddles 1. Mark-to-market system (sec. 421 of the Senate amendment)	Section 1256 contracts (regulated futures contracts, certain listed options, and forward contracts traded in the interbank market) are marked to market at the close of the taxable year, with gain taxed as 60-percent long-term and 40-percent short-term for a maximum tax rate of 32 percent. The mark to market rules do not generally apply to hedging transactions, except in the case of certain syndicates.	No provision	No provision	Gains under the mark-to-market regime are taxed as 100 percent short-term capital gains (two-thirds short-term capital gains during 1987), for a maximum tax rate equal to the top individual rate. (See Part I. A 1., above). *Effective date.*—Positions established after December 31, 1986.
2. Year-end rule for qualified covered calls (sec. 422 of the Senate amendment)	A loss-deferral rule applies to a straddle consisting of stock offset by an option, subject to an exception for qualified covered call options. However, the qualified covered call exception is denied to a taxpayer who fails to hold stock for 30 days after the related call option is disposed of at a loss, where gain on sale of the stock is included in the subsequent year.	No provision.	No provision	The qualified covered call exception is denied, and the loss-deferral rule is thus applied, to cases in which it is the stock that is sold at a loss, and the related option that is not held for 30 days thereafter and the gain on which is included in the subsequent year This is the converse of the situation addressed under present law. *Effective date.*—Positions established after December 31, 1986
3. Hedging exception (sec. 423 of the Senate amendment)	Except in the case of certain syndicates, hedging transactions are not subject to either the mark to market rules or the year end loss deferral rules (described in items 1. and 2., above).	No provision	No provision.	The exceptions from the mark to market and loss deferral rules for certain hedging transactions are repealed for dealers, except for dealers in agricultural or horticultural commodities (other than trees which bear fruit or nuts). (Floor amendment by Sen Evans, adopted by voice vote) *Effective date*—Positions established after December 31, 1986

Item	Present Law	President's Proposal	House Bill	Senate Amendment
A. Agricultural Provisions 1. Special expensing provisions				
a. Soil and water conservation expenditures (sec. 922 of the House bill and sec. 701 of the Senate amendment)	(a) Certain expenditures incurred by farmers for soil and water conservation improvements may be expensed rather than capitalized. The deduction in each year may not exceed 25 percent of gross income derived from farming.	(a) Repealed. *Effective date.*—Expenditures after December 31, 1985.	(a) Retain provision, but limit it to improvements consistent with USDA (or State) soil or water conservation plans. *Effective date.*—Expenditures after December 31, 1985.	(a) Same as House bill. *Effective date.*—Expenditures after December 31, 1986.
b. Fertilizer and soil conditioning expenditures (sec. 921 of the House bill)	(b) Certain expenditures incurred for fertilizer and soil conditioning may be expensed rather than capitalized.	(b) Repealed. *Effective date.*—Expenditures after December 31, 1985.	(b) Repealed. *Effective date.*—Expenditures after December 31, 1985.	(b) No provision.
c. Land clearing expenditures (sec. 921 of the House bill and sec. 702 of the Senate amendment)	(c) Certain expenditures incurred by farmers for land clearing may be expensed rather than capitalized. The deduction in any year may not exceed the lesser of $5,000 or 25 percent of taxable income from farming.	(c) Repealed. *Effective date.*—Expenditures after December 31, 1985.	(c) Repealed. *Effective date.*—Expenditures after December 31, 1985.	(c) Same as House bill. *Effective date.*—Expenditures after December 31, 1985. (As modified by floor amendment by Senators Kassebaum and Boren, adopted by voice vote.)
2. Dispositions of converted wetlands and highly erodible croplands (sec. 923 of the House bill and sec. 703 of the Senate amendment)	Gain from the sale of real property used in a trade or business and held for more than 6 months is taxed as capital gain if gains on all sales of section 1231 assets (real property and depreciable personal property used in a trade or business and held for more than 6 months) during the year exceed losses on such sales. If losses on section 1231 assets exceed gains, the net loss is an ordinary loss.	No provision.	Provides that gain on the disposition of converted wetland or highly erodible cropland is treated as ordinary income, and any loss on the disposition of such property is treated as a long-term capital loss. *Effective date.*—Dispositions of land converted to farming use after December 31, 1985.	Same as House bill. *Effective date.*—Dispositions of land converted to farming use after March 1, 1986.
3. Preproductive period expenses of farmers				
a. In general (sec. 905 of the House bill and sec. 302 of the Senate amendment)	The Code and regulations provide exceptions from the otherwise applicable tax accounting rules for certain farmers. For example, certain farmers may elect to use the cash method of accounting when the accrual method otherwise would be required, and may use simplified inventory methods if an accrual method is adopted. Most farmers use the cash method of accounting, and therefore, do not capitalize preproductive period expenses.	In general, farmers would be subject to the uniform capitalization rules generally applicable to producers of property (see VIII.D., below) if the plant or animal produced had a preproductive period of 2 years or longer. *Effective date.*—Costs incurred after December 31, 1985.	Farmers (including growers of nursery stock and ornamental trees (but not timber (see B., below)) are subject to the uniform capitalization rules generally applicable to producers of property (see VIII D., below) if the plant or animal has a preproductive period of more than 2 years. However, certain farmers (in general, those not required to use the accrual method of accounting under present law and those not part of a farming syndicate) may elect to deduct currently preproductive period costs. Taxpayers making this election must recapture these costs as ordinary income on disposition of the product, and must use nonincentive depreciation on all farm assets placed in service in any year the election is in effect. *Effective date.*—Costs incurred after December 31, 1985.	Retains present law.

Item	Present Law	President's Proposal	House Bill	Senate Amendment
b. Expenses relating to grove, orchard, and vineyard crops (sec. 905 of the House bill and sec. 705 of the Senate amendment)	Costs incurred in planting, cultivating, maintaining, or developing citrus or almond groves before the end of the fourth taxable year after planting must be capitalized. Farming syndicates must capitalize planting and maintenance costs incurred with respect to other orchard or grove crops or vineyard crops until production of commercial quantities begins. However, if an orchard, grove, or vineyard is lost or damaged by reason of freezing temperatures, drought, disease, pests, or casualty, otherwise deductible replanting and maintenance costs are currently deductible if the taxpayer replants the same property	No provision	Replanting and maintenance costs incurred following loss of or damage to an orchard, grove, or vineyard of the taxpayer by reason of freezing temperatures, etc. are currently deductible even though replanting does not take place on the same property. Thus, costs incurred at a different location (although not in excess of the original acreage) but by the same taxpayer may qualify *Effective date.*—Costs incurred after December 31, 1985	The present-law rules allowing a deduction for costs incurred following loss or damage due to freezing temperatures, etc is extended to persons other than the person who owned the grove, orchard, or vineyard at the time of the loss or damage, provided (1) the taxpayer who owned the property at such time retains an equity interest of more than 50 percent in the property, and (2) the person claiming the deduction owns part of the remaining equity interest and materially participates in the replanting and maintenance of the property *Effective date*—Costs incurred after date of enactment.
4. Prepayments of farming expenses (sec. 704 of the Senate amendment)	Persons engaged in the trade or business of farming (not including timber growers) generally are permitted to use the cash method of accounting. However, farm syndicates are not allowed to deduct any amount paid for feed, seed or other supplies prior to the year in which such supplies are used or consumed	No provision.	No provision.	Farmers (not including timber growers) using the cash method of accounting may not deduct any amount paid for feed, seed, fertilizer or other supplies prior to the year in which supplies are used or consumed to the extent that more than 50 percent of the expenses incurred in the trade or business are prepaid *Effective date.*—Prepayments made on or after March 1, 1986.
5. Treatment of certain plant variety protection certificates as patents (sec. 925 of the House bill)	A sale or exchange of all substantial rights to a patent by the individual whose efforts created the patent generally produces long-term capital gain. The Department of Agriculture administers a program pursuant to the Plant Variety Protection Act which extends protection to developers of sexually propagated plant varieties similar to those provided to patent holders.	No provision	Provides that the term "patent" includes a plant variety protection certificate for purposes of the provision allowing capital gains treatment on certain dispositions of patents *Effective date*—Dispositions after December 31, 1985.	No provision
6. Recapture income on installment sales of farm irrigation equipment (sec. 313 of the Senate amendment)	In an installment sale of depreciable real or personal property, all depreciation recapture income under sections 1245 and 1250 is recognized in the taxable year of the disposition, whether or not principal payments are received in that year. Any gain in excess of the depreciation recapture income is taken into account under the installment method.	No provision	No provision	Depreciation recapture income resulting from an installment sale of equipment used to irrigate farmland is recognized under the rules in effect prior to the Deficit Reduction Act of 1984 Accordingly, any depreciation recapture with respect to such equipment is recognized as gain is recognized under the installment method rather than entirely in the year of sale

Item	Present Law	President's Proposal	House Bill	Senate Amendment
7. Discharge of indebtedness income for certain farmers (sec. 706 of the Senate amendment)	If a solvent taxpayer receives income from discharge of trade or business indebtedness, the taxpayer may exclude the income if an election to reduce basis in depreciable property is made. If the amount of the indebtedness forgiven exceeds the taxpayer's available basis, income must be recognized to the extent of the excess. If an insolvent taxpayer has discharge of indebtedness income, the taxpayer may exclude the income to the extent of his or her insolvency. The taxpayer's tax attributes (e.g., net operating loss and investment credit carryovers) and basis in property are reduced by the amount of the excluded income. However, the taxpayer's aggregate basis in his or her assets may not be reduced below the amount of the taxpayers remaining undischarged liabilities. If discharge of indebtedness income exceeds the taxpayer's available tax attributes and basis, tax on the excess is forgiven.	No provision.	No provision	Income arising from discharge of indebtedness owed by a farmer to an unrelated lender is treated as income realized by an insolvent taxpayer, if the debt was incurred to finance the production of agricultural products or is otherwise related to the farming business and is secured by farmland or farm assets. Thus, discharge of indebtedness income is forgiven after reduction of tax attributes and basis (including basis in farmland). (As modified by floor amendment by Senators Kassebaum and Boren, adopted by voice vote.) *Effective date.*—Discharges of indebtedness after April 9, 1986
8. Income averaging for agricultural producers (sec. 141 of the House bill and sec. 141A of the Senate amendment)	An eligible individual (i.e., one who has been self-supporting and a U.S. citizen or resident during the past three years) may elect to have a lower marginal rate apply to the portion of income that is more than 40 percent higher than his or her income for the prior three years	Income averaging would be repealed. *Effective date.*—Taxable years beginning on or after January 1, 1986.	Income averaging is repealed. *Effective date.*—Taxable years beginning on or after January 1, 1986.	Same as House bill, except *see* I.A.6., above, for an exception for farmers
9. Agricultural wages subject to FUTA (sec. 707 of the Senate amendment)	FUTA tax applies to wages of workers in agricultural operations having a quarterly payroll of at least $20,000 with 10 or more employees in 20 weeks of the year	No provision.	No provision.	*See*, XVII. D.4., for a special rule for FUTA treatment of wages paid in agricultural operations

Item	Present Law	President's Proposal	House Bill	Senate Amendment
B. Timber Provisions				
1. Preproductive period expenses of growing timber (sec. 911 of the House bill and sec. 302 of the Senate amendment)	Some costs of producing timber, such as planting costs and costs incurred before the seedlings are established, must be capitalized and recovered when the timber is sold. Most other costs generally may be deducted currently.	The uniform capitalization rules, including the interest capitalization rule (*see*. VIII D., below), would apply to timber. Thus, all costs of planting and growing timber would be accumulated and deducted when the timber is sold. *Effective date.*—Growing costs attributable to timber planted before 1986 would be subject to capitalization under a 10-year phase-in rule (10 percent of such costs incurred in 1986 would have to be capitalized, 20 percent in 1987, etc.).	Same as President's proposal, except qualified small timber producers (taxpayers with 75,000 acres or less) may elect to amortize costs otherwise required to be capitalized as a result of the bill over a period of 5 years. The benefit of the election is phased out at a rate of 4 percent for each 1,000 acres (or part thereof) of timberland in excess of 50,000 acres. Taxpayers making the election are required to use non-incentive depreciation for assets used in the timber business which are placed in service while an election is in effect. *Effective date.*—Costs incurred after December 31, 1985. The capitalization of costs attributable to timber planted before 1986 is phased in over a 5-year period.	Retains present law for producers of timber
2. Reforestation expenses (secs. 211 and 911 of the House bill)	Taxpayers may amortize over a 7-year period up to $10,000 of reforestation expenditures incurred in each taxable year. A 10-percent tax credit is allowable for these expenditures.	The 7-year amortization and tax credit provisions would be repealed. *Effective date.*—Expenditures after December 31, 1985.	Same as President's proposal. *Effective date.*—Expenditures after December 31, 1985	Retains present law
3. Capital gains for timber (sec. 912 of the House bill)	Timber royalty income qualifies for capital gain treatment, where the timber is held for 6 months before being cut. Owners of timber (or a right to cut timber) may elect to treat the cutting of timber as a sale or exchange qualifying for capital gains treatment. To qualify, the timber (or contract cutting right) must be held for 6 months prior to cutting.	Capital gains treatment would be phased out over a 3-year period beginning January 1, 1986. *Effective date.*—For individuals, the exclusion rate on capital gains from timber would be reduced to 30% in 1986, 20% in 1987, 10% in 1988 and 0 percent thereafter. For corporations, the tax rate would increase to 30% in 1986, 31% in 1987, 32% in 1988, and such gains would be taxed at ordinary corporate rates thereafter.	(a) Repeals capital gains treatment for timber on Federal lands, effective January 1, 1986. (b) Repeals capital gain treatment for ornamental trees, effective January 1, 1986. (c) An alternative corporate tax rate of 30% in 1986, 31% in 1987, and 32% in 1988 is provided for capital gains on timber. Such gains are taxed at ordinary capital rates thereafter (36% under the House bill).	Retains present law. However, the changes made to the individual capital gains rules (*see* III A.) also apply to capital gains for timber.

Item	Present Law	President's Proposal	House Bill	Senate Amendment
. Oil, Gas and Geothermal Properties 1. Intangible drilling costs (sec. 251 of the House bill and sec. 715 of the Senate amendment)				
a. General rule	(a) Intangible drilling and development costs (IDCs) generally may be expensed or capitalized at the election of the operator of an oil, gas, or geothermal property. In the case of integrated producers, 80% of IDCs may be expensed and the remaining 20% must be amortized over a 36-month period beginning with the month the costs are paid or incurred. Costs with respect to a nonproductive well ("dry hole") may be deducted currently by any taxpayer in the year the dry hole is completed.	(a) Retain present law.	(a) Retains present law, including rules for integrated producers, with respect to domestic IDCs incurred prior to commencement of the installation of the production string of casing ("casing point"). IDCs incurred at, or subsequent to, the casing point are to be amortized over a 26-month period, beginning in the month paid on incurred. These costs are not subject to the 20 percent reduction for integrated producers. As under present law, unrecovered IDCs with respect to a dry hole can be deducted in the year the dry hole is completed. *Effective date.*—Costs paid or incurred after December 31, 1985.	(a) Retains present law.
b. Treatment of foreign IDCs	(b) IDCs qualify for expensing whether incurred in the United States or in a foreign country.	(b) Retain present law.	(b) IDCs incurred outside of the United States are recovered (i) over a 10-year, straight-line amortization schedule, or (ii) at the election of the operator, as part of the basis for cost depletion. *Effective date.*—Costs paid or incurred after December 31, 1985.	(b) Same as House bill. *Effective date.*—Costs paid or incurred after December 31, 1986 (other than with respect to certain licenses for North Sea development).

Item	Present Law	President's Proposal	House Bill	Senate Amendment
2. Depletion for oil, gas, and geothermal properties (secs. 252–254 of the House bill)				
a. General rule	(a) Depletable costs with respect to oil and gas properties must be recovered using whichever of two methods provides the higher deduction: cost depletion or percentage depletion. Under cost depletion, the fraction of depletable costs recovered is equal to the ratio of hydrocarbons produced during the taxable year to total remaining reserves. Under percentage depletion, 15% of the taxpayer's gross income is allowed as a deduction in any taxable year, not to exceed (i) 50% of net income for the property, or (ii) 65% of overall taxable income. Percentage depletion for oil and gas properties is limited to independent producers and royalty owners for up to a daily production of 1,000 barrels of crude oil or the equivalent production of natural gas. Geothermal properties are treated similarly to oil and gas wells, but are not subject to the 65% or 1,000 barrels per day rules.	(a) Phase out percentage depletion for most oil, gas, and geothermal properties over a 5-year period, by reducing depletion rate 3 percentage points in each year. Percentage depletion would be retained for oil and gas stripper wells owned by independent producers, but would not be available to royalty owners. The basis for cost depletion would be indexed for inflation. *Effective date.*—Production after December 31, 1985.	(a) Same as President's proposal, except that it phases out percentage depletion for oil, gas, and geothermal properties over a 3-year period, by reducing depletion rates 5 percentage points in each year. Also, percentage depletion is retained for oil and gas stripper wells owned by both independent producers and royalty owners. Cost depletion is not indexed. *Effective date.*—Production after December 31, 1985	(a) Retains present law
b. Treatment of bonuses and advance royalties	(b) Percentage depletion is available with respect to oil and gas lease bonus or advance royalty payments.	(b) No provision	(b) Denies percentage depletion for lease bonuses, advance royalty payments, or other payments made without regard to actual production from an oil, gas, or geothermal property. *Effective date.*—January 1, 1986	(b) Retains present law.
3. Gain on disposition of interests in oil, gas or geothermal property (sec. 213 of the House bill)	Expensed intangible drilling costs incurred after 1975 are recaptured as ordinary income to the extent of the excess of such costs over the amount that would have been deducted if the costs had been capitalized and deducted through depletion.	All gain would be treated as ordinary income	Expensed intangible drilling costs and depletion which reduced basis are recaptured as ordinary income. *Effective date.*—Dispositions of property placed in service after December 31, 1985, unless acquired pursuant to a written contract binding on September 25, 1985	Retains present law
4. Windfall profit tax exemption for certain exchanges of crude oil (sec. 255 of the House bill)	An excise tax (the crude oil windfall profit tax) is imposed on domestic crude oil when it is removed from the production premises. The tax does not apply if crude oil is used to power production equipment on the same property.	No provision	An exemption is provided for certain otherwise taxable crude oil which is exchanged for an equal amount of residual fuel oil, to be used in enhanced recovery processes on the producing property. Only crude oil attributable to an operating mineral interest qualifies for the exception. No depletion deduction (including cost or percentage depletion) is allowed with respect to crude oil qualifying for the exception. *Effective date.*—Residual fuel oil used, and crude oil removed, after the date of enactment.	Retains present law

Item	Present Law	President's Proposal	House Bill	Senate Amendment
D. Hard Minerals **1. Exploration and development costs (sec. 262 of the House bill and sec. 716 of the Senate amendment)**				
a. General rule	(a) Exploration and development costs associated with mines and other hard mineral deposits may be deducted currently at the election of the taxpayer. Exploration (but not development) costs which have been deducted currently either (1) are applied to reduce depletion deductions, or (2) at the taxpayer's election, are recaptured in income once the mine begins production, and then recovered as a depletable expense. In the case of corporations, only 80% of hard mineral exploration and development costs may be expensed. The remaining 20% must be recovered over the 5-year ACRS depreciation schedule (beginning in the year that exploration and development costs are paid or incurred), with an investment tax credit for domestic costs.	(a) Retains present law	(a) Same as present law, but requires recapture of both expensed development and exploration costs at the time the mine begins production. Recaptured amounts, and development costs incurred after the mine begins production, are recovered in the same manner as depreciable property in Class 1 (3-year recovery period). The 20 percent of corporate exploration and development costs that is expensed is recovered in the same manner as depreciable property in Class 2 (5-year recovery period), beginning in the year that costs are paid or incurred. *Effective date.*—Costs paid or incurred after December 31, 1985.	(a) Retains present law
b. Foreign exploration costs	(b) Foreign exploration costs must be capitalized to the extent the taxpayer's foreign and domestic exploration costs exceed $400,000	(b) Retains present law	(b) Foreign exploration and development costs are recovered (i) over a 10-year, straight-line amortization schedule, or (ii) at the election of the taxpayer, as part of the basis for cost depletion. *Effective date.*—Cost paid or incurred after December 31, 1985.	(b) Same as House bill. *Effective date.*—Costs paid or incurred after December 31, 1986
2. Percentage depletion of hard mineral deposits (sec. 261 of the House bill)	Depletable costs with respect to hard mineral deposits must be recovered using the greater of— (i) cost depletion, or (ii) percentage depletion at the applicable statutory rate for the mineral. Percentage depletion may not exceed 50% of net income from the property in any taxable year. For corporations only, percentage depletion of coal or iron ore, in excess of adjusted basis (determined without regard to the depletion deduction for that year), is reduced by 15 percent.	Phases out percentage depletion of hard minerals ratably over a 5-year period. The basis for cost depletion of hard minerals would be indexed for inflation. *Effective date.*—Production after December 31, 1985.	With the exceptions below, mineral depletion rates are phased down ratably to 5 percent in 1988. Minerals having a 5-percent present-law rate (e.g., sand, gravel, and certain clay) are phased down ratably to 0 in 1988. In conjunction with these changes, the 50 percent of net income limitation is phased down ratably to 25 percent. Present law depletion (rate and net income limitation) is retained for (i) minerals used to produce fertilizer or animal feed ("agricultural minerals"), and (ii) dimension stone. *Effective date.*—Production after December 31, 1985.	Retains present law

Item	Present Law	President's Proposal	House Bill	Senate Amendment
3. Gain on disposition of interest in mining property (sec. 262 of the House bill)	Adjusted exploration expenditures (generally amounts expensed in excess of amounts which would have been deducted if the costs had been capitalized) are recaptured as ordinary income.	All gain would be treated as ordinary income	Expensed exploration and development expenses and depletion which reduced basis are recaptured as ordinary income. *Effective date.*—Dispositions of property placed in service after December 31, 1985, unless acquired pursuant to a written contract binding on September 25, 1985.	Retains present law
4. Royalty income from coal and domestic iron ore (sec. 242 of the House bill)	Royalties on dispositions of coal and domestic iron ore qualify for capital gain treatment, provided the coal or iron ore is held for more than six months before mining. Capital gain treatment does not apply to (i) income realized as a co-adventurer, partner, or principal in the mining of coal or iron ore, or (ii) certain related party transactions. If capital gain treatment applies, the royalty owner is not entitled to percentage depletion with respect to the same coal or iron ore.	Phase out capital gain treatment over a 3-year period beginning January 1, 1986 *Effective date.*—For individuals, the exclusion rate on capital gains from coal and domestic iron ore royalties would be reduced to 30% in 1986, 20% in 1987, 10% in 1988, and 0 percent thereafter. For corporations, the tax rate on such capital gains would increase to 30% in 1986, 31% in 1987, 32% in 1988, and would be taxed at ordinary corporate rates thereafter (33% under the proposal).	Same as President's proposal. *Effective date.*—For individuals, the exclusion rate on capital gains from coal and domestic iron ore royalties is reduced to 30% in 1986, 20% in 1987, 10% in 1988, and 0 percent thereafter. For corporations, the tax rate on such capital gains increases to 30% in 1986, 31% in 1987, 32% in 1988, and is taxed at ordinary corporate rates thereafter (36% under the House bill).	Retains present law However, the changes made to the individual capital gains rules (sec III A) also apply to capital gain royalty income
E. Energy-Related Tax Credits and Other Incentives				
1. Residential renewable energy tax credit (sec. 271 of the House bill)	A 40-percent tax credit was allowed on the first $10,000 spent through 1985 for renewable energy property, i e., solar, wind and geothermal ($4,000 maximum credit). Unused credits may be carried over through 1987 Eligible equipment and parts included those necessary to transmit or use geothermal energy.	Would retain present law, i.e., credits expired after 1985.	The solar energy tax credit is extended for three years at reduced credit rates—30% in 1986 and 20% in 1987 and 1988 Expenditures for solar hot water property are limited to $5,000 The credit is not to be used to create a sun room, greenhouse, or similar structure.	Same as President's proposal

Item	Present Law	President's Proposal	House Bill	Senate Amendment
2. Business energy tax credits (sec. 272 of the House bill and sec. 711 of the Senate amendment)				
a. Credit allowed	(a) The business energy tax credits were available in addition to the investment tax credit *Solar, wind, geothermal and ocean thermal property:* 15-percent credit through 1985. *Intercity buses and biomass property:* 10-percent credit through 1985. *Small-scale hydroelectric projects:* 11-percent credit through 1985.	Would retain present law, i.e., credits expired after 1985.	(a)(1) Extends solar energy credit rate at 15% in 1986, 12% in 1987 and 8% in 1988 (2) Extends geothermal energy credit rate at 15% in 1987 and 10% in 1987 and 1988 (3) Retains 1985 expiration for ocean thermal property (4) Retains 1985 expiration for wind and biomass property (5) Retains 1985 expiration for buses and small-scale hydroelectric projects	(a)(1) Extends solar energy credit rate at 15% in 1986 and 12% in 1987 and 1988 (2) Same as House bill. (3) Extends ocean thermal energy credit rate at 15% in 1986-1988 (4) Extends wind and biomass energy credit rates at 15% in 1986 and at 10% in 1987 (5) Same as House bill
b. Extension of energy tax credit for chlor-alkali electrolytic cells (sec. 711 of Senate amendment)	(b) Modifications to chlor-alkali electrolytic cells (an item of specially defined energy property in I.R.C. sec. 48(l)(5)(M)) was eligible for the 10 percent energy tax credit through 1982.	(b) No provision.	(b) No provision	(b) The expiration date (in Code sec 46(b)(2)(A)(vii)) is changed to December 31, 1983
c. Affirmative commitment rules	(c) The expired 10-percent credit for certain alternative energy property continues to be available for long-term projects which meet rules requiring (1) completion of engineering studies and application for all required permits before 1983, (2) binding contracts for 50% of special project equipment before 1986, and (3) project completion before 1991. The 11-percent credit for small-scale hydroelectric projects is available through 1988 for projects which had been docketed by the Federal Energy Regulatory Commission before 1986	(c) Present law affirmative commitment rules (including hydroelectric) would be retained	(c) Consistent with the general transitional rules applicable to repeal of the general ITC, (1) allowable energy credits are spread ratably over 5 years (i.e., 20% of the credit in each of 5 years), and (2) a full basis adjustment is required for the full energy tax credit in the first taxable year.	(c) Same as President's proposal

Item	Present Law	President's Proposal	House Bill	Senate Amendment
3. Credit for fuels from nonconventional sources (sec. 273 of the House bill.)	A tax credit is provided for the domestic production and sale of specific fuels from nonconventional sources. The credit applies to eligible fuels sold after December 31, 1979, and before January 1, 2001, produced from: (1) facilities placed in service after December 31, 1979, and before January 1, 1990, or (2) wells drilled after December 31, 1979, and before January 1, 1990, on properties which first began production after December 31, 1979.	The credit generally would be terminated after December 31, 1985. Under a transitional provision, the credit would continue to be available for qualifying fuel which is produced from a well drilled, or facility completed, before January 1, 1986, and which is sold before January 1, 1990	Terminates credit after December 31, 1985, except continues credit for methane gas produced from wood in facilities placed in service before January 1, 1989, and sold before January 1, 2001	Retains present law
4. Alcohol fuels credit and tax exemptions; import duty (secs. 274–275 of the House bill and secs. 713–714 of the Senate amendment)				
a. Alcohol fuels income tax credit and excise tax exemption	(a)(1) A 60-cents-per-gallon (equivalent to $25.20 per barrel of alcohol) credit is allowed for alcohol mixed with gasoline, diesel fuel, or any special motor fuel, if the mixture is sold or used as fuel. The credit also is provided for alcohol used in a trade or business or sold at retail and placed in a vehicle fuel tank. Eligible alcohol includes ethanol and methanol but not if made from petroleum, natural gas, or coal (including peat), or alcohol less than 150 proof. Expires after 1992.	(a)(1) After December 31, 1985, the alcohol fuels tax credit would be available only for alcohol fuels produced from facilities completed before January 1, 1986, and sold before January 1, 1993.	(a)(1) The 60-cents-per-gallon income tax credit is repealed after December 31, 1985.	(a)(1) Retains present law (Floor amendment by Senator Roth, adopted by voice vote.)
	(2) An alternative 6-cents-per-gallon (equivalent to $25.20 per barrel of alcohol) exemption from excise taxes on gasoline, diesel fuel, and special motor fuels is provided for these fuels if they are mixed with at least 10 percent alcohol. Eligible alcohol may not be derived from petroleum, natural gas, or coal.	(2) Would repeal excise tax exemption after 1985.	(2) Retains present law.	(2) Same as House bill (retains present law)
b. Duty on imported alcohol fuels	(b) A 60-cents-per-gallon (equivalent to $25.20 per barrel of alcohol) duty is imposed on alcohol imported into the United States for use as a fuel. Expires after 1992.	(b) The present-law duty on alcohol imported for use as a fuel would be retained	(b) Same as President's proposal	(b) Same as President's proposal and House bill, except allows duty-free entry into the United States only for ethyl alcohol produced in a CBI country or insular possession from source material which is the product of a CBI country, insular possession, Israel free-trade area, or the United States. The change in the source material requirement would not apply, as of January 1, 1986, to certain facilities which were either established and operating (up to a maximum of 20 million gallons per year) or ready for shipment to and installation in a CBI country (up to a maximum of 50 million gallons per year)

Item	Present Law	President's Proposal	House Bill	Senate Amendment
5. Neat alcohol fuels (sec. 275 of the House bill and sec. 712 of the Senate amendment)	A 9-cents-per-gallon (equivalent to $4.45 per barrel of alcohol) exemption from the excise tax on special motor fuels is provided for neat methanol and ethanol fuels which are not derived from petroleum or natural gas. A 4½ cents exemption (equivalent to $2.23 per barrel) is provided if the fuels are derived from natural gas. Neat alcohol fuels are at least 85 percent methanol, ethanol, and other alcohol. Expires after 1992.	The excise tax exemptions would be repealed after 1985.	The 9-cents-per-gallon exemption is reduced to 6-cents-per-gallon (equivalent to $2.96 per barrel), effective after December 31, 1985.	Same as House bill, except effective after December 31, 1986.
6. Taxicab fuels tax exemption (sec. 275 of the House bill)	A 4-cents-per-gallon partial exemption from the motor fuels taxes (9 cents for gasoline and special motor fuels and 15 cents for diesel fuel) was provided for fuels used in qualifying taxicabs (through Sept. 30, 1985). The exemption was effectuated through a credit or refund (without interest).	No provision.	The 4-cents-per-gallon motor fuels tax exemption for taxicabs is extended for the period from October 1, 1985, through September 30, 1988 (the current expiration date for all Highway Trust Fund excise taxes).	Retains present law (allows exemption to expire).

Item	Present Law	President's Proposal	House Bill	Senate Amendment
A. At-Risk Rules (sec. 401 of the House bill and sec. 1411 of the Senate amendment)	The loss limitation at-risk rules limit the losses in excess of income with respect to an activity, which individuals and closely held corporations may deduct, to the amount the taxpayer has actually invested in the activity, including borrowed amounts to the extent the taxpayer is personally liable to repay or has pledged other non-financed property (except property used in the activity) as security, and has not borrowed the funds from a person with an interest in the activity other than as a creditor. The investment tax credit at-risk rules limit the credit base of property in an activity that is subject to the loss limitation at-risk rules, and generally provide that nonrecourse debt is treated as an amount at risk for investment credit purposes where (1) it is borrowed from an unrelated commercial lender, (2) the property is acquired from an unrelated person, (3) the lender is unrelated to the seller, and (4) the nonrecourse debt does not exceed 80 percent of the credit base of the property The at-risk rules apply to all activities except the holding of real estate.	Applies the at-risk rules to real estate activities *Effective date.*—Property acquired after December 31, 1985.	The bill applies the at-risk rules to real estate activities, but with an exception for real estate losses providing that third party nonrecourse debt borrowed from an unrelated commercial lender is treated as at risk under rules similar to the present-law credit at-risk rules (without the requirement limiting the nonrecourse debt to 80 percent). *Effective date.*—Property acquired after December 31, 1985.	Same as the House bill, except the third party nonrecourse debt exception for real estate losses applies notwithstanding that (1) the lender is related to the taxpayer, and (2) the taxpayer acquired the property from a related party. (See also low-income housing credit at-risk rules, Part II E 3 above.) *Effective date*—Property acquired after December 31, 1986 One transitional rule is provided
B. Limitations on Losses and Credits from Passive Activities (sec. 1401 of the Senate amendment)	Generally, present law does not limit the use of deductions or credits from a particular business activity to offset income from other activities, except in certain specific instances (e g., the limitation on the deduction of net capital losses, and the rule that research and development credits cannot offset unrelated income in the case of an individual).	No provision.	No provision.	(a) *General rule.*— Deductions in excess of income (i.e losses) from passive trade or business activities generally may not offset other income such as salary, interest, dividends, and active business income. Deductions from passive activities may offset income from passive activities. Credits from passive activities generally are limited to the tax attributable to income from passive activities Disallowed losses and credits are carried forward and treated as deductions and credits from passive activities in the next taxable year Disallowed losses from an activity are allowed in full when the taxpayer disposes of his entire interest in the activity in a taxable transaction Credits are not so allowed upon disposition

Item	Present Law	President's Proposal	House Bill	Senate Amendment
B. Limitations on Losses and Credits from Passive Activities (sec. 1401 of the Senate amendment.) (Cont.)				Applies to individuals, estates, trusts, and personal service corporations. Closely held corporations may not offset portfolio income with passive losses and credits but may use passive losses and credits to offset active business income. (b) *Definition of passive activities*.— Passive activities include (1) trade or business activities in which the taxpayer (or spouse) does not materially participate (i.e., is not involved on a regular, continuous, and substantial basis), and (2) rental activities where payments are primarily for the use of tangible property. Passive activities do not include working interests in oil and gas properties in which the taxpayer's form of ownership does not limit liability. (c) *Rental real estate*.— In the case of rental real estate activities in which an individual actively participates, up to $25,000 of losses (and credits in a deduction-equivalent sense) from all such activities are allowed each year against non-passive income of the taxpayer. The $25,000 amount is phased out ratably between $100,000 and $150,000 of adjusted gross income (determined without regard to passive losses). Low-income housing credits may be taken under the $25,000 allowance (in a deduction-equivalent sense) against non-passive income without regard to whether the individual actively participates. *Effective date*.—Taxable years beginning after December 31, 1986, with a phase-in rule. Investments made before date of enactment become subject to disallowance 35 percent in taxable years beginning in 1987, 60 percent in taxable years beginning in 1988, 80 percent in taxable years beginning in 1989, and 90 percent in taxable years beginning in 1990, and 100 percent in taxable years beginning after 1990. (Floor amendment by Senator Mitchell, adopted by voice vote, limited phase-in rule to investments made prior to date of enactment.)

Item	Present Law	President's Proposal	House Bill	Senate Amendment
C. Nonbusiness Interest Limits (sec. 402 of the House bill and sec. 1421 of the Senate amendment)				
1. General limitation	The deduction for investment interest of noncorporate taxpayers is limited to the sum of $10,000, plus net investment income, plus certain deductible expenditures in excess of rental income from net lease property. Other nonbusiness interest and business interest generally is not subject to limitation. Interest deductions not allowed due to this limitation carry over to future years.	(a) The deduction for all nonbusiness interest of noncorporate taxpayers would be limited to the sum of $5,000, plus net investment income, plus certain deductible expenditures in excess of rental income from net lease property. (b) Interest on debt secured by the taxpayer's principal residence to the extent of its fair market value would not be subject to the limitation (c) No provision	(a) The deduction for nonbusiness interest of noncorporate taxpayers is limited to $10,000 ($20,000 for joint returns), plus net investment income, plus certain deductible expenditures in excess of rental income from net lease property. (b) Interest on debt secured by the taxpayer's principal residence and a second residence of the taxpayer (to the extent of their fair market value) is not subject to limitation. (c) A residential lot is treated as a residence and up to 6 weeks of time-sharing of residential properties is treated as one residence.	(a) The deduction for investment interest of noncorporate taxpayers is limited to net investment income plus certain deductible expenditures in excess of rental income from net lease property Consumer interest is not deductible (b) Same as House bill. (c) No provision
2. Definition of interest subject to limitation	Investment interest means interest on debt to purchase or carry investment property.	(a) Nonbusiness interest means all interest not incurred in a trade or business of the taxpayer, including the taxpayer's share of interest of S corporations in whose management he does not actively participate, and the taxpayer's share of interest expense of limited partnerships in which he is a limited partner. (b) No provision.	(a) Nonbusiness interest means all interest not incurred in the taxpayer's trade or business, including the taxpayer's share of interest of S corporations in whose management he does not actively participate, the taxpayer's share of interest expense of limited partnerships in which he is a limited partner, and the taxpayer's share of interest expense of certain trusts and other entities in which he is a limited entrepreneur (b) Interest expense attributable to low-income housing which is (i) very low income housing, (ii) certain bond-financed low-income housing, or (iii) housing eligible for 5-year amortization of rehabilitation expenses under present law, is not subject to the limitation.	(a) Investment interest (in conformity with the passive loss rule) includes all interest subject to limitation in the House bill as well as other interest attributable to an activity in which the taxpayer does not materially participate (or in the case of rental real estate activities, does not actively participate). Consumer interest means interest not attributable to a trade or business or an activity engaged in for profit (b) No provision

Item	Present Law	President's Proposal	House Bill	Senate Amendment
3. Investment income defined	(a) Net investment income means investment income net of investment expense. Investment income means interest, dividends, rents, royalties, short-term capital gain from disposition of investment property and depreciation recapture not from conduct of a trade or business. (b) Investment expense means deductible investment expenses (other than interest), except that straight-line (not accelerated) depreciation over useful life, and cost (not percentage) depletion are used in calculating investment expenses.	(a) Investment income would be expanded to include the same income items as present law plus the taxpayer's share of income from investments, interest from which would be investment interest under the proposal (item 2, above). (b) Investment expense would be determined the same as under present law except that the Treasury report RCRS depreciation schedule would be substituted for present-law straight-line depreciation.	(a) Investment income is expanded to include the same income items as under present law plus the taxable portion of net gain from the disposition of investment property, plus income from investments, interest from which would be investment interest under the provision (item 2 above). (b) Investment expense includes the depreciation and depletion the taxpayer actually utilized.	(a) Same as House bill. (b) Same as House bill.
4. Net leases	Property subject to a net lease is treated as an investment, unless the trade or business deductions exceed 15 percent of the rental income.	Retain present law.	Provides that, to the extent the taxpayer performs personal services in lieu of incurring deductible expenses with respect to leased property in certain circumstances, the value of such services may be included with the actual trade or business deductions in determining whether such deductions exceed 15 percent of the rental income.	Same as House bill.
5. Effective date		Subject to two phase-in rules, the limitation would be effective for interest paid or incurred in taxable years beginning on or after January 1, 1986, regardless of when the obligation was incurred. The first phase-in rule is that the $10,000 limit under present law would be reduced to $5,000 for taxable years beginning on or after January 1, 1988. The second phase-in rule is that interest not subject to the limitation under present law, but which would be subject to the expanded limitation, would become subject to the limitation ratably (10 percent per year) over 10 years commencing with taxable years beginning in 1986.	Taxable years beginning after December 31, 1985, with a phase-in rule. Interest not disallowed under present law, but which is disallowed under the new provision, becomes subject to disallowance ratably (10 percent per year) over 10 years commencing with taxable years beginning in 1986.	Taxable years beginning after December 31, 1986, with a phase-in rule. Interest not disallowed under present law, but which is disallowed under the new provision, becomes subject to disallowance 35 percent in taxable years beginning in 1987, 60 percent in taxable years beginning in 1988, 80 percent in taxable years beginning in 1989, 90 percent in taxable years beginning in 1990, and 100 percent in taxable years beginning after 1990.

Item	Present Law	President's Proposal	House Bill	Senate Amendment
A. Corporate Tax Rates (sec. 301 of the House bill and sec. 601 of the Senate amendment)	Corporate taxable income is subject to tax under a 5-bracket graduated rate structure as follows *Taxable Income* — *Rate* $25,000 or less .... 15 $25,000-$50,000 .... 18 $50,000-$75,000 .... 30 $75,000-$100,000 .... 40 Over $100,000 .... 46 An additional 5 percent tax is imposed on a corporation's taxable income in excess of $1 million, up to a total additional tax of $20,250. This results in elimination of the benefit of the graduated rate structure (in effect, payment of tax at a flat 46 percent rate) for corporations having taxable income of $1,405,000 or more.	Corporate income would be subject to tax under a 4-bracket graduated rate structure as follows *Taxable Income* — *Rate* $25,000 or less .... 15 $25,000-$50,000 .... 18 $50,000-$75,000 .... 25 Over $75,000 .... 33 The graduated rates would be phased out for corporations with taxable income in excess of $140,000 by imposing an additional 5-percent tax on income between $140,000 and $345,000. Thus, corporations having taxable income of $345,000 or more would, in effect, pay tax at a flat 33 percent rate. *Effective date.*—July 1, 1986 (income in taxable years that include July 1, 1986, would be subject to "blended" rates).	Corporate income is subject to tax under a 3-bracket graduated rate structure as follows *Taxable income* — *Rate* $50,000 or less .... 15 $50,000-$75,000 .... 25 Over $75,000 .... 36 An additional 5-percent tax is imposed on income between $100,000 and $365,000. Thus, corporations having taxable income of $365,000 or more in effect pay tax at a flat 36 percent rate. *Effective date.*—July 1, 1986 (income in taxable years that include July 1, 1986, is subject to blended rates).	Same as House bill, except maximum corporate rate is 33 percent. Thus, corporate income is subject to tax under a 3-bracket graduated rate structure as follows: *Taxable Income* — *Rate* $50,000 or less .... 15 $50,000-$75,000 .... 25 Over $75,000 .... 33 An additional 5-percent tax is imposed on income between $100,000 and $320,000. Thus, corporations having taxable income of $320,000 or more in effect pay tax at a flat 33 percent rate. *Effective date.*—July 1, 1987 (income in taxable years that include July 1, 1987, is subject to blended rates).
B. Corporate Dividends Paid Deduction (secs. 311 and 312 of the House bill)	Corporations generally compute taxable income and are subject to a separate corporate-level tax without deduction for dividends paid to shareholders. Foreign shareholders of U.S corporations generally are subject to 30-percent withholding tax on dividends; a lower rate may be provided by treaty. Tax-exempt entities generally are not taxable on dividends received, except in certain cases where the tax-exempt entity owns debt-financed property	Domestic corporations would receive a deduction for 10 percent of dividends paid out of corporate earnings that have been subject to tax after the general effective date of the provision. An additional compensatory withholding tax equal to the tax benefit received from the deduction would be imposed on foreign shareholders not protected by treaty. No special rules would be provided for dividends paid to tax-exempt shareholders. The dividends received deduction for corporations would be modified in connection with the dividends paid deduction. (See item C, below.) *Effective date.*—Generally, taxable years beginning after December 31, 1986, with special rule for dividends paid after that date in taxable years beginning before January 1, 1987.	A domestic corporation receives a deduction for 10 percent of dividends paid by the corporation out of earnings taxed after the general effective date of the provision. A foreign corporation, at least half of whose income is from a U.S business (and thus generally subject to U.S. tax) also receives a deduction. A compensatory withholding tax is imposed on foreign shareholders, including those otherwise protected by treaty, except where the foreign country grants equivalent relief from a two-tier tax to U.S. shareholders. The deductible portion of dividends paid to tax-exempt shareholders owning 5 percent or more of the distributing corporation's stock is treated as taxable unrelated business income of the shareholder In connection with the dividends-paid deduction, the dividends received deduction is reduced (See item C, below.) *Effective date.*—The deduction and related provisions are phased in over 10 years. The deduction is 1 percent for taxable years beginning after January 1, 1987, increasing 1 percentage point annually until taxable years beginning after January 1, 1996, when the full 10 percent deduction is in effect The compensatory withholding tax on foreign shareholders otherwise protected by treaty is effective for dividends paid after 1988.	No provision.

Item	Present Law	President's Proposal	House Bill	Senate Amendment
B. Corporate Dividends Paid Deduction (cont.)			The dividends received deduction changes in connection with the dividends-paid deduction also occur incrementally to correspond to the phase-in of the dividends-paid deduction (See item C., below.)	
C. Corporate Dividends Received Deduction (sec. 303 of the House bill and sec. 611 of the Senate amendment) *(See also B., above)*	Corporations generally are entitled to an 85 percent dividends received deduction; a 100 percent dividends received deduction applies to dividends from certain affiliates. The dividends received deduction is limited for dividends from a foreign corporation, based on the extent of the foreign corporation's income from a U.S. business. No dividends received deduction is allowed for dividends on stock not held with substantial risk of loss for a specified period. The deduction is limited for dividends on certain "debt financed portfolio stock."	(a) Corporations generally would be entitled to a 100 percent dividends received deduction The extent of stock ownership would not matter. (b) The dividends received deduction for corporations would be further modified in connection with the dividends paid deduction. A 90 percent dividends received deduction would be available for dividends for which the payor was entitled to a dividends paid deduction. Dividends from foreign corporations, to the extent of the corporate earnings subject to U.S. tax eligible for a dividends received deduction under present law, would produce a 100 percent dividends received deduction but no dividends paid deduction would be allowed to the foreign corporation. *Effective date.*—The general 100 percent dividends received deduction, as well as the 90 percent deduction for dividends where the payor was entitled to the dividends paid deduction, would both become effective at the same time as the dividends paid deduction (item B, above). The provisions generally would be effective for taxable years beginning after December 31, 1986, with a special rule for certain dividends paid after that date in taxable years beginning before January 1, 1987.	(a) The 85 percent dividends received deduction is reduced to 80 percent. (b) The dividends received deduction for corporations is modified in connection with the dividends paid deduction The 80 percent dividends received deduction for distributions from non-affiliates (item (a) above) is reduced to 70 percent. For distributions from affiliates, the 100 percent dividends received deduction otherwise available is reduced to 90 percent if the payor was entitled to a dividends paid deduction *Effective date.*—(a) Dividends received after December 31, 1985 (b) The 10 percent reductions in the dividends received deduction are phased in over 10 years corresponding to the phase-in of the dividends paid deduction (Item B., above.)	(a) Same as House bill (b) No provision *Effective date.*—Dividends received after December 31, 1986.
D. Extraordinary Dividends Received by Corporate Shareholders (sec. 614 of the Senate amendment)	If a corporate shareholder receives an "extraordinary" dividend on stock and disposes of the stock without holding it for more than 1 year, the basis of the stock must be reduced by the amount of the untaxed portion of the dividend "Extraordinary dividend" is defined in terms of the size of the dividend in relation to the shareholder's adjusted basis in its stock The untaxed portion of the dividend is the excess of the value of the distribution over the taxable portion of the distribution (i.e., net of the dividends received deduction).	No provision	No provision.	The basis of stock held by a corporation is reduced at disposition of the stock by the untaxed portion of extraordinary dividends, regardless of the holding period of the stock A taxpayer may elect to measure whether the dividend is extraordinary by reference to fair market value of the stock, rather than adjusted basis, if fair market value is established to the satisfaction of the Treasury Department *Effective date* Dividends declared after March 18, 1986. A targeted transitional rule is provided

Item	Present Law	President's Proposal	House Bill	Senate Amendment
E. Corporate Shareholder Redemptions (sec. 637 of the Senate amendment)	If a shareholder surrenders stock of the issuing corporation and receives a distribution out of earnings and profits, the transaction is treated as a dividend, rather than a sale of the surrendered stock, unless specified circumstances exist. If the transaction is treated as a sale, capital gain or loss treatment may apply to the difference between the amount of the distribution and the basis of the stock surrendered. The shareholder's basis in the remaining shares is equal to the basis of all of the taxpayer's shares prior to the surender, reduced by the basis of the shares surrendered. If the transaction is treated as a dividend, the gross amount of the distribution is taxed as a dividend and the basis of the shareholder's remaining stock is not reduced. In the case of a corporate shareholder, the dividends received deduction generally is available.	No provision	No provision	If a corporate shareholder surrenders stock of the issuing corporation and receives a distribution for which the dividends received deduction would be available if the distribution were treated as a dividend, the transaction is generally treated as a sale of the surrendered stock. However, no loss is created if no loss would have been allowed under present law. (Floor amendment by Senator Stevens, adopted by voice vote.) *Effective date.*—Distributions after June 23, 1986, unless pursuant to a binding contract in effect on that date.
F. Dividend Exclusion for Individuals (sec. 313 of the House bill and sec. 612 of the Senate amendment)	The first $100 of qualifying dividends received by an individual ($200 by married couple filing a joint return) is excluded from income. Generally, qualifying dividends are dividends from domestic corporations.	The dividend exclusion for individuals would be repealed. *Effective date.*—Taxable years beginning after December 31, 1985.	Same as President's proposal. *Effective date.*—Dividends received in taxable years beginning after December 31, 1985.	Same as House bill and President's proposal. *Effective date.*—Dividends received in taxable years beginning after December 31, 1986.
G. Stock Redemption Payments (sec. 314 of the House bill and sec. 613 of the Senate amendment)	In general, a corporation may not deduct the cost of repurchasing its own stock from shareholders. Some corporations have taken the position that stock redemption payments and related expenses for the purpose of preventing a hostile takeover of the corporation (so-called "greenmail" payments) are deductible as ordinary business expenses.	No provision	No portion of payments by a corporation in connection with a redemption of its own stock is deductible. *Effective date.*—No effective date is expressly provided.	Same as House bill, with technical modifications. *Effective date.*—The provision is effective for payments on or after March 1, 1986.

Item	Present Law	President's Proposal	House Bill	Senate Amendment
H. Special Limitations on Net Operating (NOL) Carryovers (sec. 621 of the House bill and sec. 321 of the Senate amendment)				
1. General rules	NOL carryovers are eliminated or reduced in different degrees and subject to different requirements, depending on whether the transaction takes the form of a taxable purchase or a tax-free reorganization, respectively. Under the 1954 Code, in the case of a taxable purchase, NOL carryovers are eliminated if one or more of the loss corporation's ten largest shareholders increase their common stock ownership by more than 50 percentage points through taxable purchases within a two-year period, unless a business-continuation requirement described below is satisfied (item H 4). Under the 1954 Code, in the case of reorganizations subject to the rules, if the loss corporation's shareholders' continuing interest is less than 20 percent the NOL carryover is reduced by 5 percent for each percentage point less than 20 received by such shareholders. Amendments were made by the Tax Reform Act of 1976 that would substantially change these 1954 Code provisions, while retaining significant differences between the treatment of taxable purchases and tax-free reorganizations. The effective date of these amendments was repeatedly postponed until January 1, 1986. Both the House bill and the Senate amendment, however, repeal these amendments effective January 1, 1986. (See item 9 , below, regarding status of amendments made by the Tax Reform Act of 1976.)	No provision	Generally, if there is a more than 50 percent change in ownership of a loss corporation over a three-year period (however effected) the total NOL carryovers are not reduced but there is an annual limitation on their use after the change. In general, the annual amount of earnings against which the losses may be used after the change cannot exceed the value of the loss corporation at the time of the change multiplied by a special rate of return (see item H.3., below). Similar rules apply for purposes of other carryover items in addition to net operating losses.	Generally, same as House bill In addition to the principal substantive differences in the implementation of the general approach that are discussed below, there are various other technical and drafting differences. These include differences in the application of certain attribution and other rules to determine whether a change has occurred that brings the limitations into effect, and differences in the way in which the value of the corporation is determined in the case of certain transactions.
2. Certain transfers of stock that are disregarded in determining whether the special limitations apply	In addition to certain related party exceptions, acquisitions by gift or bequest (as well as certain other acquisitions) are not purchases subject to the taxable purchase rules.	No provision.	In addition to certain related party exceptions, if stock is acquired by reason of death, the transferee is treated as having owned stock during the period held by a decedent who was a family member	In addition to certain related party exceptions, transfers by reason of death, gift, divorce, or separation are disregarded Acquisitions by ESOPs or ESOP participants are also disregarded.

Item	Present Law	President's Proposal	House Bill	Senate Amendment
3. Rate of return limitation	No provision	No provision.	The rate that is applied to the loss corporation's value to determine the annual limitation on use of NOL carryovers is the Federal long-term bond rate at the time of the ownership change, adjusted to take into account tax exemption for interest.	The rate that is applied to the loss corporation's value to determine the annual limitation on use of NOL carryovers is the Federal mid-term bond rate, without any adjustment to provide a tax-exempt rate.
4. Business continuation requirements	In the case of a taxable purchase, NOL carryovers are eliminated if the loss corporation fails to continue the conduct of a trade or business that was conducted before the ownership change. In the case of a tax-free reorganization there is no specific business continuation requirement apart from the continuity of business enterprise that is required for reorganization treatment	No provision	NOL carryovers are eliminated in taxable purchases, as well as in tax-free reorganizations, unless the loss corporation satisfies the continuity of business enterprise requirement that applies to tax-free reorganizations under present law, for the two-year period following the ownership change	No provision
5. Built-in gains and losses	The statutory limitations on NOL carryovers do not apply to built-in gains and losses. (Built-in gains and losses are, generally, gains and losses not recognized at the time of an ownership change but attributable to appreciation or depreciation that had occurred prior to that time.) However, under regulations, built-in losses (including depreciation deductions) are limited in certain consolidated return situations, subject to a 15-percent de minimis rule.	No provision.	The statutory limitations on NOL carryovers apply to built-in losses (including built-in depreciation deductions), with relief for built-in gains These rules apply to built-in gains and losses recognized during a 10-year recognition period following the change of ownership, subject to a de minimis rule where net built-in losses do not exceed 15 percent of the value of the loss corporation	Generally same as House bill, with a shorter recognition period (5 years instead of 10 years) and a larger de minimis amount (25 percent instead of 15 percent). However, built-in depreciation deductions are not treated as built-in losses subject to the limitations

Item	Present Law	President's Proposal	House Bill	Senate Amendment
6. Bankruptcy proceedings and stock-for-debt exchanges				
a. Bankruptcy proceedings generally	(a) Special rules treat creditors who receive stock in a bankruptcy proceeding as continuing stockholders, so that NOLs generally are available without limitation However, limitations can apply in some situations involving trade creditors if there are not sufficient security holders.	No provision	(a) Creditors who receive stock in exchange for their claims are treated as new stockholders, not continuing stockholders, for purposes of determining whether a change of ownership has occurred. Accordingly, after a bankruptcy reorganization or a stock-for-debt exchange that occurs as part of a bankruptcy reorganization, the limitations will apply if former creditors receive more than 50 percent of the company. In applying the rate of return limitation, a loss corporation's value is measured immediately after the change, thus taking account of additional positive value (if any) resulting from the surrender of creditors' claims.	(a) Creditors who receive stock in exchange for their claims are treated as continuing shareholders if the debt was held for one year before the filing of bankruptcy or arose in the ordinary course of the loss corporation's business Thus, the special limitations do not apply after a bankruptcy reorganization or a stock-for-debt exchange that occurs as part of a bankruptcy reorganization, if such creditors and/or former shareholders retain a 50-percent interest in the corporation. Interest deductions on converted debt are backed out of NOL carryovers if deducted during three-year period preceding bankruptcy proceeding On a second ownership change within two years, NOL's are eliminated
b. Financially troubled thrifts	(b) Special rules enable certain acquisitions of financially troubled thrifts to qualify as tax-free reorganizations. (See IX D.1.) In addition, there are special NOL rules for reorganizations involving financially troubled thrifts (See IX. D.2.) These rules provide treatment of depositors as continuing shareholders in a manner that preserves net operating loss carryovers in certain situations that could otherwise be viewed as invoking the special limitations due to ownership changes.	No provision.	(b) The special rules for financially troubled thrifts are repealed (See IX D 1 and 2.)	(b) The special reorganization rules for financially troubled thrifts are retained (See IX D 1) The NOL carryover rule for bankruptcy reorganizations ((a) above) applies to transactions involving financially troubled thrifts that receive special treatment under present law, but with modifications generally to preserve NOL carryovers that would not be limited under present law (See IX D 2.)
7. Investment assets	There is no specific limitation on investment assets. However, under the rule for taxable purchases, the loss corporation must hold assets used in a trade or business	No provision.	If at least one-third of loss corporation's assets consists of passive assets, the income against which NOL carryovers can be used is subject to reduction.	NOL carryovers are eliminated if two-thirds or more of loss corporation's asset value is attributable to assets held for investment (except if a RIC or a REIT).
8. Capital contributions	There is no specific rule with respect to pre-acquisition capital contributions	No provision	The value of the loss corporation is reduced by the value of capital contributions made within three years prior to the acquisition date.	The value of the loss corporation is reduced by capital contributions made with a tax-avoidance motive Capital contributions made within two years prior to the acquisition date are presumed to have a tax avoidance motive, except as provided in regulations
9. Effective date and status of amendments made by Tax Reform Act of 1976	The 1976 Act amendments apply to purchases after December 31, 1985, and reorganizations pursuant to plans adopted on or after January 1, 1986.	No provision.	*Effective date.*—The amendments are effective for acquisitions on or after January 1, 1986, and reorganizations pursuant to plans adopted on or after January 1, 1986, subject to general transition rules for bankruptcy reorganization and several targeted transition rules The 1976 Act amendments do not come into effect at any time.	The new provisions are effective for purchases after December 31, 1986 and reorganizations pursuant to plans adopted after December 31, 1986 (subject to several targeted transition rules). The 1976 Act amendments are repealed, effective January 1, 1986.

Item	Present Law	President's Proposal	House Bill	Senate Amendment
I. Net Operating Loss Carrybacks—Tax Rate Limitation (sec. 559 of the Senate amendment)	Net operating losses may be carried back (generally, to each of the three years preceding the taxable year of the loss) without regard to any difference in the maximum statutory tax rates in the year in which the loss arose and the year to which the loss is carried back.	No provision	No provision	A net operating loss of a corporation can reduce such corporation's income tax liability for a carryback year only up to the product of (a) the amount of the carryback, times (b) the highest regular corporate tax rate in effect in the taxable year in which the loss arose However, the number used as such highest rate of tax is to be adjusted under regulations, so that the revenues produced by this provision do not exceed $200 million during the period of fiscal years 1987-1991 (Floor amendment by Sen Bumpers, adopted by voice vote) *Effective date* —Net operating losses for taxable years beginning after December 31, 1986.

Item	Present Law	President's Proposal	House Bill	Senate Amendment
J. Recognition of Gain or Loss on liquidating Sales and Distributions	On a liquidating distribution or sale, a corporation may recognize gain under recapture provisions, the tax benefit doctrine, or other statutory or judicial rules. Apart from these rules, however, under the so-called "General Utilities" rule (the remaining statutory codification of the result in a Supreme Court case), a corporation generally recognizes no gain or loss on a sale or distribution of its assets in liquidation. Such nonrecognition also applies to the "deemed" liquidating sale that occurs when one corporation acquires the stock of another and elects to step up the basis of the corporate assets (under section 338). In all these cases, the recipient of appreciated assets obtains a new, stepped-up (basically, fair market value) basis for purposes of computing future depreciation or other deductions and for purposes of determining gain or loss on future asset sales. A corporation that sells its assets without liquidating recognizes gain or loss in full. Gain (but not loss) is generally recognized by a corporation on a nonliquidating distribution of property with respect to its stock (e.g., a dividend or redemption). The gain recognized is generally the excess of the fair market value of the property over its basis in the hands of the corporation. A corporation may be entitled to nonrecognition on a nonliquidating distribution if it relates to "qualified stock." Qualified stock is stock held by a long-term noncorporate shareholder owning 10 percent or more of the corporation's outstanding stock.	No provision	In general, gain or loss is recognized by a corporation on a liquidating distribution of its assets, as if the corporation had sold the assets at fair market value, and on liquidating sales. Nonrecognition would be permitted for the following transactions by a liquidating corporation: (1) certain carryover basis distributions to controlling corporate shareholders; (2) certain distributions in connection with tax-free transactions; (3) certain distributions with respect to stock held by noncorporate, long-term shareholders holding 10 percent or more of the distributing corporation's stock (under rules similar to the qualified stock exception applicable to nonliquidating distributions under present law); and (4) certain liquidating sales of property, and sales of stock treated as asset sales under section 338, to the same extent nonrecognition would be available under (3) above if the property had been distributed. The recapture rules and other statutory and judicial rules of present law continue to apply to these excepted transactions. In addition, gain on ordinary income property and short-term capital gain property is subject to tax under (3) and (4). In general, present law rules continue to apply to nonliquidating distributions, except that the rules relating to the qualified stock exception under present law are conformed to the rules for liquidating distributions provided by the bill. *Effective date.*—In general, the provisions apply to liquidating distributions and sales and exchange occurring on or after November 20, 1985. Under transitional rules, distributions and sales made pursuant to a plan of liquidation adopted before that date are not affected. Particular rules apply in determining whether a plan was adopted before November 20 for this purpose, including rules for certain stock sales underway before that date.	No provision.

Item	Present Law	President's Proposal	House Bill	Senate Amendment
K. Allocation of Purchase Price in Certain Sales of Assets (sec. 632 of the Senate amendment)	In the case of an acquisition of a corporation by a stock purchase, a corporate purchaser may elect to treat the purchase as a purchase of assets (sec. 338). In such case, the purchase price must be allocated among the target corporation's assets. Recently issued temporary and proposed Treasury regulations provide that, for acquisitions after January 29, 1986, the allocation must be made using the "residual" method. Under the residual method, the purchase price is first allocated to the fair market value of tangible and intangible assets other than goodwill and going concern value. Any excess is allocated to goodwill and going concern value. This approach does not permit use of a so-called "second-tier" method of allocation which would produce a basis different from fair market value for depreciable or separately resaleable assets. In the case of a direct acquisition of the assets of a going business, however, neither the Code nor the regulations expressly require use of the residual method in allocating purchase price among assets.	No provision.	No provision	The rules relating to stock acquisitions are the same as under present law. The rules relating to asset acquisitions are conformed to the stock acquisition rules so that both the buyer and the seller in a sale of a business are required to use the residual method in allocating purchase price. The Treasury Department is authorized to require information reporting by the parties regarding amounts allocated to goodwill or going concern value and other allocations. *Effective date.*—Transactions after May 6, 1986.

Item	Present Law	President's Proposal	House Bill	Senate Amendment
L. Related Party Sales (sec. 638 of the Senate amendment)	Installment sale treatment is not available for gain on a sale of property to a related party if the property is depreciable in the hands of the transferee, unless it is established to the satisfaction of the Internal Revenue Service that tax avoidance was not a principal purpose of the sale. Gain on sales of depreciable property between related parties is treated as ordinary income. In the case of certain related party partnership transactions, ordinary income treatment is also required if the property is not a capital asset in the hands of the transferee. Related parties for these purposes include a person and all entities which are 80 percent owned, directly or indirectly, with respect to that person Specified attribution rules apply.	No provision	No provision.	Related parties include a person and all entities more than 50 percent owned, directly or indirectly, by that person Related parties also include entities more than 50 percent owned, directly or indirectly, by the same persons The attribution and relationship rules are generally based on present law rules that apply to limit losses on sales between related parties For example, there is attribution between parents and childen (Floor amendment by Sen Durenberger, adopted by voice vote) *Effective date* —Sales after June 20, 1986, unless made pursuant to a binding contract in effect on that date.
M. Amortizable Bond Premium (sec. 1723 of the Senate amendment)	An amortizable bond premium exists where a taxpayer buys a bond for more than face value. The amount of that excess is allowed as a deduction over the remaining term of the bond, generally offsetting interest income on the bond	No provision.	No provision.	The amortizable bond premium deduction is treated as interest, except as otherwise provided by regulations. Thus, for example, bond premium is treated as interest for purposes of applying the investment interest limitations (Floor amendment by Sen Byrd, adopted by voice vote) *Effective date* —Obligations acquired after date of enactment

Item	Present Law	President's Proposal	House Bill	Senate Amendment
N. Cooperative Housing Corporations (sec. 1405 of the House bill and secs. 1703-1704 of the Senate amendment)	A tenant-stockholder in a cooperative housing corporation is entitled to deduct his or her "proportionate share" of the housing cooperative's expenses for interest and taxes. Tenant-stockholders generally are limited to individuals. The tenant-stockholder's proportionate share is the portion of the cooperative's interest and taxes that bears the same ratio to the cooperative's total expenses for interest and taxes that the portion of the cooperative's stock held by the tenant-stockholder bears to the total outstanding stock of the cooperative.	No provision.	Cooperative housing corporations that charge tenant-stockholders with a portion of the cooperative's interest and taxes in a manner that reasonably reflects the costs to the cooperative of the interest and taxes allocable to each tenant-stockholder's dwelling unit, may elect to have such tenant-stockholders deduct the separately allocated amounts. *Effective date.*—Taxable years beginning after December 31, 1985.	Corporations, trusts, and other taxpayers besides individuals may be treated as tenant-stockholders in cooperative housing corporations. Maintenance and lease expenses are disallowed where payments by tenant-stockholders are allocable to amounts properly chargeable to the capital account of the cooperative. *Effective date.*—Taxable years beginning after December 31, 1986. Special rules are provided for two limited profit cooperatives.
O. Real Estate Investment Trusts 1. General requirements	An entity that qualifies as a real estate investment trust ("REIT") is subject to a corporate tax but is allowed a deduction for dividends paid to shareholders. To qualify as a REIT, an entity (1) must be taxable as a domestic corporation, (2) must have at least 100 shareholders, (3) must not have 50 percent or more of its stock held by five or fewer shareholders, (4) must distribute most of its income currently, (5) must hold a minimum percentage of its assets in real estate related and other passive assets, and (6) must derive minimum percentages of its income from such assets. A REIT is required to be a calendar year taxpayer unless it was in existence as a REIT for any taxable year beginning prior to October 4, 1976.	No provision.	No provision.	A taxpayer is permitted to change its accounting year without consent in connection with its initial election of REIT status. An entity is not disqualified from electing REIT status in the first taxable year of its existence because it was closely held. Partner to partner attribution is ignored in determining if the REIT is closely held. Corporations that have never qualified as a REIT and that have earnings and profits accumulated as a regular corporation are required to distribute accumulated earnings and profits in order to elect REIT status.
2. Asset and income requirements	In general, to meet the asset requirement, at the close of each quarter of the taxable year, at least 75 percent of the value of the REIT's assets must be represented by real estate assets, cash and cash items, and Government securities. In general, to meet the income requirements, at least 75 percent of the REIT's gross income for the taxable year must be derived from rents on real property, interest on obligations secured by real property, gain from the sales of interests in real property (other than property held for sale in the ordinary course of a trade or business), dividends from a REIT, refunds of property taxes, and certain other limited sources. In addition, at least 95 percent of the REIT's gross income must be derived from these sources and interest or dividends or gains from the sale of securities.	No provision.	No provision.	REITs are permitted to hold assets in wholly owned subsidiaries. REIT qualification tests would be applied on an entity wide basis (i.e., ignoring the separate corporate status of the subsidiaries). For a one-year period after the receipt of new equity capital, income from the temporary investment of the new capital that is derived from stock or securities is treated as qualifying "75 percent income."

Item	Present Law	President's Proposal	House Bill	Senate Amendment
3. Definition of rents	Rents from real property include rents from interests in real property and charges for services customarily furnished in connection with the rental of real property whether or not such charges are separately stated. Rents are not considered to qualify if services are provided other than through an independent contractor. In addition, rents are not considered to qualify if they are based on the net profits of the tenant.	No provision.	No provision.	REITs are permitted to provide without being required to use independent contractors those services that may be furnished in connection with the rental of real property by a tax-exempt organization without giving rise to unrelated business income. REITs are permitted to receive rents based on the net income of the tenant, provided that the tenant's profits are derived only from sources that would be qualified rent if earned directly by the REIT.
4. Distribution requirement	In general, the distribution requirement is satisfied if for the taxable year the REIT distributes 95 percent of its taxable income determined without regard to any capital gains recognized by the REIT.	No provision.	No provision.	Any income that is accrued but not received with respect to original issue discount on a loan issued in connection with the sale of property, or with respect to a deferred rental agreement, or any income that is recognized as the result of the failure of an exchange that the REIT intended in good faith but that was ultimately determined not to qualify for treatment as a tax-free like kind exchange, is not subject to the distribution requirement to the extent that such amounts exceed 5 percent of the REIT's taxable income. The REIT is required to pay tax on the undistributed amount. The amount of a REIT's current earnings and profits will not be less than the REIT's taxable income for the purpose of determining whether a distribution was made out of earnings and profits.
5. Capital gains	If the REIT has recognized any capital gain during a taxable year, the REIT is taxable on the amount of such gain unless it elects to pay a capital gain dividend. The REIT may elect to pay a capital gain dividend by designating in a notice mailed to shareholders within 30 days of the end of the REIT's taxable year, that a portion of dividends paid during the taxable year are capital gain dividends. The portion so designated may not exceed the REIT's net capital gain recognized reduced by any net operating losses. Any dividend so designated is treated as a capital gain by the recipient shareholder.	No provision.	No provision.	REITs are permitted to compute their net capital gain without offset for net operating losses. NOL's not used to offset capital gain income would be carried over according to the ordinary rules. REITs are permitted to send capital gain notices to shareholders with the mailing of their annual report, rather than 30 days after year end.

Item	Present Law	President's Proposal	House Bill	Senate Amendment
6. Prohibited transactions	A 100 percent tax is imposed on a REIT's net income from prohibited transactions. Any net loss from prohibited transactions is not deductible in computing taxable income. In general, a prohibited transaction is the sale of property held primarily for sale in the ordinary course of business. A safe harbor is provided whereby a sale of property is not treated as a prohibited transaction if such property has been held for at least four years (for the production of rental income if land and improvements), the aggregate expenditures during the four-year period preceding the date of sale that are includible in the basis of the property do not exceed 20 percent of the selling price of the property, and the sale is one of not more than five sales of property by the REIT during the taxable year. In general, the disposition of property acquired pursuant to a foreclosure is not treated as a prohibited transaction.	No provision.	No provision.	The number of sales that a REIT is able to make within the prohibited transaction safe harbor is expanded from 5 to 7. An alternative safe harbor is provided whereby a REIT may make any number of sales during a taxable year provided that the gross income from such sales does not exceed 15 percent of the REIT's taxable income for such year. The extent of improvements that a REIT is permitted to make is increased from 20 percent to 30 percent of the property's adjusted basis. Any marketing or development is required to be done through independent contractors. Losses from prohibited transactions are permitted to offset taxable income but are not permitted to offset gains from prohibited transactions.
7. Deficiency dividends	If it is determined that a REIT failed to satisfy the distribution requirement in a taxable year on account of a subsequent adjustment to its taxable income, then the REIT may avoid disqualification by the prompt distribution of a "deficiency dividend." A REIT for which such a deficiency is determined must pay interest on the deficiency as well as a penalty equal to the amount of interest not in excess of half of the amount of the deficiency.	No provision	No provision.	The penalty tax under section 6697 on deficiency dividends is eliminated.
8. Effective date				*Effective date.*—Generally, taxable years beginning after December 31, 1986.

Mortgage-Backed Securities (secs. 1111-1115 of the Senate amendment)	*(a) Imposition of corporate tax* *In general.*—A corporation generally is treated as a taxpayer separate from its shareholders. The corporation is taxed on its income, and the shareholder is taxed on the subsequent distribution of the corporation's income in the form of dividends Corporations receive a deduction in computing their taxable income for interest paid on indebtedness. *Corporations treated as conduits.*—Certain small business corporations ("S corporations") generally are not subject to a corporate level tax Rather, the income of the corporation is allocated among and taxed directly to the shareholders. To qualify as an S corporation, a corporation must be a domestic corporation that has 35 or fewer shareholders none of whom are corporations, and must also meet certain other requirements. Real estate investment trusts ("REITs") and regulated investment companies ("RICs") generally are treated as pass-through entities since they receive deductions for dividends paid to shareholders. Capital gains realized by a REIT or a RIC may be passed through to its shareholders. To qualify as a REIT, a corporation must derive most of its income from real estate related sources, must hold primarily real estate assets, must distribute most of its income currently, and must meet certain other requirements. An interest in a corporate debt obligation that is secured by real property mortgages is not treated as a qualifying real estate asset for a REIT To qualify as RIC, a corporation must derive most of its income from investments in securities, must distribute most of its income currently, and must meet certain other requirements Certain requirements are imposed on both REITs and RICs that are intended to prevent these entities from engaging in the active conduct of a trade or business	(a) No provision	(a) No provision.	*(a) REMICs* *In general*—A REMIC is an entity that is formed for the purpose of holding a fixed pool of mortgages secured by an interest in real property, and issuing multiple classes of interests therein. A REMIC is treated as a corporation for income tax purposes, but is given a deduction for all amounts includible in income of holders of "regular interests" regardless of whether such interests otherwise would be treated as debt for Federal income tax purposes, and is also given a deduction for amounts distributed to holders of "residual interests" up to the amount of a deemed return that is based on the "long-term Federal rate." Rules are provided to prevent active business activities with respect to the REMIC's assets. *Regular and residual interests.*—All interests in a REMIC must be either regular or residual interests. Regular interests are treated as debt instruments for Federal income purposes Residual interests generally are treated as stock for Federal income tax purposes, but special rules are provided for the inclusion in income of distributions with respect to residual interests, the adjustment of the holder's basis in the residual interest, and for dispositions of residual interests. *Transfers of property to a REMIC.*—The transfer of property to a REMIC in exchange for either regular or residual interests, or for cash or other property, results in the recognition of gain upon the transfer Loss is recognized on the transfer of property to a REMIC for cash or other property, but if property is transferred to a REMIC in exchange for regular or residual interests, loss is deferred until the disposition of the interests

P. Mortgage-Backed Securities (cont'd.)	*Entity classification.*—Under Treasury regulations, certain noncorporate entities that have sufficient corporate characteristics are treated as corporations for Federal income tax purposes. Among the entities that are treated as "associations taxable as corporations" under the regulations are trusts that have multiple classes of interests. *(b) Original issue discount and market discount* *Original issue discount.*—Under the original issue discount ("OID") rules, any OID, which is defined as the excess of the stated redemption price of a debt instrument over its issue price, is treated as interest. Both borrower and lender generally are required to account for the accrual of original issue discount on an economic basis over the term of the debt instrument. The application of the OID rules is uncertain for debt instruments the maturity of which may be accelerated on account of prepayments on obligations that collateralize the debt instrument. *Market discount.*—Market discount generally is that portion of the excess of a debt instrument's stated redemption price over the holder's basis, which portion exceeds the amount of OID, if any, with respect to the instrument. The holder of a debt instrument with market discount generally recognizes the market discount as interest income at the time that the portion of the debt instrument's stated redemption price to which the market discount relates is paid. The application of the market discount rules to debt instruments the principal of which is payable in more than one installment is uncertain.	(b) No provision	(b) No provision	*(b) OID and market discount rules* *OID rules.*—The application of the OID rules to debt instruments, the maturity of which is accelerated on account of prepayments on obligations that collateralize the instrument, is clarified. OID on such an instrument is calculated taking into account prepayments as such prepayments occur. *Market discount rules.*—Regulatory authority is granted to the Treasury Department to provide rules for the treatment of market discount and premium on obligations the principal of which is paid in installments, whether or not such obligations are subject to prepayment.

P. Mortgage-Backed Securities (cont'd.)	*(c) Other* Certain thrift institutions are permitted to deduct a percentage of their taxable income as a bad debt deduction provided that a specified portion of the institution's assets are "qualifying assets," including "qualifying real property loans." Corporate debt obligations secured by real property mortgages are not treated as qualifying real property loans. Issuers of debt instruments that have original issue discount are required to report to certain holders the amount of the annual accrual of OID.	(c) No provision.	(c) No provision	*(c) Other* An interest in a REMIC is treated as a real estate asset for purposes of the requirements for qualification as a REIT and is treated as a qualifying real property loan for purposes of the requirements relating to percentage bad debt deductions for certain thrift institutions. Reporting requirements are expanded "Owners' debt pools" are treated as corporations. In general, an owners' debt pool is an entity that is treated as a trust or partnership, a substantial portion of whose assets consist of real property mortgages, and whose principal activity is to issue debt in varying maturities. *Effective date.*—Generally effective for taxable years beginning after December 31, 1986. The OID and market discount provisions are effective for debt instruments issued after December 31, 1986. The owners' debt pool provisions generally are effective for entities formed after December 31, 1986.
Q. Regulated Investment Companies (secs. 633 and 1451-1454 of the Senate amendment)	A regulated investment company ("RIC") receives a deduction for dividends paid to shareholders, if at least 90 percent of its ordinary income is derived from specified sources commonly considered passive investment income, if it distributes at least 90 percent of its ordinary income to shareholders, if not more than 30 percent of its gross income is derived from sales of stock or securities held for less than three months, if it is regulated under the Investment Company Act of 1940 and if it also meets certain other requirements. RICs that have long-term capital gain income may designate dividends as capital gain dividends in a notice filed with shareholders within 45 days after the end of its taxable year. Shareholders treat such capital gain dividends as long-term capital gain regardless of their holding period for the RIC stock. The RIC is not required to pay any capital gains tax on the amount so designated.	No provision	No provision.	RICs are required to adopt a calendar year as their taxable year. A RIC is required to pay a nondeductible five percent excise tax on dividends paid after the close of its taxable year that are treated as having been paid in the preceding taxable year. The definition of securities is clarified by reference to the definition of securities in the Investment Company Act of 1940. Permitted income for RICs is defined to include income from foreign currencies, and options and futures contracts, derived with respect to the RIC's business of investing. Regulatory authority is given to exclude certain gains from investment in foreign currency. (Floor amendment by Senator Armstrong, adopted by voice vote.)

Item	Present Law	President's Proposal	House Bill	Senate Amendment
Q. Regulated Investment Companies (secs. 633 and 1451-1454 of the Senate amendment) (cont.)	A RIC may adopt any fiscal year as its taxable year. RICs are permitted to treat certain dividends paid after the close of a taxable year as paid during the preceding taxable year. Shareholders receiving such "spillover dividends" recognize income attributable to such dividends in the year of payment. If a RIC has several "series" of funds with stockholders whose interest in the RIC is limited to a interest in a particular fund, the RIC generally is treated as a single corporation. If the RIC is organized as a business trust, each series fund may be treated as a separate corporation, however. In the case of certain summonses served upon "third party recordkeepers," certain notice requirements are imposed on the Internal Revenue Service. Third party recordkeepers generally include various types of financial institutions, and others such as attorneys, accountants, and brokers, but do not include RICs.			In the case of RICs that have series funds, each fund is treated as a separate corporation. Tax-free treatment is given to the deemed formation of the separate corporations that are deemed to be formed under the provision. The time for filing notices for capital gains dividends and certain other purposes is extended from 45 to 60 days. RICs are treated as third party recordkeepers. (Floor amendment by Senator Armstrong, adopted by voice vote.)
R. Definition of Personal Holding Company Income (sec. 1106 of the House bill and sec. 1302 of the Senate amendment)	(a) Personal holding companies are subject to a tax on personal holding company income that is not distributed to shareholders. Generally, personal holding companies are corporations at least 50 percent of whose stock is owned by not more than five individuals and at least 60 percent of whose adjusted ordinary gross income is personal holding company income. Personal holding company income includes computer software royalties, regardless of whether such royalties are received in connection with the active conduct of the trade or business of developing the software that generates the royalites.	(a) No provision.	(a) An exception from the definition of personal holding company income is provided for computer software royalties that are received by certain corporations that (i) are actively engaged in the business of developing compter software, (ii) derive at least 50 percent of their gross income from such computer software, (iii) incur substantial trade on business expenses, and (iv) distribute most of their passive income other than computer software royalties. *Effective date.*—Royalties received after December 31, 1985.	(a) Same as House bill, except that the exception is extended to foreign personal holding companies and the requirement that at least 50 percent of the taxpayer's gross income must be derived from computer software is deleted. Similar rules are provided for a particular medical research corporation. *Effective date.*—Royalties received before, on, or after December 31, 1986.
	(b) Personal holding company income also includes all gross interest income, regardless of whether such interest is received in connection with the active conduct of the business of brokering or dealing securities.	(b) No provision.	(b) Another exception is provided from the definition of personal holding company income for interest on securities held in the inventory of a dealer in securities. In addition, a dealer in securities may deduct interest on "offsetting loans" in computing interest income. *Effective date.*—Interest received after December 31, 1985.	(b) Interest received from specified sources by a particular broker-dealer in securities is not included in personal holding company income. *Effective date.*—Interest received after the date of enactment.

Item	Present Law	President's Proposal	House Bill	Senate Amendment
S. Certain Entity Not Taxed as a Corporation (sec. 1619 of the Senate amendment)	Entities that are organized as trusts under local law may be subject to Federal income tax as corporations rather than as trusts, if they possess certain corporate characteristics. Such entities must pay corporate level tax in addition to the tax at the beneficiary level. A certain trust has been held to be taxable as a corporation due to the existence of certain business powers.	No provision.	No provisions.	A certain trust will not be taxed as a corporation if, among other things, it makes an election and agrees not to exercise business powers contained in its trust instrument. (Floor amendment by Sen. Durenberger, adopted by voice vote.) *Effective date.*—Taxable years beginning after the taxable year in which the election is made, provided that all conditions of the Senate amendment continue to be satisfied.

Item	Present Law	President's Proposal	House Bill	Senate Amendment
A. Individual Minimum Tax (sec. 501 of the House bill and sec. 1101 of the Senate amendment) 1. Structure	An alternative tax, applying to a broader income base and at a lower rate than the regular tax, and payable to the extent in excess of regular tax liabilities.	Same as present law.	Same as present law	Same as President's proposal and House bill
2. Rate	20 percent.	Same as present law	25 percent.	20 percent (same as President's proposal and present law)
3. Exemption amount	$40,000 for joint returns, $30,000 for singles, $20,000 for marrieds filing separately	The sum of the following (1) $15,000 for joint returns, $12,000 for heads of household, $10,000 for singles, $7,500 for marrieds filing separately; (2) the first $10,000 of preferences; and (3) the taxpayer's personal exemptions.	Same as present law.	Same as House bill, except that the exemption amount is reduced by 25 cents for each $1 that minimum taxable income exceeds $150,000 ($112,500 for singles and $75,000 for marrieds filing separately)
4. Tax preferences *a. Dividends excluded from gross income (up to $100 per person, $200 for joint returns)*	(a) Treated as a preference.	(a) Repealed for regular tax purposes	(a) Same as President's proposal.	(a) Same as President's proposal and House bill
b. Accelerated depreciation on real property	(b) Excess over straight-line depreciation is a preference	(b) Same as present law for real property placed in service before 1986. For real property placed in service beginning in 1986, excess over Treasury 1 depreciation would be a preference.	(b) For property placed in service after 1985, treat as a preference the excess of regular tax depreciation over the alternative depreciation described above in the depreciation section of the comparison (15 years for certain low-income housing rehabilitation). Same as present law for property placed in service before 1986	(b) Same as House bill, except that (1) effective date is delayed one year, (2) property grandfathered under the depreciation rules is treated as pre-1987 property, and (3) no special rule applies to low-income housing
c. Accelerated depreciation on personal property	(c) Solely for leased personal property, excess over straight-line depreciation is a preference	(c) Same as present law for property placed in service before 1986. For leased personal property placed in service beginning in 1986, excess of regular tax depreciation over Treasury 1 depreciation would be a preference.	(c) For property placed in service after 1985, treat as a preference the excess of regular tax depreciation over the alternative depreciation (generally ADR midpoint lives) described in the depreciation section of the comparison. Same as present law for property placed in service before 1986 (i.e., for leased property only, excess over straight-line is a preference).	(c) Same as House bill, except that (1) effective date is delayed one year, and (2) property grandfathered under the depreciation rules is treated as pre-1987 property

Item	Present Law	President's Proposal	House Bill	Senate Amendment
d. Expensing of intangible drilling costs	(d) Excess over 10-year amortization (or cost depletion), to the extent in excess of net oil and gas income, is a preference.	(d) 8-percent of intangible drilling costs treated as a preference.	(d) Retains present law, except treated as a preference to the extent in excess of 65 percent of net oil and gas income	(d) Same as present law
e. 60-month amortization on certified pollution control facilities	(e) Excess over depreciation otherwise allowable is a preference.	(e) Same as present law for property placed in service before 1986 The provision would be repealed for regular tax purposes, effective in 1986	(e) Same as present law for property placed in service before 1986 The provision is repealed for regular tax purposes, effective in 1986.	(e) Same as present law
f. Expensing of mining exploration and development costs	(f) Excess over 10-year amortization is a preference.	(f) Same as present law	(f) Same as President's proposal	(f) Same as President's proposal and House bill.
g. Expensing of circulation expenditures (for newspapers, magazines, etc.)	(g) Excess over 3-year amortization is a preference.	(g) Not a preference.	(g) Same as present law	(g) Same as House bill.
h. Expensing of research and experimentation expenditures	(h) Excess over 10-year amortization is a preference.	(h) Same as present law	(h) Same as President's proposal.	(h) Same as President's proposal and House bill
i. Percentage depletion	(i) Excess over adjusted basis of the depletable property is a preference.	(i) Same as present law for property placed in service before 1986. For property placed in service beginning in 1986, excess over cost depletion would be a preference.	(i) Same as present law	(i) Same as House bill
j. Net capital gain deduction	(j) Treated as a preference.	(j) Same as present law	(j) Same as present law except that a portion of gain is excluded so that the minimum tax rate, like the maximum regular tax rate on capital gains, is 22 percent	(j) Deduction repealed for regular tax purposes
k. Incentive stock options	(k) Excess of fair market value of stock over exercise price is a preference.	(k) Same as present law.	(k) Same as President's proposal	(k) Same as President's proposal and House bill.
l. Tax-exempt interest	(l) Not a preference.	(l) Not a preference. For regular tax purposes, exemption would be repealed for newly issued securities other than government obligations	(l) Treat as a preference interest on any newly issued nonessential function bonds that continue to be exempt. Refundings of pre-1986 bonds not a preference.	(l) Same as present law
m. Excludable income earned abroad by U.S. citizens	(m) Not a preference.	(m) Same as present law	(m) Treat as a preference	(m) Same as President's proposal and present law

Item	Present Law	President's Proposal	House Bill	Senate Amendment
n. Completed contract and other methods of accounting for long-term contracts	(n) Not a preference	(n) Same as present law.	(n) Treat as a preference, by requiring use of percentage of completion method, for minimum tax purposes, on post-September 25, 1985 long-term contracts.	(n) Same as House bill for post-March 1, 1986, long-term contracts
o. Installment method of accounting	(o) Not a preference.	(o) Same as present law.	(o) Same as present law	(o) Treat as a preference by not permitting dealers to use the installment method for minimum tax purposes on sales after March 1, 1986. The provision does not apply (1) to certain sales by a manufacturer to a dealer where special relief is provided under the regular tax rules, and (2) in the case of certain elections to pay interest on the deferral of income with respect to sales of timeshares and residential lots
p. Net loss from passive investment activities	(p) Not a preference.	(p) Same as present law.	(p) To the extent otherwise deductible under minimum tax, treat as a preference the excess net loss with respect to trade or business activities (including the production of rental or royalty income) in which the taxpayer did not materially participate in management or provide substantial personal services Excess net loss is defined as net loss in excess of cash basis, which includes no more than $50,000 attributable to all of the taxpayer's tax shelter investments.	(p) Same as House bill, except that the preference (1) applies to the entire loss without regard to cash basis, (2) is reduced by the amount, if any, of the taxpayer's insolvency, and (3) conforms to the regular tax passive loss provision by applying to all rental activities, allows up to $25,000 of certain real estate rental losses, does not apply to certain working interests in oil and gas properties, and applies to certain corporations. Technical rules from the regular tax passive loss provision apply (e g. the definition of material participation, active participation, separate activities and dispositions).
q. Net loss from passive farming activities	(q) Not a preference.	(q) Same as present law	(q) Treat as a preference excess passive farm losses. Rule resembles the passive loss rule set forth above, except that it applies only to farming, applies separately to each farming activity, and treats as a preference only losses in excess of twice cash basis (without limiting cash basis from tax shelters).	(q) Same as House bill except that (1) the preference applies to the entire net loss without regard to cash basis, (2) the preference applies to personal service corporations, (3) the preference is reduced by the amount, if any, of the taxpayer's insolvency, and (4) the definition of a passive farm activity is conformed to the passive loss activity rules

5. Itemized deductions	Allowed only for casualty and theft losses, gambling losses to extent of gambling gains, charitable deductions, medical deductions (to the extent in excess of 10 percent of adjusted gross income), interest expenses (restricted to housing interest plus net investment income), and certain estate taxes.	Allowed for all itemized deductions retained under the President's proposal, except (i) interest in excess of the sum of housing interest and net investment income; and (ii) for charitable contributions of appreciated property, the amount of untaxed appreciation allowed as a regular tax deduction.	Same as present law, except that with respect to charitable contributions of appreciated property, the lesser of the amount of untaxed appreciation allowed as a regular tax deduction or the amount of the taxpayer's other preferences is treated as a preference	Same as present law, except that investment interest definition is conformed to definition for regular tax purposes
6. Regular tax elections	Taxpayers generally can elect to have minimum tax rules for measuring a particular item apply for regular tax purposes	No election rules are stated.	Same as present law	Same as House bill
7. Adjustments in other years when taxpayer pays minimum tax	No provision	No provision	Amount of minimum tax liability relating to deferral preferences allowed as a carryforward credit against regular tax liability	Same as House bill.
8. Incentive credits	Not allowed against minimum tax. Credits that do not benefit the taxpayer due to minimum tax can be used as credit carryovers against regular tax	Not allowed against minimum tax. No carryover rules are stated.	Same as present law.	Same as House bill
9. Foreign tax credit	Allowed against minimum tax (under limits similar to those applying under regular tax).	Rule is not stated	Same as present law.	Same as House bill, except that foreign tax credits can not offset more than 90% of tentative tax liability
10. Net operating losses (NOLs)	Allowed against minimum taxable income. For years after 1982, minimum tax NOLs are reduced by the items of tax preference.	Rule is not stated.	Same as present law.	Same as House bill.
11. Effective date		Taxable years beginning after December 31, 1985.	Taxable years beginning after December 31, 1985.	Taxable years beginning after December 31, 1986.

Item	Present Law	President's Proposal	House Bill	Senate Amendment
B. Corporate Minimum Tax (sec. 501 of the House bill and sec. 1101 of the Senate amendment)				
1. Structure	An add-on tax, equalling a percentage of certain preferences minus regular tax paid	An alternative minimum tax, applying to a base of regular taxable income plus preferences, and payable to the extent in excess of regular tax liability.	Same as President's proposal	Same as President's proposal and House bill
2. Rate	15 percent	20 percent.	25 percent	20 percent (same as President's proposal).
3. Exemption amount	The greater of $10,000 or the taxpayer's regular tax liability.	$15,000, plus the first $10,000 of preference income.	$40,000 (same as for individuals filing joint returns under present law).	Same as House bill, except that the exemption amount is reduced by 25 cents for each $1 that minimum taxable income exceeds $150,000
4. Tax preferences				
a. Accelerated depreciation on real property	(a) Excess over straight-line depreciation is a preference.	(a) Same as present law for property placed in service before 1986; for property placed in service beginning in 1986, excess over Treasury I depreciation would be a preference.	(a) For property placed in service after 1985, treat as a preference the excess of regular tax depreciation over the alternative depreciation described above in the depreciation section of the comparison (15 years for certain low-income housing rehabilitation). Same as present law for property placed in service before 1986.	(a) Same as House bill, except that (1) effective date is delayed one year, (2) property grandfathered under the depreciation rules is treated as pre-1987 property, and (3) no special rule applies to low-income housing
b. Capital gain preference	(b) Benefit of lower rate on capital gains is a preference.	(b) Capital gain fully included in minimum taxable income	(b) Same as President's proposal.	(b) Same as President's proposal and House bill.
c. 60-month amortization of certified pollution control facilities	(c) Excess over depreciation otherwise allowable is a preference.	(c) Same as present law for facilities placed in service before 1986; amortization rule repealed for regular tax purposes beginning in 1986.	(c) Same as present law for facilities placed in service before 1986; amortization rules repealed for regular tax purposes beginning in 1986.	(c) Same as present law
d. Bad debt reserve deduction for financial institutions	(d) Excess of deduction over amount allowable under the experience method is a preference.	(d) Bad debt reserve deduction would be repealed for regular tax purposes	(d) Same as present law	(d) Same as House bill
e. Percentage depletion	(e) Excess over adjusted basis of the depletable property is a preference.	(e) Same as present law for property placed in service before 1986; for property placed in service beginning in 1986, excess over cost depletion would be a preference.	(e) Same as present law	(e) Same as House bill
f. Accelerated depreciation on personal property	(f) Not a preference except for personal holding companies (PHCs). For PHCs, applying solely to leased personal property, excess over straight-line depreciation is a preference	(f) Same as present law for property placed in service before 1986. For leased property placed in service by a PHC beginning in 1986, excess of regular depreciation over Treasury I depreciation would be a preference. For all personal property, the lesser of (i) excess over Treasury I depreciation, or (ii) 25 percent of the corporation's net interest expense would be a preference.	(f) For property placed in service after 1985, treat as a preference the excess of regular tax depreciation over the alternative depreciation (generally ADR midpoint lives) described in the depreciation section of the comparison. Same as present law for property placed in service before 1986 (i.e., solely for leased property placed in service by a PHC, excess over straight-line is a preference). One transitional rule is provided	(f) Same as House bill, except that (1) effective date is delayed one year, and (2) property grandfathered under the depreciation rules is treated as pre-1987 property
g. Expensing of mining exploration and development costs	(g) Solely for PHCs, excess over 10-year amortization is a preference.	(g) Treat as a preference for all corporations	(g) Same as President's proposal	(g) Same as present law

h. Expensing of intangible drilling costs	(h) Solely for PHCs, excess over 10-year amortization (or cost depletion), to the extent in excess of net oil and gas income, is a preference	(h) For all corporations, 8 percent of intangible drilling costs is treated as a preference.	(h) Treat as a preference for all corporations. Use present law rule, but with 65 percent net income offset, to measure the preference	(h) Same as present law, except that preference applies to all corporations
i. Expensing of circulation expenditures (by newspapers, magazines, etc.)	(i) Solely for PHCs, excess over 3-year amortization is a preference.	(i) Not a preference	(i) Same as present law	(i) Same as House bill
j. Expensing of research and experimentation expenditures	(j) Solely for PHCs, excess over 10-year amortization is a preference.	(j) Same as present law	(j) Not a preference for any corporation	(j) Same as House bill
k. Tax-exempt interest	(k) Not a preference.	(k) Not a preference; for regular tax purposes, only governmental obligations remain exempt.	(k) Treat as a preference interest on any newly issued nonessential function bonds that continue to be exempt. Refundings of pre-1986 bonds not a preference.	(k) Same as present law
l. Excludable foreign sales corporation (FSC) income	(l) Not a preference	(l) Same as present law	(l) Treat as a preference	(l) Same as present law and President's proposal
m. Completed contract and other methods of accounting for long-term contracts	(m) Not a preference.	(m) Same as present law	(m) Treat as a preference by requiring use of percentage of completion method, for minimum tax purposes, on post-September 25, 1985 long-term contracts.	(m) Same as House bill for post March 1, 1986, long-term contracts
n. Charitable contributions of appreciated property	(n) Not a preference.	(n) Amount of untaxed appreciation claimed as a deduction is a preference	(n) Lesser of untaxed appreciation or the amount of the taxpayer's other preferences is a preference.	(n) Same as present law
o. Installment method of accounting	(o) Not a preference.	(o) Same as present law	(o) Same as present law	(o) Treat as a preference by not permitting dealers to use the installment method for minimum tax purposes on sales after March 1, 1986. The provision does not apply (1) to certain sales by a manufacturer to a dealer where special relief is provided under the regular tax rules and (2) in the case of certain elections to pay interest on the deferral of income with respect to sales of timeshares and residential lots
p. Capital construction funds for shipping companies	(p) Not a preference.	(p) Repealed for regular tax purposes	(p) Same as present law	(p) Treat as a preference
q. Business untaxed reported profits	(q) Not a preference	(q) Same as present law	(q) Same as present law	(q) Treat as a preference 50 percent of the excess of the taxpayer's pre-tax book income over alternative minimum taxable income (determined without regard to this preference and prior to reduction by NOLs). Book income is the income of the taxpayer as shown in financial reports or statements filed with the S.E.C. or other Federal, State or local regulators, or provided to shareholders, owners or creditors. Under certain circumstances, earnings and profits may be substituted for book income. The preference is computed by consolidating the book income of those corporations which are consolidated for tax purposes

Item	Present Law	President's Proposal	House Bill	Senate Amendment
q. Business untaxed reported profits (cont'd)				Earnings of a corporation that does not file a consolidated tax return with the taxpayer are taken into account only to the extent of dividends received from the other corporation. Certain Alaska native corporations may calculate book income using the asset bases determined under the Alaska Native Claims Settlement Act. Certain amounts paid to other Alaska native corporations may be treated as expenses for book purposes in the same year as the amounts are deductible for tax purposes. (Floor amendment by Senator Stevens, adopted by voice vote.) One transitional rule is provided.
5. Regular tax elections	No provision.	No provision.	Permit elections to apply minimum tax rules for regular tax purposes.	Same as House bill.
6. Adjustment in other years when taxpayer pays minimum tax	No provision.	No provision.	Amount of minimum tax liability is allowed as a carryforward credit against regular tax liability in other years.	Amount of minimum tax liability relating to deferral preferences is allowed as a carryforward credit against regular tax liability.
7. Incentive credits	Not allowed against minimum tax. Credits that do not benefit the taxpayer due to minimum tax can be used as credit carryovers against regular tax.	Not allowed against minimum tax. No carryover rules are stated.	(a) Generally, apply present-law rule under alternative minimum tax on individuals (not allowed against minimum tax but can be carried over). (b) Corporations with NOLs in 2 of the last 3 years before 1986 can use pre-1986 credits to offset 75 percent of minimum tax liability. (c) Income eligible for the Puerto Rico and possessions tax credit (sec. 936) is exempted from the minimum tax.	(a) Same as House bill. (b) No provision. (c) Same as House bill.
8. Foreign tax credit	Foreign preferences not subject to add-on tax.	Rule is not stated.	Apply present-law rule under alternative minimum tax on individuals (allowed subject to limits similar to those under regular tax).	Same as House bill, except that foreign tax credits can not offset more than 90% of tentative tax liability.
9. Net operating losses (NOLs)	Allowed in calculating add-on tax.	Rule is not stated.	Allow against minimum taxable income. For years before 1986, reduce minimum tax NOLs by the items of tax preference under present law. For years after 1985, reduce minimum tax NOLs by all newly enacted items of tax preference.	Same as House bill, adjusted for change in effective date.
10. Estimated tax payments	Corporations are not required to make estimated tax payments with respect to minimum tax liability.	No provision.	Require that estimated tax payments be made with respect to minimum tax liability.	Same as House bill.
11. Effective date		Taxable years beginning after December 31, 1985.	Taxable years beginning after December 31, 1985.	Taxable years beginning after December 31, 1986.

Item	Present Law	President's Proposal	House Bill	Senate Amendment
A. Limitations on the Use of the Cash Method of Accounting (sec. 902 of the House bill and sec. 321 of the Senate amendment)	(a) A taxpayer may elect to use any method of accounting that clearly reflects income and is regularly used in keeping its books. The cash receipts and disbursements method (the cash method) generally is considered to clearly reflect income for Federal income tax purposes under present law, except where inventories are required to be kept.	(a) Any taxpayer with annual gross receipts from a business exceeding $5 million, computed on a 3-year moving average basis, would not be permitted to use the cash method of accounting for Federal income tax purposes. For businesses other than farming, use of the cash method also would be disallowed if another method of accounting has been used regularly to ascertain the income, profit or loss of the business for the purpose of reports or statements to shareholders, partners, other proprietors, beneficiaries, or for credit purposes. The proposal would apply in addition to the current law limitation on the use of the cash method with respect to a business in which inventory accounting is required.	(a) The cash method of accounting generally may not be used by any C corporation, partnership that has a C corporation as a partner, or tax-exempt trust with unrelated business income. Exceptions are made for farming businesses, qualified personal service corporations, and entities with average annual gross receipts of $5 million or less. Computation of average annual gross receipts is done on the basis of the 3 previous taxable years (not including the current taxable year).	(a) The cash method of accounting may not be used by any financial institution, bank for cooperatives, production credit association or finance company that is allowed to use the reserve method of computing losses from bad debts. (See VIII F below.)
	(b) An accrual basis taxpayer must accrue an amount as income when all the events have occurred which fix the right to receive such income and the amount can be determined with reasonable accuracy. An accrual basis recipient of services may not deduct the cost of such services prior to the time of economic performance.	(b) No provision.	(b) A taxpayer other than a financial institution or a utility is not required to accrue as income any amount to be received for the performance of services prior to the time the amount is billed. A taxpayer, other than a financial institution, is not required to accrue as income any amount to be received for the performance of services which, on the basis of experience, will not be collected, as long as unpaid balances do not bear interest or result in a late payment charge. An accrual basis recipient of services generally may not treat the services as economically performed prior to the time of billing.	(b) No provision.
		Effective date.—Taxable years beginning after December 31, 1985. The adjustment to income resulting from the change in tax accounting method would be recognized ratably over a period not to exceed 6 years beginning with the first tax year for which the proposal is effective.	*Effective date.*—Taxable years beginning after December 31, 1985. The adjustment to income resulting from the change in tax accounting method is recognized over a period not to exceed 5 years (not to exceed 10 years in the case of a hospital). Taxpayers may elect to continue to report income from loans, leases and transactions with related persons entered into before September 25, 1985, using the cash method.	*Effective date.*—Taxable years beginning after December 31, 1986. The adjustment to income resulting from the change in tax accounting method is recognized over a period not to exceed 5 years.

Item	Present Law	President's Proposal	House Bill	Senate Amendment
B. Simplified Dollar Value LIFO Method for Certain Small Businesses (sec. 901 of the House bill)	A taxpayer whose average annual gross receipts do not exceed $2 million may elect to use a single, dollar value LIFO inventory pool for any trade or business. Under regulations, a taxpayer using the dollar value LIFO method may use data published by the Bureau of Labor Statistics to construct an individualized index that estimates the annual change in prices for items in an inventory pool.	No provision	A taxpayer whose average annual gross receipts do not exceed $5 million may elect to use a simplified method of determining dollar value LIFO inventory values. The method establishes inventory pools in accordance with general categories of inventory items published by the Bureau of Labor Statistics and uses the change in the published index for the category to estimate the annual change in prices for inventory items in the pool. Repeals the rule which permits taxpayers to use a single, dollar value LIFO inventory pool for taxpayers who had not previously elected to use the single pool prior to the date of enactment. *Effective date.*—Taxable years beginning after December 31, 1985.	No provision.
C. Installment Sales (sec. 903 of the House bill and secs. 311-312 of the Senate amendment)	A taxpayer who sells property in exchange for deferred payments generally may report income on the installment method. Generally, under the installment method, gain is reported in proportion to the payments received on the outstanding installment obligations. Under Treasury regulations, a portion of sales made on a revolving credit plan are treated as installment sales eligible for reporting on the installment method.	*General rule.*—If an installment obligation is pledged for a loan, the proceeds of the loan generally would be treated as payment on the obligation, and a proportionate amount of deferred gain would be recognized. *Special rule for dealer property.*—If an installment obligation received for property sold in the ordinary course of a trade or business is pledged for a loan in the ordinary course of trade or business, the proceeds of the loan would trigger gain to the extent the loan proceeds exceed the basis of the obligation.	If an installment obligation is pledged for a loan, the proceeds of the loan are treated as a payment on the obligation, and a proportionate amount of deferred gain is recognized. An exception is provided for any installment payments that are due within 9 months regardless of the maturity of other payments on the obligation. For a taxpayer who sells property on a revolving credit plan, the amount eligible for the exception is that portion of the receivable balance that is determined (pursuant to a statistical sampling technique) to be paid in 9 months.	The use of the installment method is denied for a portion of sales of dealers (other than sales under revolving credit plans) and for a portion of sales of business or rental property the selling price of which exceeds $150,000. The disallowed portion is that portion that bears the same ratio to the total installment sales that the taxpayer's outstanding debt bears to the sum of the taxpayer's installment obligations and adjusted basis of the taxpayer's other assets.

Item	Present Law	President's Proposal	House Bill	Senate Amendment
C. Installment Sales (sec. 903 of the House bill and secs. 311-312 of the Senate amendment) (cont.)	The portion of sales made on a revolving credit plan that may be treated as sales eligible for installment reporting is that portion of the sales that contemplate payments being made in two or more installments and that are in fact paid for in two or more installments The determination of this portion is made on the basis of a statistical sample of the revolving credit accounts A revolving credit plan includes cycle budget accounts, flexible budget accounts, continuous budget accounts and other similar plans or arrangements under which the customer agrees to pay during each period of time for which a periodic statement of charges and credits is rendered, a part of the outstanding balance of the customer's account. If an installment obligation is disposed of, any deferred gain generally is recognized If an installment obligation is pledged as collateral for a loan, deferred gain generally is recognized only as payments are received on the obligation	*Subsequent payments.*—Payments by obligor on an installment obligation would trigger additional gain to the extent that the gain attributable to such payments exceeds gain recognized on account of the pledge. *Exceptions.*—Inapplicable to pledge of an obligation that by its terms is due within 12 months, or an obligation received under a revolving credit plan that contemplates all purchases would be paid for within 12 months Also inapplicable to pledges of obligations for debt that by its terma is payable within 90 days, provided that debt is not renewed or continued Also inapplicable to indebtedness owed to a financial institution and secured by a general lien on all of the borrower's trade or business assets, except if substantially all the borrower's assets are installment obligations. *Effective date.*—Applicable to obligations pledged after December 31, 1985. Any installment obligation pledged before January 1, 1986, would be treated as pledged on January 1, 1991, if still outstanding.	The provision does not apply to pledges of obligations for debt that by its terms is payable within 90 days, provided that the debt is not renewed or continued, and provided that the taxpayer does not issue additional debt within 45 days. Anti-avoidance rules are included subjecting a borrowing to the pledging rule if it is reasonable to expect that the lender took into account payments on the installment obligations as a source for payments on the indebtedness, but a safe harbor is provided where more than 50 percent of the taxpayer's assets are used in an active trade or business. *Effective date.*—Applicable to obligations pledged after December 31, 1985, and applicable to obligations created after September 25, 1985, if pledged for a debt obligation outstanding after December 31, 1985. The provision is phased in over 3 years for installment obligations arising from the sale of property in the ordinary course of business that are pledged in 1986, and phased in over 2 years for like installment obligations pledged in 1987. One residential condominium project is grandfathered	The provision does not apply to installment sales of personal use property and farm property In addition, personal use and farm property and indebtedness related to such property is not taken into account for purposes of applying the proportionate disallowance rule. An exception is provided for sales by a manufacturer to a dealer (a) where the term of the dealer's obligation is dependent upon the time that the property is resold or is rented by the dealer, (b) the manufacturer has the right to repurchase the property if the dealer does not resell or rent the property within a specified period, and (c) the amount of the manufacturer's installment obligations exceeds fifty percent of the manufacturer's sales to dealers Use of the installment method for sales made pursuant to a revolving credit plan and for sales of publicly traded property is eliminated Sales by dealers of certain timeshares and of residential lots, the development of which is not made by the seller of the lot, are eligible to elect to pay interest at the short-term Federal rate on the deferral of tax under the installment method and not be subject to the proportionate disallowance rule. *Effective date.*—The elimination of the installment method for sales on a revolving credit plan and for sales of publicly traded property is effective for sales of property after December 31, 1986 Taxpayers who sell property on a revolving credit plan and who may no longer use the installment method of accounting for revolving credit plans may include the resulting adjustment in income over a period not exceeding five years The proportionate denial of the installment method is effective as of January 1, 1987, with respect to sales made on or after March 1, 1986 Specified indebtedness of a particular taxpayer is not taken into account for purposes of applying the proportionate disallowance rule.

Item	Present Law	President's Proposal	House Bill	Senate Amendment
D. Capitalization Rules for Inventory, Construction, and Development Costs (sec. 905 of the House bill and sec. 302 of the Senate amendment) 1. Inventory	Manufacturers generally must accumulate costs of producing "inventory" goods in an inventory account Costs in the inventory account may be deducted only as the goods to which they relate are disposed of Under regulations, the "full absorption method" determines which costs are includible in inventory All direct production costs, including costs of materials incorporated into the product or consumed during production and labor directly involved in manufacturing, must be inventoried The treatment of indirect production costs varies according to the nature of the cost some costs are deductible; others are inventoriable; others ("financial conformity" costs) are deductible only if deducted by the taxpayer for financial reporting purposes. Purchasers of goods for resale (e g., wholesalers and retailers) must include in inventory the invoice price of the purchased goods plus transportation and other necessary costs incurred in acquiring possession.	Comprehensive capitalization rules (hereinafter, the "uniform capitalization rules") would apply to the manufacture of inventory goods. These rules essentially would parallel the full absorption rules, but would require that most financial conformity costs be inventoried In addition, all tax depreciation, current pension and fringe benefit costs, and a portion of general and administrative expenses would be treated as inventory costs. However, research and experimental costs (within the meaning of sec. 174) would not be subject to capitalization in the case of inventory. Special rules would apply to farmers (see IV.A.3). No special rules would apply to producers of timber *Effective date.*—Taxable years beginning after December 31, 1985. The section 481 adjustment would be spread ratably over a period of not more than 6 years under the rules applicable to a change in a method of accounting initiated by the taxpayer	Generally the same as the President's proposal *See*, IV.A 3. and IV B 1., respectively, regarding special rules (differing from those in the President's proposal) applicable to farmers and producers of timber *Effective date.*—Taxable years beginning after December 31, 1985. The section 481 adjustment is to be spread ratably over a period of not more than 5 years under the rules applicable to a change in a method of accounting initiated by the taxpayer	Same as House bill except that purchasers of goods for resale having average annual gross receipts in excess of $5 million generally are subject to the uniform capitalization rules Thus, costs (including general and administrative costs) attributable to purchasing, transporting, repackaging or other processing, and storage of goods, and other similar costs associated with the goods, are to be treated as inventory costs *See*, IV.A 3 and IV B 1, respectively, regarding exceptions from the uniform capitalization rules for farmers and producers of timber *Effective date.*—Taxable years beginning after December 31, 1986. Depreciation on property placed in service before March 1, 1986, is not subject to the new capitalization rules The section 481 adjustment is to be spread ratably over a period of not more than 5 years under the rules applicable to a change in a method of accounting initiated by the taxpayer
2. Self-constructed property and noninventory property produced for sale	The costs of acquiring, constructing, or improving buildings, machinery, equipment, or other assets having a useful life beyond the end of the taxable year are not currently deductible. These "capital expenditures" become part of the basis of the asset, and may be recoverable over the useful life of the property through depreciation or amortization deductions if the property is held for business or investment purposes. Any unrecovered basis may be offset against the amount realized if the property is sold Although a taxpayer's direct costs of constructing an asset for its own use or a noninventory asset produced for sale must be capitalized, the proper treatment of many indirect costs is uncertain	Cost (other than research and experimental costs) incurred in connection with construction of noninventory property and self-use property would be subject to the uniform capitalization rules. *Effective date.*—Costs incurred after December 31, 1985, unless incurred in connection with property on which substantial construction had begun on or before that date.	Costs (other than research and experimental costs) incurred in connection with construction of noninventory property and self-use property are subject to the uniform capitalization rules. *Effective date.*—Costs incurred after December 31, 1985	Same as House bill *Effective date.*—Costs incurred after December 31, 1986, unless incurred in connection with property on which substantial construction occurred before March 1, 1986

Item	Present Law	President's Proposal	House Bill	Senate Amendment
3. Interest	Interest is generally deductible when paid or incurred. However, interest incurred by a taxpayer during construction or improvement of real property to be held in a trade or business or activity for profit generally must be capitalized and amortized over 10 years	A taxpayer would be required to capitalize interest on debt incurred to finance the construction or production of (1) real property, and (2) long-lived personal property to be used by the taxpayer in a trade or business or an activity for profit, or (3) other tangible property requiring 2 or more years to produce or construct, or to reach a productive stage. *Effective date.*—Interest paid or incurred after December 31, 1985	A taxpayer must capitalize interest on debt incurred to finance the construction or production of (1) real property, (2) long-lived personal property, and (3) other tangible property requiring 2 or more years to produce or construct, or to reach a productive stage. Interest incurred to finance the construction or manufacture of property costing more than $1 million also must be capitalized if the property requires more than 1 year to produce. *Effective date.*—Interest paid or incurred after December 31, 1985 (with a targeted transitional rule).	Same as House bill, except long-lived personal property is subject to the interest capitalization rule only if it is to be used by the taxpayer in a trade of business or activity for profit (i e., is not held for sale). *Effective date.*—Interest paid or incurred after December 31, 1986, unless incurred with respect to property on which substantial construction began before March 1, 1986. Several targeted transitional rules apply
E. Long-Term Contracts (sec. 904 of the House bill and sec. 301 of the Senate amendment)	The treatment of costs of producing property under a "long-term contract" varies depending on the method of accounting used by the taxpayer. In addition to an inventory method (e.g., accrual shipment or accrual delivery) taxpayers may use one of two special methods of accounting for long-term contracts the percentage of completion method or the completed contract method Under the percentage of completion method, gross income is recognized according to the percentage of the contract completed during each taxable year, and contract costs are currently deductible Under the completed contract method, the gross contract price is included in income, and costs associated with the contract may be deducted, in the year that the contract is completed and accepted The rules relating to which costs are contract costs vary depending on whether the contract is an extended period contract (in general, a contract requiring longer than 2 years to complete) or a non-extended period contract. The rules applicable to extended period contracts are essentially the same as the uniform capitalization rules. Non-extended period contracts are subject to similar but somewhat less comprehensive rules.	All long-term contracts would be subject to the uniform capitalization rules, including the interest capitalization rule (see item D, above), unless reported on the percentage of completion method Moreover, additional general and administrative costs attributable to cost-plus contracts and to Federal government contracts requiring certification of costs would be treated as contract costs. *Effective date.*—Contracts entered into after December 31, 1985	All long-term contracts must be reported under the percentage of completion method. Thus, long-term contract costs are currently deductible to the extent attributable to contracts reported under the percentage of completion method Interest is payable by (or to) the taxpayer if the actual profit on the contract varies from the estimated profit used in reporting income. An exception is provided for contracts for the construction of real property to be completed within 2 years of the contract date, if performed by a taxpayer whose average annual gross receipts do not exceed $10 million Present law capitalization rules are retained for contracts not required to be reported under the percentage of completion method *Effective date.*—Contracts entered into after September 25, 1985.	In general, same as President's proposal, except present law is retained for real property construction contracts not requiring more than 2 years to complete, if performed by a taxpayer with average annual gross receipts of $10 million or less *Effective date.*—Contracts entered into on or after March 1, 1986

Item	Present Law	President's Proposal	House Bill	Senate Amendment
F. Reserves for Bad Debts (sec. 906 of the House bill and sec. 303 of the Senate amendment)	A taxpayer may take a deduction for losses on business debts under the "reserve method" (sec. 166(c)). The "reserve method" allows a current deduction for that portion of business debts currently owed the taxpayer which are expected to become uncollectible. A similar rule applies to debt that is guaranteed by a dealer in property where the debt arises from the sale of tangible property and related services in the ordinary course of business.	The use of the reserve method in computing the deduction for bad debts would be disallowed. Instead, deductions for bad debts would be allowed when specific loans become partially or wholly worthless (i.e., the "specific charge-off" method). Wholly worthless debts would have to be treated as worthless on a taxpayer's books in order for a deduction to be allowed for Federal income tax purposes, as is the case under present law for partially worthless debts. Present law would be retained on guarantees by a dealer in property. *Effective date.*—Taxable years beginning after December 31, 1985. The balance in any reserve for bad debts at that time would be included in income ratably over a 10-year period beginning with the first taxable year beginning on or after January 1, 1986.	The use of the reserve method in computing the deduction for bad debts is disallowed for all taxpayers other than commercial banks whose assets do not exceed $500 million and thrift institutions. Wholly worthless debts must be treated as worthless on a taxpayer's books in order for a deduction to be allowed for Federal income tax purposes, as is the case under present law for partially worthless debts. Present law is retained on deductions for reserves for guarantees by a dealer in property. *Effective date.*—Taxable years beginning after December 31, 1985. The balance in any reserve for bad debts at that time is included in income ratably over a five-year period beginning with the first taxable year for which the provision is effective.	The use of the reserve method in computing the deduction for bad debts is disallowed for all taxpayers other than financial institutions, banks for cooperatives, production credit associations and certain finance companies. Finance companies meeting a definitional test are allowed to use the reserve method of computing the deduction for bad debts only with regard to qualified indebtedness. Wholly worthless debts must be treated as worthless on a taxpayer's books in order for a deduction to be allowed for Federal income tax purposes, as is the case under present law for partially worthless debts. The use of the reserve method in computing the deduction for losses on debts guaranteed by a dealer is disallowed. *Effective date.*—Taxable years beginning after December 31, 1985. The balance in any bad debt or guarantee reserve at that time is included in income ratably over a five-year period beginning with the first taxable year for which the amendment is effective.

Item	Present Law	President's Proposal	House Bill	Senate Amendment
G. Taxable Years of Partnerships, S Corporations, and Personal Service Corporations (sec. 304 of the Senate amendment)	(a) *Partnerships* —A partnership may not adopt or change to a taxable year other than that of all of its principal partners unless it establishes, to the satisfaction of the Secretary of the Treasury, a business purpose for adopting or changing to a different taxable year If the principal partners have different taxable years, or if the partnership has no principal partners, the calendar year is used in place of the taxable year of all of the principal partners. Under a transitional rule to the above rules, a partnership that has previously made a valid election to use a taxable year different than that of all of its principal partners (or the calendar year) is not required to change its taxable year The Internal Revenue Service has indicated that a taxable year providing 3 months or less of deferral of income generally is accepted as satisfying the requirement that a different taxable year have a business purpose.	(a) No provision	(a) No provision	(a) *Partnerships* —A partnership is required to adopt the same taxable year as that of the partners owning a majority interest in partnership profits and capital If partners owning a majority of partnership profits and capital do not have the same taxable year, the partnership is required to adopt the taxable year of all of its principal partners. A partnership not covered by either of the above rules is required to adopt the calendar year A partnership may adopt a different taxable year if it establishes, to the satisfaction of the Secretary of the Treasury, a business purpose for doing so The present law rule that accepts as satisfying the business purpose requirement a taxable year that provides deferral of income of 3 months or less will no longer apply (Floor amendment by Senator Mitchell, adopted by voice vote.)
	(b) *S corporations.*—An S corporation may not adopt or change to a taxable year other than the calendar year unless it establishes, to the satisfaction of the Secretary of the Treasury, a business purpose for adopting or changing to a different taxable year. Under a transitional rule to the above rules, an S corporation having previously made a valid election to use a taxable year other than the calendar year is not required to change its taxable year. The Internal Revenue Service has indicated that a taxable year providing 3 months or less of deferral of income generally is accepted as satisfying the requirement that a different taxable year have a business purpose.	(b) No provision.	(b) No provision	(b) *S corporations.*—All S corporations are required to adopt the calendar year as the taxable year, unless the S corporation establishes, to the satisfaction of the Secretary of the Treasury, a business purpose for using a different taxable year. The present law rule that accepts as satisfying the business purpose requirement a taxable year that provides deferral of income of 3 months or less will no longer apply (Floor amendment by Senator Mitchell, adopted by voice vote)
	(c) *Personal service corporations.*—A personal service corporation, other than an S corporation, is allowed to adopt the taxable year of its choice, as long as that taxable year conforms with its annual accounting period	(c) No provision.	(c) No provision.	(c) *Personal service corporations* —All personal service corporations are required to adopt the calendar year, unless the corporation establishes, to the satisfaction of the Secretary of the Treasury, a business purpose for using a different taxable year

Item	Present Law	President's Proposal	House Bill	Senate Amendment
G. Taxable Years of Partnerships, S Corporations, and Personal Service Corporations (cont.)				The deferral of income for three months or less does not constitute a business purpose. (Floor amendment by Senator Mitchell, adopted by voice vote.) *Effective date.*—Taxable years beginning after 1986. Partners of partnerships and shareholder of S corporations that are required to include items from more than one taxable year of the partnership or S corporation in any taxable year will take the net income of any short taxable year into account ratably over 4 years. An election to include all such income in the first taxable year is provided. Personal service corporations required to change their taxable years must annualize the income for that year.
H. Special Treatment of Certain Items 1. Qualified Discount Coupons (sec. 321 of the Senate amendment)	An accrual-basis taxpayer may elect to deduct the cost of redeeming "qualified discount coupons" outstanding at the close of the taxable year and received for redemption up to 6 months following the close of the taxable year (sec. 466). A "qualified discount coupon" is one which is issued and redeemable by the taxpayer and which allows a discount of not more than $5 on the purchase price of merchandise or other tangible personal property. For the first year to which an election applies, a special rule delays a portion of the deduction attributable to the election to prevent a bunching of deductions.	The election to deduct the cost of redeeming "qualified discount coupons" received after the close of the taxable year would be repealed. Any portion of the delayed deduction from the first year of election, which has not yet been allowed as a deduction, would be deductible in the first taxable year for which the proposal is effective. *Effective date.*—The proposal would be effective for taxable years beginning after December 31, 1985.	No provision.	Same as President's proposal. Any adjustment required to be made as a result of the change in method of accounting will be reduced by the amount of any suspense account and included in income over a period not to exceed five taxable years. *Effective date.*—Taxable years beginning after December 31, 1986.
2. Utilities using accrual accounting (sec. 322 of the Senate amendment)	Utilities using the accrual method of accounting are allowed to defer the recognition of income attributable to services provided to customers during the taxable year, but after the last meter reading date occurring within the taxable year.	No provision.	No provision	Accrual basis providers of utility services are required to recognize income attributable to the furnishing or sale of utility services to customers not later than the taxable year in which such services are provided. The adjustment to income resulting from the change in accounting method is recognized ratably over four years. *Effective date.*—Taxable years beginning after December 31, 1986.

Item	Present Law	President's Proposal	House Bill	Senate Amendment
3. Contributions in aid of construction (sec. 908 of the House bill)	A regulated public utility that provides electric energy, gas, water or sewage disposal services may treat contributions received in aid of construction as nontaxable contributions to capital.	No provision.	The bill repeals the provision of present law allowing contributions in aid of construction to be treated as nontaxable contributions to capital. *Effective date.*—Contributions received after December 31, 1985.	No provision
4. Discharge of indebtedness of solvent taxpayers (sec. 323 of the Senate amendment)	Solvent taxpayers who would otherwise be required to currently recognize income from the discharge of qualified business indebtedness may elect to reduce the basis of depreciable property instead of currently recognizing such income.	No provision.	No provision	The election for solvent taxpayers to reduce the basis of depreciable property rather than currently recognize income from the discharge of qualified business indebtedness is repealed. No change is made in the treatment of discharges of indebtedness that occur in title 11 (bankruptcy) cases or when a taxpayer is insolvent. *Effective date.*—Discharges of indebtedness occurring after December 31, 1986.

Item	Present Law	President's Proposal	House Bill	Senate Amendment
A. Reserves for Bad Debts 1. Commercial banks (sec. 801(a) of the House bill)	Commercial banks are allowed to deduct loan losses prior to the time that loans become wholly or partially worthless using either of two reserve methods (1) the experience method, and (2) the percentage of eligible loans method. The availability of the percentage of eligible loans method is scheduled to expire for taxable years beginning after 1987. If the bad debt deduction computed under the percentage of eligible loans method exceeds the deduction that would have been allowed under the experience method, then the deduction is reduced by 20 percent of such excess.	The use of both the experience and percentage of eligible loans methods would be repealed. Deductions for bad debts would be allowed when the loans are partially or wholly worthless (i.e., the "specific charge-off" method). *Effective date.*—Taxable years beginning after 1985. The existing balance in the reserve for bad debts as of the effective date would be included in income ratably over a 10-year period, starting with the first taxable year beginning after 1985. Banks could elect to include the entire reserve balance in income in the first taxable year beginning after 1985.	The use of the experience and percentage of eligible loans methods is repealed for banks with assets in excess of $500 million. Thus, deductions for bad debts would be allowed when the loans are partially or wholly worthless (i.e., the "specific charge-off" method). Present law is retained for other banks. *Effective date.*—Taxable years beginning after 1985. The existing reserve balance on the effective date is to be included in income ratably over a 5-year period starting with the first taxable year beginning after 1985. Taxpayers could elect the amount to be recaptured in the first taxable year beginning after 1985, and ratably recapture the balance over the next 4 years. Taxpayers could also elect to account for existing loans using a "cutoff" method.	No provision.
2. Thrift institutions (sec. 801(b) of the House bill and sec. 801 of the Senate amendment)	Thrift institutions may deduct loan losses, prior to the time that loans become wholly or partially worthless, using the reserve methods available to banks (the "experience" and "percentage of eligible loans" methods) or the "percentage of taxable income" method, which is available only to thrifts. The percentage of eligible loans method is scheduled to expire for taxable years beginning after 1987. Under the percentage of taxable income method, an annual deduction is allowed for 40 percent of taxable income if 82 percent of the thrift's assets are qualified (72 percent for mutual savings banks without stock). The deduction phases down to zero when less than 60 percent of the thrift's assets are qualified (50 percent for mutual savings banks without stock). Qualified assets include home mortgage loans and certain other assets.	Use of the experience, percentage of eligible loans, and percentage of taxable income methods would be repealed. Deductions for loan losses would be allowed when the loans are partially or wholly worthless (i.e., the "specific charge-off" method).	Thrift institutions using the reserve method to compute their losses on bad debts may use the experience method allowed commercial banks under present law or the percentage of taxable income method with the percentage reduced from 40 percent to 5 percent. An institution must hold at least 60 percent of its assets as qualifying assets to be considered a "thrift institution" for this purpose.	Thrift institutions using the reserve method to compute their losses on bad debts may use the experience method allowed commercial banks, the percentage of eligible loans method allowed commercial banks (until its scheduled expiration) or the percentage of taxable income method with the percentage reduced from 40 percent to 25 percent. The deduction of 25 percent of taxable income is allowed only if 82 percent of the thrift's assets are qualified (72 percent for mutual savings banks without stock). The percentage of taxable income allowed as a deduction is reduced by one-half of one percentage point (by one percentage point for mutual savings banks) for each percent by which the thrift fails to hold the percentage qualified assets necessary to receive the maximum percentage deduction. No deduction under the percentage of income method is allowed when less than 60 percent of the thrift's assets are qualified (50 percent for mutual savings banks.)

Item	Present Law	President's Proposal	House Bill	Senate Amendment
2. Thrift institutions (cont.)	If the bad debt deduction computed under either the percentage of eligible loans method or the percentage of taxable income method exceeds the deduction that would have been allowed under the experience method, then the deduction is reduced by 20 percent of such excess.		The bad debt deduction under the percentage of taxable income method is not reduced by reason of it exceeding the deduction allowable under the experience method	The bad debt deduction allowed under either the percentage of eligible loans method or the percentage of taxable income method is reduced by 20 percent of the excess of such amount over the deduction that is allowed under the experience method.
		Effective date. Taxable years beginning after 1985. The portion of the bad debt reserve on the effective date which is equal to the greater of the reserve balance computed under the experience and percentage of eligible loans methods would be included in income ratably over a 10-year period starting with the first taxable year beginning after 1985. Taxpayers could elect to include the entire recapture amount in the first taxable year beginning after 1985.	*Effective date.*—Taxable years beginning after 1985	*Effective date* —Taxable years beginning after 1986

Item	Present Law	President's Proposal	House Bill	Senate Amendment
3. Interest on Debt Used to Purchase or Carry Tax-Exempt Obligations (sec. 802 of the House bill)	No deduction is allowed for interest payments on debt incurred or continued to purchase or carry tax-exempt obligations. Under a long-standing judicial and administrative interpretation, financial institutions generally are permitted to invest deposited funds in tax-exempt obligations, while continuing to deduct interest paid to depositors. The corporate tax preference rules reduce by 20 percent the amount which may be deducted by financial institutions for interest on funds allocable to tax-exempt obligations acquired after 1982. The portion of funds allocable to tax-exempt obligations is deemed to be equivalent to the ratio of— (1) the average annual adjusted basis of tax-exempt obligations acquired after 1982 and held by the financial institution, to (2) the average annual adjusted basis of the financial institution's total assets.	Denies financial institutions 100 percent of interest deductions that are allocable to tax-exempt obligations acquired on or after January 1, 1986. The amount of interest allocable to tax-exempt obligations would be determined in the same manner as for purposes of the tax preference reduction under present law. The present law (i.e., 20 percent) reduction would continue to apply with respect to tax-exempt obligations acquired in 1983 through 1985.	Denies financial institutions 100 percent of interest deductions that are allocable to tax-exempt obligations acquired on or after January 1, 1986. The amount of interest allocable to tax-exempt obligations is determined in the same manner as for purposes of the tax preference reduction under present law. The present law (i.e., 20 percent) reduction continues to apply with respect to tax-exempt obligations acquired in 1983 through 1985. Tax-exempt obligations that (1) are acquired pursuant to a written commitment that was entered into before September 25, 1985 or (2) are qualified tax-exempt obligations acquired during calendar years 1986, 1987 or 1988, are treated as having been acquired before January 1, 1986. A qualified tax-exempt obligation is an essential function tax-exempt bond designated by an issuer (in existence on October 3, 1985) that is either a tax anticipation note with a term not exceeding one year or part of an issue to provide qualified project financing that does not exceed $3 million. Not more than $10 million of aggregated obligations may be designated by any issuer during any calendar year. The interest disallowance rule is to be applied before the rules requiring the capitalization of interest in connection with the manufacture or construction of property. (See VIII D.3.)	Retains present law.
Net Operating Losses of Financial Institutions (sec. 803 of the House bill and sec. 802 of the Senate amendment)	Commercial banks and thrift institutions may carry net operating losses back to the preceding ten taxable years and forward to the succeeding five taxable years. This contrasts with the general rule for other taxpayers allowing a net operating loss to be carried back to the preceding three taxable years and forward to the succeeding 15 taxable years.	The carryback and carryforward rules applicable to commercial banks and thrift institutions would be repealed. Commercial banks and thrift institutions would carryback and carryforward net operating losses under the general rule applicable to other taxpayers (3-year carryback; 15-year carryforward). *Effective date.*—Net operating losses incurred in taxable years beginning on or after January 1, 1986. Net operating losses incurred in earlier years would continue to be subject to the rules of present law.	Same as President's proposal. *Effective date.*—Net operating losses incurred in taxable years beginning on or after January 1, 1986. Net operating losses incurred in earlier years would continue to be subject to the rules of present law.	Generally retains present law. Net operating losses incurred by a thrift institution in taxable years beginning after 1981 and before 1986 may be carried forward to the succeeding eight taxable years (rather than five taxable years). *Effective date.*—Date of enactment.

	Present Law	President's Proposal	House Bill	Senate Amendment
D. Reorganizations of Financially Troubled Thrift Institutions (sec. 801 of the House bill)				
1. Qualification for tax-free status	Continuity of proprietary interest is generally a prerequisite to qualification of a transaction as a tax-free reorganization. Thus, the equity owners of the acquired corporation must retain a substantial continuing interest in the acquiring corporation. The Code contains a special provision under which a merger of a financially troubled thrift institution into another corporation may qualify as a reorganization even though continuity of proprietary interest is absent.	The special rules relating to qualification of an acquisition of a financially troubled thrift institution as a tax-free reorganization would be repealed. *Effective date.*—Acquisitions on or after January 1, 1991	Same as President's proposal *Effective date*—Acquisitions on or after January 1, 1986.	No provision
2. Net operating losses	The rules limiting use of an acquired corporation's net operating loss carryovers by the acquiring corporation are relaxed in certain situations for troubled thrift reorganizations	The special treatment of net operating losses in a troubled thrift reorganization would be repealed. *Effective date.*—Acquisitions on or after January 1, 1991.	The special treatment of net operating losses in a troubled thrift reorganization is repealed. (See VI H.6 b., above). *Effective date.*—Acquisitions on or after January 1, 1986.	Generally retains present law for net operating loss carryovers of troubled thrift reorganizations (See VI H 6 b., above)
3. FSLIC payments	Payments received by certain financially troubled thrift institutions from the Federal Savings and Loan Insurance Corporation (FSLIC) are not income to the recipient and are exempt from the general requirement that a taxpayer's basis in its assets be reduced by nonshareholder contributions to capital	The special rules relating to the exclusion from income, or exemption from the basis reduction requirement, of FSLIC payments to troubled thrift institutions would be repealed. *Effective date.*—Payments on or after January 1, 1991	The special rules relating to the exclusion from income, or exemption from the basis reduction requirement, of FSLIC payments to troubled thrift institutions are repealed. *Effective date.*—Payments on or after January 1, 1986. In addition, present law is clarified by providing that FSLIC payments to financially troubled thrift institutions exempt under the present-law exclusion are not subject to the provision disallowing expenses attributable to such payments.	No provision.
E. Losses on Deposits in Insolvent Financial Institutions (sec. 805 of the House bill and sec. 803 of the Senate bill)	A loss realized by a taxpayer with respect to a deposit or account in a financial institution is deductible in the year in which it is determined that there is no prospect of recovery, in the same manner as any other type of bad debt loss. Unless the deposit was created in connection with a trade or business of the taxpayer, the loss is treated as a short-term capital loss, the deduction of which is limited under the Code.	No provision.	Individuals may elect to deduct losses on deposits or accounts in certain types of financial institutions as a casualty loss at the time the loss can be reasonably estimated. The election applies only where the loss arises as a result of the bankruptcy or insolvency of the financial institution. *Effective date.*—Losses in taxable years after December 31, 1982	Same as House bill

Item	Present Law	President's Proposal	House Bill	Senate Amendment
A. Insurance Products 1. Exclusion for interest on installment payments of life insurance proceeds (sec. 1001 of the House bill and sec. 1001 of the Senate amendment)	A beneficiary of a life insurance policy may receive installment payments of the proceeds of the policy. Amounts in the nature of interest (up to $1,000 annually) on the unpaid proceeds of the policy paid to the surviving spouse of the insured are not included in the spouse's income.	No provision	Repeals the $1,000 annual exclusion for the amounts in the nature of interest received by the surviving spouse of an insured. *Effective date.*—The provision generally is effective for amounts received by a beneficiary with respect to deaths occurring after December 31, 1985.	Same as House bill, except that the provision requires the use of sex neutral mortality tables for purposes of determining the amounts in the nature of interest. *Effective date.*—The provision generally is effective for amounts received by a beneficiary with respect to deaths occurring after December 31, 1986.
2. Structured settlements (sec. 1003 of the House bill and sec. 1002 of the Senate amendment)	Present law excludes from income the amount of any damages received on account of personal injuries or sickness, whether by suit or agreement and whether as a lump sum or as periodic payments. The person liable to pay the damages may assign to a third party (a structured settlement company) the obligation to pay the periodic payments. The portion of the amount received by that third party for agreeing to the assignment that is used to purchase assets to fund the liability is not included in the third party's income. The overall effect of these rules is that no taxpayer is subject to tax on the investment income earned on assets used to fund the periodic payment of damages for personal injuries.	Under the President's proposal, third-party assignees of liabilities to make periodic personal injury damage payments would include the full amount of consideration received from the assignor in gross income. An assignee purchasing an annuity contract to fund its liabilities to an injured party would be treated as the owner of the annuity and would be taxed on the income component of all amounts paid to it under the terms of the annuity contract. The assignee would be given an election concerning the tax treatment (i.e., the timing of its deduction), and if the taxpayer makes the election, its basis in the annuity is not reduced by the deduction. *Effective date.*—The proposal would be effective for all assignments entered into after December 31, 1985.	Retains present law, but limits the exclusion for structured settlement agreements to cases involving physical injury or sickness. *Effective date.*—Assignments entered into after December 31, 1985.	Same as President's proposal. *Effective date.*—Assignments entered into after December 31, 1986.
3. Policyholder loans (sec. 1003 of the Senate amendment)	Life insurance policies often permit the policyholder to borrow up to the cash surrender value of the policy. Until repaid, the policyholder loan reduces the proceeds payable to the policyholder in the event of a surrender of the policy or to the beneficiaries in the event of the death of the policyholder. Under present law, policyholder loans generally are treated as loans and not as withdrawals from the policy. Interest paid on policyholder loans generally is deductible by the policyholder. No deduction is allowed for amounts paid or accrued on indebtedness incurred or continued to purchase or carry a single premium life insurance contract.	The President's proposal did not recommend any specific changes relating to the tax treatment of policyholder loans. However, the President's proposal would generally limit the deduction for nonbusiness interest to the sum of net investment income, interest on debt secured by the taxpayer's principal residence (up to its value), and $5,000. *Effective date.*—The nonbusiness interest limitation generally would be effective (subject to two phase-in rules) for interest expense paid or incurred after December 31, 1985.	No statutory provision, but restates present-law rule that no amount paid or accrued on indebtedness incurred or continued to purchase or carry a single premium life insurance contract is deductible. (See, also, Nonbusiness interest limits, item V C., above.)	Provides that a deduction for interest on policyholder loans is not allowed in the case of loans aggregating more than $50,000 per officer, employee, or owner of an interest in a trade or business carried on by the taxpayer. (See also, Nonbusiness interest limits, item V C. above.) (Floor amendment by Senator Dole, adopted by voice vote. *Effective date.*—The provision is effective for interest on loans under policies purchased after June 20, 1986.

Item	Present Law	President's Proposal	House Bill	Senate Amendment
4. **Treatment of policies to cover prearranged funeral expenses (sec. 1825 of the Senate amendment)**	A life insurance contract generally is defined as a contract which meets either (1) a cash value accumulation test, or (2) a test consisting of a guideline premium requirement and a cash value corridor requirement. Future increases in death benefits may cause a contract not to qualify under these tests	No provision	No provision	Provides that future increases in death benefits may be taken into account in determining whether the definition of life insurance contracts is satisfied with respect to certain policies to cover prearranged funeral expenses Such contracts can qualify as a life insurance contract if the initial death benefit is $5,000 or less (treating all contracts issued to the same contract owner as one contract), and if the contract provides for fixed annual increases in the death benefit not exceeding 10 percent of the initial death benefit or 8 percent of the death benefit at the end of the preceding year (Floor amendment by Senator Long, adopted by voice vote)
5. **Deduction for policyholder losses (sec. 1002 of the House bill)**	A taxpayer generally may deduct a loss sustained during the taxable year and not compensated for by insurance or otherwise. The casualty loss deduction is allowable only to the extent that the losses exceed 10 percent of the taxpayer's adjusted gross income (AGI). If a casualty or other event occurs which results in a claim for reimbursement with respect to which there is a reasonable prospect of recovery (such as an insurance claim), then the loss may not be deducted until it can be ascertained with reasonable certainty that the reimbursement will not be received Some recent cases have held that the deduction is allowable when an individual has insurance coverage on nonbusiness property, but elects not to file a claim	Under the President's proposal, taxpayers suffering losses covered by insurance would be permitted to elect to claim a deduction with respect to those losses without regard to the prospect of recovery from the insurance company. Insurance proceeds would be taxable income when received to the extent of any portion of the loss that was previously deductible. Present law would continue to apply to nonelecting taxpayers. *Effective date.*—The proposal would be effective for all losses incurred in taxable years beginning after December 31, 1985, that are insured under policies issued after December 31, 1985.	Retains present law, but the casualty loss deduction is denied to the extent that an individual has insurance coverage on nonbusiness property and elects not to file a claim. *Effective date.*—The provision is effective for taxable years beginning after December 31, 1985.	No provision. *Effective date* —Contracts issued after December 31, 1984

Item	Present Law	President's Proposal	House Bill	Senate Amendment
B. Life Insurance Companies 1. Special life insurance company deduction (sec. 1011 of the House bill and sec. 1011 of the Senate amendment)	A life insurance company is taxed at corporate rates on its life insurance company taxable income (LICTI). A life insurance company is allowed a special life insurance company deduction of 20 percent of its tentative LICTI (LICTI in excess of the small company deduction) for any taxable year. This deduction has the effect of reducing the tax rates imposed on LICTI. General corporate tax rates apply to LICTI after reduction by the deduction.	The special deduction would be repealed *Effective date.*—Taxable years beginning after December 31, 1985.	Same as President's proposal. *Effective date.*—Taxable years beginning after December 31, 1985	Same as House bill and President's proposal *Effective date.*—Taxable years beginning after December 31, 1986 A special rule provides that, in the case of a life insurance company owning the stock of another corporation, which stock was acquired on January 14, 1981, income, gain, loss, or deduction attributable to the ownership of such stock is taken into account at present law rates, before calculation of the small company deduction. Such items are taken into account at the rate of 46/36.8, which provides the same tax benefit to the life insurance company as is provided under present law (Floor amendment by Senator Metzenbaum, adopted by voice vote.)
2. Tax-exempt organizations engaged in insurance activities (sec. 1012 of the House bill)	For certain tax-exempt organizations, the provision of insurance benefits to members or to the general public forms the basis for the organization's exemption from Federal income tax.			
a. Charitable organizations (sec. 501(c)(3)) and social welfare organizations (sec. 501(c)(4))	(a) A charitable organization directly engaged in providing insurance generally would be considered to be conducting a commercial activity which benefits a private, rather than public, interest and would not be entitled to tax exemption. Past IRS policy has permitted certain organizations, whose principal activities are providing life insurance, health insurance, and annuities to be treated as tax exempt. An organization is entitled to tax exemption if it is operated exclusively for the promotion of social welfare. Some health insurance providers have been treated as tax-exempt social welfare organizations.	(a) No provision	(a) Under the bill, a charitable or social welfare organization is not entitled to tax-exempt status unless no substantial part of its activities consists of providing commercial-type insurance. Commercial-type insurance does not include (1) insurance provided at less than cost to a class of charitable recipients, (2) health insurance provided by a health maintenance organization that is incidental to the organization's principal activity of providing health care, and (3) property and casualty insurance (such as fire insurance) provided by a church or convention of churches solely for such church or convention. The bill authorizes Treasury regulations providing special treatment with respect to the activities of Blue Cross and Blue Shield, relating to high-risk individuals and small groups	(a) No provision
b. Fraternal beneficiary societies (sec. 501(c)(8))	(b) A fraternal beneficiary society, order, or association that is operating under the lodge system, and providing for the payment of life, sick, accident, or other benefits to the members of such society, order, or association or their dependents, is entitled to tax exemption	(b) No provision.	(b) The bill requires a study of fraternal beneficiary societies by the Treasury Department, to be reported to the Congress by January 1, 1988. *Effective date.*—The provision generally is effective for years beginning after December 31, 1985. A special rule provides that the provision does not apply with respect to the pension business of Mutual of America. A delayed effective date is provided for the pension business of TIAA-CREF so that the provision does not apply to that portion of its business until January 1, 1988.	(b) No provision

Item	Present Law	President's Proposal	House Bill	Senate Amendment
3. Treatment of electing mutual life insurance company (sec. 1013 of the Senate amendment)	A mutual life insurance company may elect to treat all its individual noncancellable (or guaranteed renewable) accident and health insurance contracts as cancellable, for purposes of determining whether the company is taxable as a life insurance company or a property and casualty insurance company. As a condition of making this election, all stock life insurance company affiliates of an electing mutual life insurance company which is the common parent of the group are treated as mutual life insurance companies subject to tax under all provisions of the Code applicable to mutual life insurance company, including the provisions regarding the differential earnings amount of mutual companies.	No provision	No provision.	The requirement that stock life insurance company affiliates of an electing mutual life insurance company common parent are treated as mutual life insurance companies is repealed. (A floor amendment by Senator Metzenbaum, adopted by voice vote, provides that the repeal is effective only for taxable years beginning after December 31, 1985, and before January 1, 1992.)
4. Physicians' and surgeons' mutual protection associations (sec. 1031 of the Senate amendment)	In general, the gross income of a mutual insurance company (other than life insurance company) includes gross premiums and other consideration, gross investment income, and gain from the sale or other disposition of property. Present law provides a special deduction for dividends and similar distributions paid to policyholders in their capacity as such. In the case of corporations, gross income does not include any contribution to capital (sec. 118). However, the provisions covering the taxation of nonlife mutual insurance companies have no specific provisions regarding paid in capital or the distribution of such capital. Under present law, premiums for liability insurance in carrying on any trade or business are deductible in the year they are paid or incurred. For example, premiums paid by a physician for medical malpractice insurance generally are deductible. However, no deduction is allowed as an expense paid or incurred during the taxable year for a contribution to capital.	No provision	No provision.	Contributions to a pooled malpractice insurance association are currently deductible to the extent they do not exceed the cost of a commercial insurance premium and are included in the association's income. Refunds of such contributions are deductible to the fund only to the extent included in income of the recipient. The provision applies to associations operating under State law prior to January 1, 1984. (Floor amendment by Senator Matsunaga, adopted by voice vote.) *Effective date*.—Contributions and refunds after the date of enactment.

Item	Present Law	President's Proposal	House Bill	Senate Amendment
5. **Operations loss deduction of insolvent companies (sec. 1013 of the House bill and sec. 1012 of the Senate amendment)**	The Life Insurance Company Tax Act of 1984 repealed the deduction for additions to a policyholders surplus account (PSA), which was originally adopted to provide a cushion of assets to protect the interests of the policyholders However, a stock life insurance company is required to include in income any amount deemed to be distributed from an existing PSA	No provision	A life insurance company is permitted to apply its current loss from operations and its unused loss carryovers to offset taxable income from amounts deemed distributed from its policyholder surplus account (PSA) if (1) the company was insolvent on November 15, 1985, (2) the company is liquidated pursuant to a court order in a title 11 or similar case, and (3) as a result of the liquidation, the company's tax liability would be increased due to distributions from the PSA. *Effective date*.—The provision applies to liquidations on or after November 15, 1985	Same as House bill *Effective date*.—Same as House bill.
C. Property and Casualty Insurance Companies 1. **Treatment of acquisition expenses (sec. 1021 of the House bill and sec. 1021 of the Senate amendment)**	A property and casualty insurance company may generally deduct incurred premium acquisition expenses, even though taxation of the associated premium income may be deferred, by means of the unearned premium reserve deduction, to the period to which the premium income relates.	Unearned premiums would be subject to the QRA proposal (see loss reserve discounting, item 3, below).	Includes in income of a property and casualty company 20 percent of the increase (if any) in the unearned premium reserve. Also includes in income, ratably over 5 years, 20 percent of the company's unearned premium reserve at the beginning of the year in which the provision is first effective. *Effective date*.—The provision is effective for taxable years beginning after December 31, 1985.	Includes annually in income of a property and casualty company 20 percent of the increase (if any) in the unearned premium reserve. Also includes in income, ratably over 7½ years, 20 percent of the company's unearned premium reserve at the beginning of the year in which the provision is first effective A company that ceases to be subject to tax as a property and casualty insurance company must include the amount not yet included in income under this provision. For this purpose, the unearned premium reserve does not include life insurance reserves With respect to insurance against default in the payment of principal or interest on securities with a maturity of 5 years or more, the amount included in income is 10 percent of the increase (if any) in the unearned premium reserve, and 10 percent, ratably over 7½ years, of the company's unearned premium reserve at the beginning of the taxable year in which the provision is first effective. *Effective date*.—The provision is effective for taxable years beginning after December 31, 1986

2. Treatment of tax-exempt income (sec. 1022 of the House bill)	No special treatment applies to the tax-exempt income of a property and casualty insurance company	No special rule would apply to tax-exempt income other than the effect on tax-exempt income of the QRA proposal (see item 3, below)	Reduces deductions for loss reserves by 10 percent (15 percent for taxable years beginning after December 31, 1987) of the sum of (i) tax-exempt interest income and (ii) the deductible portion of dividends received Provides an exception for interest and dividends received or accrued on investments acquired before November 15, 1985 *Effective date* —The provision is effective for taxable years beginning after December 31, 1985.	No provision.
3. Treatment of loss reserves (sec. 1027 of the House bill and sec. 1022 of the Senate amendment)	A property and casualty insurance company may deduct from its gross income the increase in losses incurred during the year Losses incurred include unpaid losses and losses that have been incurred but not reported ("IBNR" losses), which represents the full amount of actual and estimated insurance losses it expects to pay The deduction is allowed in the year the losses are incurred or estimated to have been incurred, rather than the year in which they are paid or have accrued under generally applicable principles of tax accounting This loss reserve deduction rule does not take account of the difference between the time the reserve for losses incurred is established (i.e., the year in which the event covered by insurance occurs) and the time when the items are released from the reserve (i.e., the year in which claims are satisfied or otherwise extinguished). Present law treatment of reserves of a title insurance company is unclear	A property and casualty insurance company's deduction for unearned premiums, and for unpaid losses with respect to a line of business, during a taxable year would be limited to the amount it credits to a qualified reserve account ("QRA"). If the total amount credited to a QRA exceeds the statutory reserves for the line of business for which the QRA is established in any year, the excess must be currently included in the company's income The President's proposal is equivalent to after-tax discounting of reserve deductions to reflect the time value of money This is accomplished by increasing each QRA reserve annually by a percentage equal to the after-tax rate of return earned by the company on its investments during that year No additional reserve deduction would be allowed for this annual increase in the reserve accounts A company would be allowed a deduction each year for the full amount paid to satisfy claims, but would be required to include in taxable income an equivalent amount released from the appropriate QRA Thus, if the reserve was insufficient to cover all claims, the excess claims would produce a net deduction when paid *Effective date* —The proposal would be effective for all losses incurred in taxable years beginning after December 31, 1985, that are insured under policies issued after December 31, 1985.	Requires the Secretary of the Treasury (in consultation with the Joint Committee on Taxation) to submit to the Congress a study of the treatment of loss reserves This study is due not later than January 1, 1987	Requires pretax discounting of unpaid loss and loss adjustment expense reserves The provision applies to loss reserves, including accident and health reserves, for each property and casualty line of business of all insurance companies (provided such reserves are not subject to discounting under life insurance company rules) The interest rate to be applied is 5 percent for accident years beginning before or in 1987, and 75 percent of a 5-year rolling average of the annual Federal mid-term rate thereafter. A loss payment pattern, based on insurance company annual statement data, is determined for each line of business every 5 years starting with 1987, and promulgated by the Treasury. A special rule for long-tail lines of business provides that the payment pattern is generally deemed to be the number of years for which annual statement data is available, but may be expanded an additional 5 years A company is permitted to elect in each 5-year period to discount based on its own loss payment pattern, except for international and reinsurance lines of business Reserves of title insurance companies (in an amount not in excess of loss reserves) are subject to the discounting rules, rather than the rule applicable to unearned premiums (item 1, above). *Effective date*.—The provision is effective with respect to changes in loss reserves for taxable years beginning after December 31, 1986, with special treatment for reserve strengthening after March 1, 1986 The rules are implemented on a fresh-start basis, providing a forgiveness of income in the amount of the reduction in reserves resulting from the implementation of discounting

4. **Treatment of net gain from operations (sec. 1023 of the House bill)**	No special provision of present law requires that the taxable income of a property and casualty insurance company bear a relationship to its net gain from operations as reported on its annual statement for financial accounting purposes	No provision	Requires that the taxable income of a property and casualty company must bear a relationship to the company's net gain from operations (as reported on the company's annual statement for financial accounting purposes). This rule provides that regular taxable income of a property and casualty insurance company is not less than 20/36 of its adjusted net gain from operations, and its regular taxable loss is not more than 20/36 of its adjusted net loss from operations, as set forth in its annual statement. Tax-exempt income and the deductible portion of certain dividends received attributable to investments made before November 15, 1985, are excluded from adjusted net gain or loss from operations Pre-effective date loss carryovers may not be applied against post-effective date income, and consolidated taxable income of property and casualty members of an affiliated group is generally determined separately before being taken into account in determining consolidated taxable income of the entire consolidated group. *Effective date.*—The provision is effective for taxable years beginning after December 31, 1987.	No provision
5. **Limiting policyholder dividend deduction for mutual companies (sec. 1026 of the House bill)**	Under present law, property and casualty insurance companies (whether stock or mutual) are generally permitted to deduct dividends and similar distributions paid or declared to policyholders in their capacity as such. Stock companies may not, however, deduct dividends paid to shareholders. This distinction between policyholder and shareholder dividends also exists in the case of life insurance companies, but deductible policyholder dividends paid by mutual life insurance companies are reduced by an amount intended to reflect the portion of the distribution allocable to the companies' earnings and profits (as distinguished from the portion that is a policyholder rebate).	The President's proposal would require the deduction for policyholder dividends of mutual property and casualty companies to be reduced in a manner similar to the reduction applicable to mutual life insurance companies. The proposal states that additional study is needed to determine the size of the competitive advantage that the current treatment of policyholder dividends provides to mutual property and casualty companies and to set the appropriate deduction limitation. *Effective date.*—The proposal would be effective for taxable years beginning after December 31, 1985	Requires the Secretary of the Treasury to submit to the Congress a study of the treatment of policyholder dividends by mutual property and casualty insurance companies and whether any changes in such treatment would be appropriate. This study is due not later than January 1, 1987	No provision

Item	Present Law	President's Proposal	House Bill	Senate Amendment
6. Protection against loss account for mutual companies (sec. 1024 of the House bill and sec. 1023 of the Senate amendment)	Mutual property and casualty insurance companies are permitted deductions for contributions (which are merely bookkeeping entries) to a protection against loss ("PAL") account. The amount of the deduction is equal to the sum of one percent of the underwriting losses for the year, plus 25 percent of statutory underwriting income, plus certain windstorm and other losses. The account is established for a 5-year period and, in effect, gives a 5-year deferral of a portion of mutual company underwriting income.	The President's proposal would repeal the deduction for contributions to a PAL account. Amounts currently held in the account would be included in income no later than ratably over a 5-year period. *Effective date.*—Taxable years beginning after December 31, 1985.	Repeals the deduction for contributions to a PAL account. Amounts currently held in the account are included in income over a 5-year period. *Effective date.*—Taxable years beginning after December 31, 1985.	Same as the House bill, except that the amounts currently held in the account may be included at a slower rate in the second through fourth years of the 5 year period. *Effective date.*—Taxable years beginning after December 31, 1986.
7. Special exemptions, rates, and deductions of small mutual companies (sec. 1025 of the House bill and sec. 1024 of the Senate amendment)	Under present law, mutual property and casualty companies are classified into three categories depending upon the amounts of their gross receipts. Mutual companies with certain gross receipts not in excess of $150,000 are tax-exempt. Companies whose gross receipts exceed $150,000 but do not exceed $500,000 are "small mutuals" and may be taxed solely on investment income. Small mutuals which are subject to tax because their gross receipts exceed $150,000 may claim the benefit of a special rule which phases in the regular tax on investment income as gross receipts increase from $150,000 to $250,000. Companies whose gross receipts exceed $500,000 are ordinary mutuals taxed on both investment and underwriting income. Like stock companies, ordinary mutuals generally are subject to the regular corporate income tax rates. Mutuals whose taxable income does not exceed $12,000 are not subject to tax on the first $6,000 of taxable income, and a tax of 30 percent is imposed on the next $6,000 of taxable income. For small mutual companies which are taxable on investment income, no tax is imposed on the first $3,000 of taxable investment income, and a tax of 30 percent is imposed on taxable investment income between $3,000 and $6,000. Mutual companies that receive a gross amount from premiums and certain investment income of less than $1,100,000 are allowed a special deduction against their underwriting income (if it is subject to tax). The maximum amount of the deduction is $6,000, and the deduction phases out as the gross amount increases from $500,000 to $1,100,000.	The special tax exemptions, rate reductions, and deductions of small mutual property and casualty insurance companies would be repealed. *Effective date.*—The proposal would be phased in over a 5-year period starting with the first taxable year beginning after December 31, 1985.	Provides that property and casualty insurance companies (stock or mutual) with net written premiums (or direct written premiums, if greater) of less than $500,000 are exempt from tax, and companies with such premiums equal to or greater than $500,000, but less than $2 million, may elect to be taxed only on investment income. *Effective date.*—The provision is effective for taxable years beginning after December 31, 1985.	Provides that property and casualty insurance companies (stock or mutual) with net written premiums (or direct written premiums, if greater) of less than $350,000 are exempt from tax, and companies with such premiums equal to or greater than $350,000 but less than $1.2 million may elect to be taxed only on investment income. *Effective date.*—The provision is effective for taxable years beginning after December 31, 1986.

A. Treatment of Tax-Favored Savings 1. Individual retirement arrangements (IRAs) ***a. Eligibility to make deductible IRA contributions (sec. 1101 of the House bill and secs. 1201, 1202, and 1204A of the Senate amendment)***	(a) An individual who has not attained age 70½ is entitled to deduct from gross income (within limits) the amount contributed to an individual retirement arrangement (an IRA). The limit on the deduction for a taxable year generally is the lesser of $2,000 or 100 percent of compensation (earned income, in the case of income from self-employment). Prior to ERTA, deductible IRA contributions were not permitted for any taxable year if an individual, for any part of the plan year ending with or within the individual's taxable year, was an active participant (whether or not the individual's benefits were vested) in— (1) a qualified plan (secs. 401(a) or 403(a)), (2) a tax-sheltered annuity program (sec. 403(b)), or (3) a governmental plan (whether or not tax qualified). Nondeductible IRA contributions are not permitted.	(a) No provision.	(a) Provides a first-dollar offset of an employee's IRA deduction limit by reducing the deduction limit, dollar for dollar, by the employee's elective deferrals under a qualified cash or deferred arrangement (CODA) and a tax-sheltered annuity (sec. 403(b)). Also provides for the reduction of the first $2,000 of the spousal IRA deduction limit	(a) Similar to pre-ERTA IRA provisions, no deductible IRA contribution may be made for any taxable year if an individual is an active participant (whether or not the individual's benefits are vested) in an employer-maintained retirement plan for any part of the plan year ending with or within the individual's taxable year. For purposes of this rule, an employer-maintained retirement plan means— (1) a qualified plan (secs. 401(a), 401(k), or 403(a)), (2) a tax-sheltered annuity (sec. 403(b)), (3) a simplified employee pension (sec 408(k)), (4) a plan established for its employees by the United States, by a State or political subdivision, or by any agency or instrumentality of the United States or a State or political subdivision, or (5) a plan described in section 501(c)(18). Individuals who are not eligible to make deductible IRA contributions for a taxable year may make nondeductible IRA contributions. The limit on nondeductible contributions for a taxable year is the lesser of 100 percent of compensation (earned income in the case of a self-employed individual) or $2,000 ($2,250 in the case of a spousal IRA). It is the sense of the Senate that full IRA deductibility should be retained in a manner that does not adversely affect tax rates or the distribution of tax reduction by income class. (Floor amendment by Senator Packwood, adopted by voice vote.)
			Effective date.—Taxable years beginning after December 31, 1985. In the case of certain collectively bargained plans, the provision is not effective until years beginning on or after the earlier of— (1) the termination of the collective bargaining agreement, or (2) January 1, 1991.	*Effective date.*—Taxable years beginning after December 31, 1986.

Item	Present Law	President's Proposal	House Bill	Senate Amendment
1. Individual retirement arrangements (IRAs)—(cont.)				
b. Spousal IRA (sec. 1101 of the House bill and sec. 1204 of the Senate amendment)	(b) An individual is permitted an additional deduction for contributions to an IRA for the benefit of the individual's spouse if— (1) the spouse has no compensation for the year, (2) the spouse has not attained age 70½, and (3) the couple files a joint income tax return for the year. If these requirements are met, the annual deduction limit is increased from $2,000 to $2,250. The contribution may be divided as the spouses choose, provided the contribution for neither spouse exceeds $2,000 If both spouses have any compensation, including compensation less than $250, the spousal IRA deduction is not allowed	(b) For purposes of calculating the spousal IRA deduction limit, all compensation of both spouses could be considered if the couple filed a joint return Thus, deductible IRA contributions of up to $2,000 per year to each individual's IRA would be permitted for a couple filing a joint return, provided their combined earned income was at least $4,000. *Effective date.*—Taxable years beginning after December 31, 1985	(b) Retains the present-law $2,250 limit on spousal IRAs, but permits the spouse to elect to be treated as having no compensation for a year Thus, a spouse with less than $250 of compensation will not be precluded from receiving spousal IRA contributions. *Effective date.*—Taxable years beginning after December 31, 1985.	(b) Same as House bill *Effective date.*—Taxable years beginning after December 31, 1986.
c. Additional income tax on early withdrawals (sec. 1123 of the House bill and sec. 1223 of the Senate amendment)	(c) Amounts withdrawn from an IRA prior to age 59½, death, or disability of the owner are subject to a 10-percent additional income tax	(c) The additional income tax on IRA withdrawals prior to age 59½, death, or disability would be increased from 10 to 20 percent. The 10-percent tax would continue to apply to distributions made on account of (1) acquisition of the owner's first principal residence, (2) the payment of college expenses of a dependent, or (3) unemployment during a period following the cessation of unemployment benefits *Effective date.*—Taxable years beginning after December 31, 1985	(c) The additional income tax on IRA withdrawals prior to age 59½, death, or disability is increased from 10 to 15 percent. The tax is waived if the withdrawal is one of a scheduled series of level payments under an annuity for the life of the IRA owner (or the joint lives of the owner and the owner's beneficiary). *Effective date.*—Taxable years beginning after December 31, 1985.	(c) Same as House bill, except that the increase in the tax applies only to withdrawals attributable to deductible IRA contributions and the exemption applies if payments are made over the life expectancy of the owner *Effective date.*—Taxable years beginning after December 31, 1986.
d. Interest on loans to make IRA contributions (sec. 1203 of the Senate amendment)	(d) Under present law, no deduction is allowed for interest on indebtedness incurred or continued to purchase or carry obligations the interest on which is exempt from tax (sec. 265(2)). This provision does not apply to amounts borrowed to make IRA contributions, because the interest income on an IRA is not wholly exempt from tax. Instead, the interest on IRA contributions is not taxed until it is withdrawn	(d) No provision	(d) No provision. (See, however, the limitations on nonbusiness interest deductions in V C., above.)	(d) Denies a deduction for interest on indebtedness incurred or continued to make an IRA contribution (See, also, the limits on nonbusiness interest deductions in V C., above.)
e. Acquisition of gold and silver coins by IRAs (sec. 1242 of the Senate amendment)	(e) The acquisition by an IRA of any collectible is treated as a distribution from the IRA of the cost of the collectible and is includible in the IRA owner's income for the year deemed distributed A collectible includes any stamp or coin	(e) No provision	(e) No provision	(e) Exempts any gold or silver coin issued by the United States from the rules relating to IRA investments in collectibles (Floor amendment by Senator McClure, adopted by voice vote.) *Effective date.*—Acquisitions of coins after December 31, 1986

2. Qualified cash or deferred arrangements (sec. 401(k) plans) (secs. 1102, 1111, and 1112 of the House bill and secs. 1205 and 1216 of the Senate amendment)	If a cash or deferred arrangement (CODA) meets certain requirements, an employee who has a choice of receiving current pay or having that pay deferred under a profit-sharing or stock bonus plan (or certain pre-ERISA money purchase pension plans) is not taxed as though the compensation had been received.			
a. Limit on elective deferrals	(a) Elective deferrals under a CODA are subject to the overall limits on annual additions under a defined contribution plan Thus, under present law, the elective deferrals of any employee (plus employer contributions and certain other amounts) generally cannot exceed the lesser of $30,000 or 25 percent of the employee's nondeferred compensation.	(a) As modified, the President's proposal would repeal the special treatment of cash or deferred arrangements under present law, effective for years beginning after December 31, 1986	(a) Limits the maximum annual elective deferral for an employee under all CODAs and tax-sheltered annuities to $7,000 In addition, reduces an individual's annual cap on deferrals under an eligible deferred compensation plan (sec. 457) by the individual's elective deferrals under a CODA Also permits certain employees of certain educational or health organizations to make up to $15,000 in catch-up contributions over their lifetimes *Effective date.*—Taxable years beginning after December 31, 1985. In the case of certain collectively bargained plans, the provision is not effective until years beginning on or after the earlier of— (1) the termination of the collective bargaining agreement, or (2) January 1, 1991.	(a) Same as House bill, but also applies the $7,000 annual cap to elective deferrals, which the proposal permits, under a simplified employee pension (SEP), and under a plan described in section 501(c)(18). This limit is reduced, dollar for dollar, by elective deferrals under a tax-sheltered annuity. In addition, an individual's annual cap on deferrals under an eligible State or local deferred compensation plan is reduced by elective deferrals under CODAs, SEPs, and section 501(c)(18) plans. The $7,000 cap is indexed (beginning in 1988) by reference to percentage increases in the social security taxable wage base In addition, the $7,000 cap (as indexed) is increased by up to $2,500 in the case of certain investments in employer securities under an ESOP *Effective date*—Taxable years beginning after December 31, 1986 In the case of certain collectively bargained plans, the provision is not effective until years beginning on or after the earlier of— (1) the termination of the collective bargaining agreement, or (2) January 1, 1991
b. Nondiscrimination requirements	(b) A special nondiscrimination test applies a limit on elective deferrals under a CODA by the group of highly compensated employees that is determined by reference to the rate of deferrals by other employees. *Highly compensated employees.*—An employee is considered highly compensated, for this purpose, if the employee is more highly paid than ⅔ of all employees eligible to participate in the plan.	(b) No provision.	(b) Modifies the special nondiscrimination tests applicable to qualified CODAs by redefining the group of highly compensated employees and by revising the special percentage tests *Highly compensated employees.*—Adopts a uniform definition of highly compensated employees (see the description of Item B 5., below).	(b) Retains the present law special nondiscrimination test, but modifies definition of highly compensated employees *Highly compensated employees*—Adopts a uniform definition of highly compensated employees (see the description in Item B 5., below)

b. Nondiscrimination requirements (cont.)	*Nondiscrimination test*.—A CODA meets the special nondiscrimination test for a plan year if— (1) the average deferral percentage for the highly paid employees does not exceed the average deferral percentage for the other eligible employees by more than 150 percent, or (2) The average deferral percentage for the highly paid employees does not exceed the average deferral percentage of the other eligible employees by more than the lesser of (a) 250 percent of the average of the other eligible employees, or (b) such average, plus 3 percentage points.		*Nondiscrimination test*.—Alters the special nondiscrimination test to provide that the test is met for a year if the average deferral percentage for the highly compensated employees does not exceed the greater of— (1) 125 percent of the average deferral percentage for all other eligible employees, or (2) the lesser of (i) 200 percent of the average deferral percentage for all other eligible employees, or (ii) such average, plus 2 percentage points.	*Nondiscrimination test* Retains the present law percentage tests
	Failure to satisfy nondiscrimination test.—If a cash or deferred arrangement fails to meet the special nondiscrimination test, the arrangement is not a qualified cash or deferred arrangement.	*Failure to satisfy nondiscrimination test*.— No provision	*Failure to satisfy nondiscrimination test*.—If the special nondiscrimination test is not satisfied for any year, the bill provides that the excess elective deferrals of highly compensated employees are subject to a 10 percent excise tax unless distributed (with earnings) within 2½ months after the end of the year of deferral. Violation of the special nondiscrimination test will not cause the disqualification of the arrangement if excess elective deferrals are distributed by the end of the following year.	*Failure to satisfy nondiscrimination test*.—Same as House bill
			Effective date.—The provision applies for years beginning after December 31, 1985. In the case of certain collectively bargained plans, the provisions are not effective until years beginning on or after the earlier of— (1) the termination of the collective bargaining agreement, or (2) January 1, 1991. In the case of a CODA maintained by a public employer that is grandfathered (see Item c., below), the new nondiscrimination rules do not apply for years beginning before November 22, 1987	*Effective date*.—The modification of the definition of highly compensated employees is effective for years beginning after December 31, 1988, and the treatment of a discriminatory arrangement is effective for years beginning after December 31, 1986 In the case of certain collectively bargained plans, the provisions are not effective until years beginning on or after the earlier of— (1) the termination of the collective bargaining agreement, or (2) January 1, 1991.

Item	Present Law	President's Proposal	House Bill	Senate Amendment
c. Withdrawal and other restrictions	(c) A participant in a qualified CODA is not permitted to withdraw elective deferrals (or earnings thereon) before age 59½, death, disability, separation from service, retirement, or the occurrence of a hardship It is unclear under present law whether tax-exempt and public employers may establish a CODA The IRS has issued determination letters on the qualified status of CODAs maintained by tax-exempt and State and local governments, but ceased issuing determination letters during 1985.	(c) No provision.	(c) Imposes the following additional restrictions on CODAs: (1) Limit hardship withdrawals to an employee's elective deferrals; (2) Withdrawals on account of plan termination are permitted; (3) An employer may not condition, either directly or indirectly (other than through matching contributions), contributions and benefits upon an employee's elective deferrals; (4) Employees may not be required to complete more than one year of service to be eligible to defer; and (5) CODAs are not available to employees of tax-exempt and public employers.	(c) Imposes the following additional restrictions on CODAs: (1) Same as House bill (2) Same as House bill, and also permits withdrawals in the case of certain sales of subsidiaries or assets (3) Same as House bill (4) Same as House bill. (5) CODAs are available to employees of tax-exempt employers, but are not available to State and local governments.
			Effective dates.—Generally effective for years beginning after December 31, 1985. In the case of certain collectively bargained plans, the provisions are not effective until years beginning on or after the earlier of— (1) the termination of the collective bargaining agreement, or (2) January 1, 1991.	*Effective dates.*—Generally effective for years beginning after December 31, 1988. In the case of certain collectively bargained plans, the provisions would not be effective for years beginning before the earlier of— (1) the later of January 1, 1989, or termination of the collective bargaining agreement, or (2) January 1, 1991.
			Tax-exempt employers.—The provision under which public employers may not maintain a CODA does not apply to plans adopted before November 6, 1985, if the employer submitted a determination letter request to the IRS by that date With respect to those public employer plans grandfathered under the preceding rule, the new withdrawal restrictions do not apply for years beginning before November 22, 1987.	*Tax-exempt employers*—The provision clarifying that tax-exempt employers may maintain CODAs is effective immediately The provision prohibiting State and local governments from maintaining CODAs does not apply to a CODA adopted by the employer before May 6, 1986
			Qualified offset arrangements.—A transition rule is provided for the provision that an employer cannot condition other benefits on an employee's elective deferrals The transition rule delays the effective date of the provision until plan years beginning on or after January 1, 1991, in the case of a "qualified offset arrangement."	*Qualified offset arrangements.*—Same as House bill, but the rule applies on a permanent basis and the treatment is available to successor employers.
			Withdrawals on plan termination.—The provision permitting withdrawals upon plan termination is effective for terminations after December 31, 1984	*Withdrawals on plan termination*—The provisions permitting withdrawals on plan termination and sale of a subsidiary or assets are effective for terminations or distributions after December 31, 1984

3. **Employer matching contributions and employee contributions (sec. 1112 of the House bill and sec. 1217 of the Senate amendment)** *a. Employer matching and employee contributions*	(a) If an employer contribution under a qualified plan is conditioned on an employee's contribution, then the employer matching contribution must be a uniform percentage of compensation (adjusted, to the extent permitted, for certain social security benefits).	(a) Under the proposal, two special nondiscrimination tests would be applied to employer matching contributions under any qualified plan. An aggregation rule would apply if employer matching contributions are tied to elective deferrals under a CODA.	(a) Two special nondiscrimination tests are applied to employer matching contributions and employee contributions. These tests apply in addition to the general nondiscrimination rules for qualified plans.	(a) A single special nondiscrimination test is applied to all types of employer matching contributions and employee contributions, in lieu of the general nondiscrimination test.
	An employer may elect to treat certain qualifying employer matching contributions to a CODA under the special nondiscrimination tests which permit higher contributions (as a percentage of compensation) for the top ⅓ of employees by compensation, but which do not permit social security benefits to be taken into account. Employer matching contributions are treated as qualifying matching contributions and, therefore, may be tested under the special nondiscrimination test if the contributions are fully and immediately vested and subject to the withdrawal restrictions applicable to CODAs.	*Qualifying employer matching contributions.*—Qualifying employer matching contributions for any highly compensated employee (expressed as a percentage of pay) would be limited to the greater of— (1) 125 percent of the average matching contributions (expressed as a percentage of pay) for nonhighly compensated employees, or (2) the lesser of— (i) 200 percent of the average for nonhighly compensated employees, or (ii) such average, plus 2 percentage points.	*Qualifying employer matching and employee contributions.*—The average qualifying employer matching contributions and employee contributions (expressed as a percentage of pay) for highly compensated employees are each limited to the greater of— (1) 125 percent of the average employer matching contributions and employee contributions (expressed as a percentage of pay) for nonhighly compensated employees, or (2) the lesser of (i) 200 percent of the average for nonhighly compensated employees, or (ii) such average, plus 2 percentage points.	*Employer matching and employee contributions.*—Under this test, the average employer matching contributions and employee contributions (expressed as a percentage of pay) for highly compensated employees are together limited to the greater of— (1) 150 percent of the average employer matching contributions and employee contributions (expressed as a percentage of pay) for the nonhighly compensated employees, or (2) the lesser of (i) 250 percent of the average for the nonhighly compensated employees, or (ii) such average, plus 3 percentage points.
		The definition of highly compensated employees is the same as the definition for CODAs. (See the description in Item B.1.e., below.) Qualifying employer matching contributions are required to be— (1) nonforfeitable when made, (2) ineligible for withdrawal prior to the employee's death, disability, separation from service, or plan termination, and (3) no greater than 100 percent of the employee's mandatory contributions.	A uniform definition of highly compensated employees is adopted (see the description in Item B.5., below). Qualifying employer matching contributions are required to be— (1) nonforfeitable when made, (2) ineligible for withdrawal prior to the employee's death, disability, separation from service, or plan termination, and (3) no greater than 100 percent of the employees' mandatory contributions.	A uniform definition of highly compensated employees is adopted (see the description in Item B.5., below). No distinction is made between qualifying employer matching contributions and other employer matching contributions.
		Other employer matching contributions.—Under the proposal, the average of the employer matching contributions that are not qualifying employer matching contributions for any highly compensated employee would be limited to the greater of— (1) 110 percent of the average nonqualifying contributions for the nonhighly compensated employees, or (2) the lesser of— (i) 150 percent of the average nonqualifying contributions for nonhighly compensated employees or (ii) such average, plus 1 percentage point.	*Other employer matching contributions.*—The average of nonqualifying employer matching contributions (expressed as a percentage of pay) for highly compensated employees is limited to the greater of— (1) 110 percent of the average nonqualifying employer matching contributions (expressed as a percentage of pay) for the nonhighly compensated employees, or (2) the lesser of— (i) 150 percent of the average for nonhighly compensated employee, or (ii) such average, plus 1 percentage point.	*Other employer matching contributions.*—No provision; all employer matching contributions are subject to the preceding test.

Item	Present Law	President's Proposal	House Bill	Senate Amendment
b. Excess contributions	(b) If employer matching contributions discriminate in favor of employees who are officers, shareholders or highly compensated, the plan is disqualified.	(b) Under the proposal— (1) the employer would be denied a deduction for any contributions on behalf of highly compensated employees in excess of the amount permitted under the matching contribution rules, (2) those excess contributions would be subject to a nondeductible 10-percent excise tax, and (3) unless the excess contributions (plus earnings thereon) were distributed by the end of the plan year following the year for which the contributions were made, the plan would be retroactively disqualified. *Effective date.*—The proposals would apply generally to plan years beginning after December 31, 1985. For collectively bargained plans, the proposals would apply to plan years beginning after the termination of the collective bargining agreement.	(b) If the special nondiscrimination tests for employer matching and employee contributions are not satisfied for a year, the bill provides that— (1) the excess contributions are subject to a 10-percent excise tax unless distributed (with earnings) within 2½ months after the end of the year, (2) unless the excess contributions (plus earnings thereon) are distributed no later than the end of the following year, the plan will be retroactively disqualified *Effective dates.*—Years beginning after December 31, 1985. In the case of certain collectively bargained plans, the provisions are not effective until years beginning on or after the earlier of— (1) the termination of the collective bargaining agreement, or (2) January 1, 1991. In addition, with respect to any plan that is maintained by a State or local government and that was in existence on November 6, 1985, the provisions do not apply until years beginning after November 21, 1987.	(b) Same as House bill *Effective dotes.*—Years beginning after December 31, 1988. In the case of certain collectively bargained plans, the provisions would not be effective before years beginning before the earlier of— (1) the later of January 1, 1989, or the termination of the collectively bargained agreement, or (2) January 1, 1991.
4. Unfunded deferred compensation arrangements of State and local governments and tax-exempt employers (sec. 1104 of the House bill and sec. 1207 of the Senate amendment)				
a. Eligible plan	(a) Under an eligible deferred compensation plan maintained by a State or local government or rural electric cooperative, an employee may elect annual deferrals equal to the lesser of $7,500 or 33⅓ percent of compensation (net of the deferral). A participant in an eligible plan who elects to defer the receipt of current compensation will be taxed on the deferred amounts (and income attributable thereto) when such amounts are paid or otherwise made available If an unfunded State or local plan (other than an eligible judicial plan) does not qualify as an eligible plan, the deferral is included in the employee's gross income when there is no longer a substantial risk of forfeiture of such amount	(a) The proposal would provide that the rules relating to eligible deferred compensation plans would apply also to unfunded deferred compensation plana for employees of tax-exempt employers.	(a) Same as President's proposal.	(a) Retains present law

Item	Present Law	President's Proposal	House Bill	Senate Amendment
b. Required distributions	(b)(1) *Required distributions.*—Distributions under an eligible plan are required to commence no later than 60 days after the later of (1) the year in which the employee attains normal retirement age, or (2) the year in which the employee separates from service. The total benefits scheduled to be paid to the participant must be more than 50 percent of the maximum amount that could have been paid to the participant if no provision were made for payments to the beneficiary.	(b)(1) *Required distributions.*—Under the proposal, distributions would be required— (i) to satisfy a payout schedule under which benefits projected to be paid over the lifetime of the participant are at least 66⅔ percent of the total benefits payable with respect to the participant. (ii) in the case of benefits payable over a period of more than one year, to be paid on a substantially nonincreasing basis, and (iii) after the death of the employee, to provide for the commencement of benefits to the employee's beneficiary within one year after the employee's death.	(b)(1) *Required distributions.*—Distributions are required— (i) to satisfy a payout schedule under which benefits projected to be paid over the lifetime of the participant are at least 66⅔ percent of the total benefits payable with respect to the participant, (ii) in the case of benefits payable over a period of more than one year, to be paid on a substantially nonincreasing basis, (iii) after the death of the employee, to provide for the commencement of benefits to the employee's beneficiary within 60 days after the close of the year in which employee's death occurs, and (iv) in the case of benefits that commenced before the employee's death, to provide for the payment of benefits under a method at least as rapid as the method of payment before death	(b)(1) *Required distributions.*—Same as House bill.
	(2) *Constructive receipts.*—Deferrals under an eligible plan are includible in income when distributed or made available.	(2) *Constructive receipt.*—Under the proposal, benefits would not be treated as made available merely because an employee is allowed to elect to receive a lump sum payable within 60 days of the election This rule applies only if the employee's total deferred benefit does not exceed $3,500 and the employee is no longer entitled to elect deferrals under the plan.	(2) *Constructive receipt.*—Same as President's proposal.	(2) *Constructive receipt.*—Same as House bill and President's proposal
	(3) *Rollovers.*—No rollovers between eligible plans are permitted	(3) *Rollovers.*—Certain tax-free rollovers between eligible plans would be permitted.	(3) *Rollovers.*—Same as President's proposal	(3) *Rollovers.*—Same as House bill and President's proposal
	(4) *Coordination with other contributions.*—The amount that a participant may defer under an eligible plan is reduced by contributions under a tax-sheltered annuity	(4) *Coordination with other contributions.*—No provision.	(4) *Coordination with other contributions.*—The amount that a participant may defer under an eligible deferred compensation plan is reduced, dollar for dollar, by the participant's elective deferrals under a CODA (except a CODA maintained by a rural electric cooperative).	(4) *Coordination with other contributions.*—The amount that a participant defers under an eligible deferred compensation plan reduces, dollar for dollar, the limit on the participant's elective deferrals under a CODA (except a CODA maintained by a rural electric cooperative), elective deferrals under a SEP, and deductible contributions under a section 501(c)(18) plan
		Effective date.—The provisions would apply to taxable years beginning after December 31, 1985.	*Effective date.*—Effective for years beginning after December 31, 1985 An exception is provided for State judicial plans.	*Effective date.*—Effective for years beginning after December 31, 1986. An exception is provided for State judicial plans

Item	Present Law	President's Proposal	House Bill	Senate Amendment
5. **Deferred annuity contracts (sec. 1135 of the House bill and sec. 1234 of the Senate amendment)**	(a) *Investment earnings.*—Interest credited to the cash surrender value of a deferred annuity is not taxed currently, but is taxed when paid to the policyholder	(a) *Investment earnings.*—The owner of a deferred annuity contract would include in income any increase in the excess of the contract's cash value over the owner's investment in the contract during the taxable year	(a) *Investment earnings.*—The annual increase in value of a deferred annuity contract is includible in gross income if the owner of the contract is a nonnatural person (such as a corporation or a partnership)	(a) *Investment earnings.*—Same as House bill
	(b) *Early withdrawal tax.*—If a policyholder receives any amount under an annuity contract before reaching age 59½, an additional income tax is imposed equal to five percent of the amount included in income This tax does not apply if the distribution is one of a series of periodic payments lasting at least 60 months or is made for certain other purposes.	(b) *Early withdrawal tax.*—Same as present law	(b) *Early withdrawal tax.*—The additional income tax on amounts withdrawn from deferred annuity contracts before age 59½ is conformed to the 15-percent tax on early withdrawals from IRAs The tax is waived if the withdrawal is one of a scheduled series of level payments over the life of the annuitant (or over the joint lives of the annuitant and the annuitant's beneficiary).	(b) *Early withdrawal tax.*—Retains present law for the additional income tax on amounts withdrawn from deferred annuity contracts, but (1) repeals the exception for payments made for at least 60 months and (2) waives the tax if the withdrawal is one of a scheduled series of level payments over the life (or life expectancy) of the annuitant (or over the joint lives of the annuitant and the annuitant's beneficiary).
		Effective date.—The proposal would become effective for investment income credited after December 31, 1985, to policies issued on or after the date of committee action.	*Effective date.*—Effective for amounts invested in deferred annuity contracts after September 25, 1985	*Effective date.*—Effective for amounts invested in deferred annuity contracts after February 28, 1986
6. **Elective contributions under tax-sheltered annuities (sec. 1102 of the House bill)**	Under present law, public schools and certain tax-exempt organizations (including churches and certain organizations associated with churches) may make payments on behalf of an employee to purchase a tax-sheltered annuity contract (sec. 403(b)). Payments to a custodial account investing in stock of a regulated investment company (e g., a mutual fund) are also permitted The amount paid by the employer is excluded from the employee's income for the taxable year to the extent the payment does not exceed the employee's exclusion allowance for the taxable year. The exclusion allowance is generally equal to 20 percent of the employee's includible compensation from the employer multiplied by the number of the employee's years of service with the employer, reduced by amounts already paid by the employer to purchase the annuity (sec. 403(b)(2)) Employer payments to purchase a tax-sheltered annuity contract for an employee are also subject to the overall limits on contributions and benefits under qualified plans (sec 415). Because tax-sheltered annuities generally are defined contribution plans, the limit on the annual additions on behalf of an employee generally is the lesser of 25 percent of a compensation or $30,000.	*Limit on elective deferrals.*—No provision *Coordination with other elective deferrals.*—No provision *Coordination with IRA deduction limit.*—No provision *Special catch-up election.*—No provision	*Limit on elective deferrals.*—Limits to $7,000 the amount that an employee can elect to defer for any taxable year under all tax-sheltered annuities in which the employee participates. *Coordination with other elective deferrals.*—An individual's elective deferrals under a CODA reduce, dollar for dollar, the $7,000 cap on the individual's elective deferrals under a tax-sheltered annuity *Coordination with IRA deduction limit.*—An individual's IRA deduction limit is reduced, dollar for dollar, by the employee's elective deferrals under a tax-sheltered annuity *Special catch-up election.*—A special catch-up election provides a limited exception to the $7,000 annual limit (but not the otherwise applicable exclusion allowance (sec. 403(b)) or the overall limit on contributions and benefits (sec. 415) in the case of employees of an educational organization, a hospital, a home health service agency, or a church, convention, or association of churches The catch up is limited to $3,000 per year (up to $15,000) and is available only to employees with at least 15 years of service whose contributions have not, on average, exceeded $5,000 per year	*Limit on elective deferrals.*—Retains present law *Coordination with other elective deferrals.*—Retains present law *Coordination with IRA deduction limit.*—No deductible IRA contributions may be made by an employee participating in a tax-sheltered annuity, but nondeductible IRA contributions are permitted *Special catch up election.*—No provision (See, however, the provision relating to the catch-up election to the overall limits (Item D.1 d).)

6. **Elective contributions under tax-sheltered annuities—(cont.)**	Certain catch-up elections allow an employer to contribute in excess of the usual percentage limits in certain years. The catch-up election is available only to employees of an educational organization, a hospital, a home health service agency, or a church, convention, or association of churches.		*Effective dates.*—The provisions generally are effective for years beginning after December 31, 1985. In the case of certain collective bargaining agreements, the provisions do not apply to contributions made under such an agreement in taxable years beginning before the earlier of— (1) the date on which the last of the collective bargaining agreements terminates, or (2) January 1, 1991.	
7. **Special rules for simplified employee pensions (sec. 1208 of the Senate amendment)**	Under present law, if an IRA qualifies as a simplified employee pension (SEP), the annual IRA deduction limit is increased to the lesser of— (1) $30,000 or (2) 15 percent of compensation. The increased deduction limit applies only to employer contributions. Employer contributions under a SEP are considered discriminatory unless contributions thereto bear a uniform relationship to compensation.			Adopts several simplifying SEP amendments and permits elective deferrals under a SEP, as described below.
a. Limit on elective deferrals	(a) *Limit on elective deferrals.*—Present law does not permit elective deferrals under a SEP.	(a) *Limit on elective deferrals.*—No provision.	(a) *Limit on elective deferrals.*—No provision.	(a) *Limit on elective deferrals.*—Permits employees participating in a SEP to make elective deferrals of up to $7,000 (indexed) under the SEP, provided that— (1) the employer maintaining the SEP has 25 or fewer employees, (2) at least 50 percent of the employees of the employer elect to have amounts contributed to the SEP, and (3) the employer is not a public employer. Limits the average amount deferred as a percentage of compensation (deferral percentage) for each highly compensated employee to no more than 150 percent of the average deferral percentage of all other eligible employees. (Employer contributions are subject to the nondiscrimination rules of present law). The uniform definition of highly compensated employees is applied. (See Item B.5., below.) Excess deferrals are subject to the same rules as CODAs. (See Item 2, above.)

b. Coordination with IRA deduction limit	(b) *Coordination with IRA deduction limit.*—Present law does not coordinate the limit on SEP contributions with the IRA deduction limit.	(b) *Coordination with IRA deduction.*—No provision.	(b) *Coordination with IRA deduction.*—No provision.	(b) *Coordination with IRA deduction limit.*—An individual who is an active participant in a SEP may not make deductible IRA contributions (see Item A 1.a., above).
c. Coordination with other elective deferrals	(c) *Coordination with other elective deferrals.*—No provision.	(c) *Coordination with other elective deferrals.*—No provision	(c) *Coordination with other elective deferrals.*—No provision.	(c) *Coordination with other elective deferrals.*—An employee's elective deferrals under a SEP are coordinated with elective deferrals under a CODA, and a section 501(c)(18) plan for purposes of the $7,000 cap. Such elective deferrals reduce the cap on deferrals under a section 457 plan *Effective date.*—Effective for years beginning after December 31, 1986.
8. Salary reduction permitted under section 501(c)(18) plans (sec. 1209 of the Senate amendment)	Under present law, a trust or trusts created before June 25, 1959, forming part of a pension plan funded solely by employee contributions is entitled to tax-exempt status if certain nondiscrimination requirements are met (sec. 501(c)(18)). Rev. Rul. 54-190 concluded that contributions to a section 501(c)(18) pension plan were deductible as union dues In 1982, the IRS declared Rev. Rul. 54-190 obsolete	No provision	No provision.	Participants in a section 501(c)(18) plan may make deductible contributions to the plan up to the lesser of (1) $7,000 or (2) 25 percent of compensation. This limit is coordinated with limits on elective deferrals under CODAs and SEPs. A special nondiscrimination test similar to the test for qualified cash or deferred arrangements applies to the deductible contributions *Effective date.*—Contributions made in taxable years beginning after December 31, 1986.

B. Minimum Standards for Qualified Plans				
1. Coverage requirements for qualified plans (sec. 1136 of the House bill and sec. 1212 of the Senate amendment)	(a) The coverage rules for qualified plans require that a plan cover employees in general rather than merely employees who are officers, shareholders, or highly compensated. A plan generally satisfies the coverage rules if it meets either— (1) a percentage test, or (2) a fair cross-section test	(a) Would revise the coverage test for qualified plans, as described below	(a) Directs the Secretary of the Treasury to study the effect of the present-law coverage tests, and to report to the Committee on Ways and Means of the House of Representatives and the Committee on Finance of the Senate, as well as the Joint Committee on Taxation, by July 1, 1986 The report is to include specific recommendations of any changes that the Secretary finds to be appropriate or necessary, including recommendations for implementing those changes	(a) A plan satisfies the coverage rules if it meets— (1) a percentage test, (2) a reasonable classification test, or (3) an alternative reasonable classification test
	Percentage test.—A plan meets the percentage test if— (1) it benefits at least 70 percent of all employees, or (2) it benefits at least 80 percent of the employees eligible to benefit under the plan and at least 70 percent of all employees are eligible (i e., the plan benefits at least 56 percent of all employees).	*Percentage test.*—The proposal provides that the coverage test would be met only if the percentage of highly compensated employees benefiting under the plan does not exceed 125 percent of the percentage of all other employees benefiting under the plan. Under certain very limited circumstances in the case of a compelling business reason (such as a merger), the IRS could waive the 125 percent test in favor of a more liberal test for a period of time.	*Percentage test* —No provision	*Percentage test* —A plan meets the percentage test if the plan benefits at least 80 percent of the employees
	Fair cross-section test.—A plan meets the fair cross-section test if the Secretary of the Treasury determines that it covers a classification of employees that is found not to discriminate in favor of employees who are officers, shareholders, or highly compensated IRS regulations provide that, in determining whether the fair cross-section test is satisfied, all of the surrounding facts and circumstances must be taken into account, allowing for a reasonable difference between the percentage of officers, shareholders, or highly compensated employees who are benefited by the plan and the percentage of other employees benefited by the plan The regulations do not preclude consideration of the existence of separate lines of business or of benefits provided under other plans as a fact or circumstance justifying a reasonable disparity Employees not covered by a plan that satisfies the fair cross-section test are not required to be covered under any plan of an employer.	*Fair cross-section test.*—Repeal present law	*Fair cross-section test.*—No provision	*Fair cross-section test.*—The fair cross-section test is retained for purposes of the alternative reasonable classification test (see below). *Reasonable classification test.*—A plan meets the reasonable classification test if the Secretary of the Treasury determines that it covers a reasonable classification of employees that is found not to discriminate in favor of highly compensated employees The Secretary of the Treasury is directed that the disparity between the coverage percentage of highly compensated employees and the coverage percentage of nonhighly compensated employees permitted in Rev. Rul 83-58 is excessive. In addition, the amendment clarifies that reasonable disparities between the coverage percentage of highly compensated employees and the coverage percentage of nonhighly compensated employees are permitted if justified by the attendant facts and circumstances. The test may be satisfied on a line of business or operating unit basis

Item	Present Law	President's Proposal	House Bill	Senate Amendment
I. Coverage requirements for qualified plans (cont.)	Under Revenue Ruling 83-58, the IRS ruled that a plan satisfied the fair cross-section test under the following facts and circumstances: (1) the plan covered only salaried employees, (2) the plan covered 40 out of 150 employees (27 percent of all employees); (3) 55 percent of the employees participating in the plan were officers or shareholders of the employer; and, (4) the plan covered 100 percent of those employees with compensation greater than $40,000 (100 percent of whom were officers and shareholders) and only 25 percent of employees whose compensation was less than $40,000 (50 percent of whom were officers or shareholders); and (5) the compensation of the covered employees was substantially the same as the compensation of the excluded employees.	*Alternative reasonoble classification test.*—No provision	*Alternative reasonable classification test.*—No provision	*Alternative reasonable classification test.*—A plan satisfies the alternative reasonable classification test if— (1) the plan satisfies the present-law fair cross-section test, but not the reasonable classification test, and (2) the average benefit as a percentage of compensation for employees not covered under the plan is at least 60 percent of the average benefit percentage for employees covered under the plan The test may be satisfied on a line of business or operating unit basis
	Line of business.—No specific rules apply to permit coverage requirements to be satisfied on a line of business or operating unit basis	*Line of business.*—No provision.	*Line of business.*—No provision	*Line of business.*—The reasonable classification test and the alternative reasonable classification test may be applied separately to a line of business or operating unit of the employer if the employer demonstrates to the satisfaction of the Secretary that such line of business or operating unit is operated separately for bona fide business reasons A separate line of business or operating unit is treated as operated for bona fide business reasons if such line of business or operating unit is a separate self-sustaining unit and (1) such line of business or operating unit has at least 50 employees, (2) the percentage of highly compensated employees within such line of business or operating unit is not less than 50 percent of the percentage of highly compensated employees of the employer or at least 10 percent of the highly compensated employees of the employer perform services solely for the line of business or operating unit, and (3) the percentage of highly compensated employees within such line of business or operating unit is not more than 200 percent of the percentage of highly compensated employees of the employer

1. Coverage requirements for qualified plans (cont.)				Such separate testing on a line of business or operating unit basis does not apply to a plan that does not satisfy the present law fair cross-section test
	Excludable employees.—In applying the percentage test, but not the fair cross-section test, certain employees who have not (1) completed minimum periods of service (generally one year), and (2) attained age 21 may be disregarded Employees with less than three years of service may be excluded if the plan provides for full and immediate vesting. In addition, in applying both the percentage and the fair cross-section test, employees not covered by the plan who are included in a unit of employees covered by a collective bargaining agreement are disregarded if there is evidence that retirement benefits were the subject of good faith bargaining. Certain nonresident aliens and certain airline pilots also are disregarded.	*Excludable employees*.—The proposal would narrow the class of employees who could be excluded from consideration in applying the percentage test by repealing the exceptions for employees with less than three years of service and for certain airline pilots.	*Excludable explovees*.—No provision	*Excludable employees*.—Retains present law, but provides a special rule for determining excludable employees for purposes of the alternative reasonable classification test under which the employer may (1) count all employees, or (2) exclude employees who have not completed the lowest age or service requirement in any plan of the employer Also permits an employer to disregard certain excludable employees who are covered under a separate plan that meets the coverage requirements
		Effective date.—The President's proposal would be effective for plan years beginning after December 31, 1986. For collectively bargained plans, the proposal would not apply to plan years beginning before the termination of the current collective bargaining agreement.		*Effective dates*.—Generally effective for plan years beginning after December 31, 1988. In the case of certain collectively bargained plans, the provision would not be effective before years beginning before the earlier of (1) the later of January 1, 1989, or the termination of the collective bargaining agreement, or (2) January 1, 1991

Item	Present Law	President's Proposal	House Bill	Senate Amendment
2. **Minimum participation requirement (sec. 1212 of the Senate amendment)**	No provision	No provision	No provision	A plan is required to cover the lesser of 50 employees or 40 percent of all of an employer's nonexcludable employees, effective for plan years beginning after 1988
3. **Nondiscrimination rules applicable to tax-sheltered annuities (sec. 1113 of the House bill)**	Under present law, a qualified plan is required to meet nondiscrimination requirements as to coverage and as to contributions and benefits provided under the plan, which ensure that the plan does not favor employees who are officers, shareholders, or highly compensated. A tax-sheltered annuity program maintained by a tax-exempt charitable organization or certain educational institutions is not required to meet nondiscrimination requirements.	(a) *Coverage and nondiscrimination.*—No provision.	(a) *Coverage and nondiscrimination.*—Applies the coverage and nondiscrimination rules of present law (secs. 410(b) and 401(a)(4)) to the portion of any tax-sheltered annuity program attributable to contributions by the sponsoring employer (other than employer contributions under plans maintained by churches). Directs the Secretary of the Treasury, in applying the coverage rules, to take into account the special circumstances faced by educational organizations and tax-exempt organizations (including the compressed salary scales of those organizations and the need of educational institutions to attract visiting professors).	(a) *Coverage and nondiscrimination.*—Retains present law
		(b) *Special rule for elective deferrals.*—No provision.	(b) *Special rule for elective deferrals.*—Applies a special coverage and nondiscrimination rule to the portion of any tax-sheltered annuity programs that permits elective deferrals. A tax-sheltered annuity program that permits elective deferrals will be considered discriminatory with respect to those deferrals unless the opportunity to make elective deferrals is made available to all employees of the entity sponsoring the tax-sheltered annuity program. In applying the special test for deferrals, no employees of the entity sponsoring the tax-sheltered annuity program (other than nonresident aliens with no U.S.-source earned income) may be excluded from consideration *Effective date.*—The provision is effective for plan years beginning after December 31, 1985. However, with respect to tax-sheltered annuity programs maintained by State and local governments, the provisions generally apply for plan years beginning after November 21, 1987.	(b) *Special rule for elective deferrals.*—Retains present law.

4. Integration with Social Security (sec. 1114 of the House bill and sec. 1211 of the Senate amendment)	Under present law, a plan is not qualified unless contributions or benefits do not discriminate in favor of employees who are officers, shareholders, or highly compensated. A plan is not considered discriminatory merely because benefits provided under the plan bear a uniform relationship to compensation. For purposes of determining whether benefits bear a uniform relationship to compensation, the employer-provided share of an employee's social security benefit may be taken into account. Under certain circumstances, the employer-provided share of social security benefits may be taken into account more than once under a defined benefit pension plan because an employer may reduce plan benefits by social security benefits earned with a prior employer.	No provision.	Modifies the integration rules for defined benefit pension plans, as described below.	As described below, the rules governing the integration of a qualified plan with social security are modified. A defined benefit pension plan (whether an excess plan or an offset plan) may provide that an employee's benefit under the plan may be reduced to the extent that the employee's benefit, when combined with employer-provided social security benefits attributable to the employee's years of service with that employer, exceeds 100 percent of the employee's final compensation.
a. Defined benefit plans *(1) Excess plans*	(a)(1) A defined benefit plan may be tested for discrimination in favor of highly paid employees by comparing the rate at which benefits are provided for pay in excess of a stated level (the integration level) with the rate at which benefits are provided for pay up to that level. If the difference is not more than 37½ percentage points (after adjustments), the plan will not be considered discriminatory. For an employee who retires at age 65 in 1986, an excess plan could meet the nondiscrimination standard by providing benefits at the rate of 37½ percent of average pay in excess of $15,000 and no benefits with respect to the first $15,000 of pay. For younger employees, the integration level may be increased (up to $42,000).		(a)(1) Provides that social security benefits earned with a prior employer are not to be considered in testing whether a defined benefit pension plan is considered discriminatory.	(a)(1) The rate at which benefits are provided for pay up to the integration level of a plan generally may not be less than 50 percent of the rate at which benefits are provided for pay in excess of that level. The integration level may not be more than the Social Security wage and benefit base ($42,000 for 1986). Any optional form of benefit, preretirement benefit, actuarial factor, or other benefit or feature provided with respect to pay above the integration level must be provided with respect to pay up to the integration level.
(2) Offset plans	(2) A defined benefit offset plan may provide a benefit that is reduced (offset) by social security benefits considered to be provided to a plan participant from employer payments of the social security tax. A participant's plan benefit may be reduced by up to 83⅓ percent of the primary insurance amount provided under the Social Security Act.		(2) Same as rule for excess plans.	(2) A plan may offset each participant's benefit by a specified dollar amount, but such offset may not reduce a participant's benefit by more than 50 percent. For example, if an employee's benefit before the offset was $200 per month, then the offset may not reduce the benefit below $100 per month.

b. Defined contribution plans	(b) A defined contribution plan may be tested for discrimination in favor of highly paid employees by comparing the rate at which employer contributions are provided for pay in excess of a stated level (the integration level) with the rate at which employer contributions are provided for pay up to that level. If the difference is not more than the rate of the employer FICA tax for OASDI benefits under the Social Security Act, the difference will not cause the plan to be discriminatory. For 1986, an integrated defined contribution plan could provide employer contributions equal to 5.7 percent of pay in excess of $42,000 and no contributions for the first $42,000 of pay.		(b) No provision. *Effective date.*—The proposal generally is effective for plan years beginning after December 31, 1985.	(b) The rate at which employer contributions are provided for pay up to the integration level of a plan may not be less than 50 percent of the rate at which contributions are provided for pay in excess of that level. Also, the rate for pay in excess of the integration level may not exceed the rate for pay up to that level by more than OASDI tax rate (5.7 percent for 1986). The integration level may not be more than the Social Security wage and benefit base ($42,000 for 1986). *Effective dates.*—Generally effective for plan years beginning after December 31, 1988. In the case of certain collectively bargained plans, the provision would not be effective for years beginning before the earlier of— (1) the later of January 1, 1989, or the termination of the collective bargaining agreement, or (2) January 1, 1991.
5. Definition of highly compensated employees (sec. 1111 of the House bill and sec. 1214 of the Senate amendment)	Present law generally does not explicitly define the group of employees who are officers, shareholders, or highly compensated. For purposes of the special nondiscrimination test for qualified cash or deferred arrangements, an employee is considered highly compensated if the employee is more highly paid than ⅔ of all employees eligible to participate in the plan.	The proposal would provide a uniform definition of highly compensated employees. An employee would be treated as highly compensated for a plan year if, at any time during the 3-year period ending on the last day of the plan year, the employee— (1) owns an interest of at least one percent of the employer (determined with attribution rules), (2) earns at least $50,000 in annual compensation from the employer, (3) earns at least $20,000 in compensation and is among— (a) the top 10 percent of employees by compensation, or (b) the top 3 employees by compensation, or (4) is a family member of another highly compensated employee for such year. Certain mechanical adjustments would be made to the top 10-percent and 3 highest-paid employee tests to take into account an employer's salary structure. Similarly, adjustments would be provided to the 3-year lookback rule to reflect significant fluctuations in an employer's workforce.	Adopts a uniform definition of highly compensated employees for purposes of the special nondiscrimination test for qualified cash or deferred arrangements and for employee benefit programs. Treats an employee as highly compensated for the current year if, at any time during the 2 preceding years, the employee was— (1) a 5-percent owner (determined with attribution rules), (2) earned more than $50,000 annually, or (3) was in the top 10 percent of all employees by pay, excluding— (i) employees who earned less than $20,000, and (ii) employees who earned less than $35,000 and were not among the top 5 percent by pay. *Current year.*—"Highly compensated employees" also includes employees who are 5-percent owners during the current year, and employees who are both in categories (2) or (3) and in the top 100 employees by pay during the current year.	Adopts a uniform definition of highly compensated employees for purposes of the coverage and nondiscrimination rules for qualified plans (including the special nondiscrimination test for qualified cash or deferred arrangements) and for employee benefit programs. An employee is treated as highly compensated for the current year if, at any time during the preceding year, the employee (1) was a 5-percent owner (determined with attribution rules), (2) earned— (a) more than $100,000 (indexed by reference to the percentage increase in the social security wage base), or (b) more than $50,000 (indexed by reference to the percentage increase in the social security wage base) and was among the top 20 percent of employees by pay, or (3) was an officer (as defined in sec. 416(i)). *Current year.*—Same as House bill.

5. Definition of highly compensated employees (cont.)			*Family members*.—Elective deferrals of (and compensation paid to) family members of— (a) 5-percent owners, and (b) the top 10 highly compensated employees by pay are aggregated with the elective deferrals of such highly compensated employees for purposes of applying the special nondiscrimination tests. A family member is defined as a spouse, parent, lineal ascendant or descendant, and a spouse of a lineal ascendant or descendant. *Effective date*.—Years beginning after 1985.	*Family members*.—Same as House bill. Also, an individual who has separated from service continues to be treated as a highly compensated employee if the individual was a highly compensated employee at separation from service or at such other times as regulations may prescribe. *Effective date*.—Years beginning after December 31, 1986, for employee benefit purposes, and December 31, 1988, for pension purposes.
6. Top-heavy plans (sec. 1115 of the House bill and sec. 1218 of the Senate amendment)	Under present law, the benefit accrual rules generally applicable to qualified defined benefit plans do not apply to the minimum benefits required under a top-heavy plan. The fractional benefit accrual rule provides that each participant's accrued benefit at the end of any year must be at least equal to an amount determined by dividing the participant's years of participation by the total number of years of participation to normal retirement age.	No provision.	Applies a uniform benefit accrual rule in testing whether a qualified defined benefit plan is top heavy. In determining whether a plan is top heavy, the fractional benefit accrual rule is applied. *Effective date*.—Effective for plan years beginning after December 31, 1985.	Same as House bill. *Effective date*.—Effective for plan years beginning after December 31, 1986.
7. Includible compensation (sec. 1103 of the House bill and sec. 1206 of the Senate amendment)	(a) *Qualified plans*.—Under present law, in the case of a qualified plan that is not top heavy, there is no limit on the amount of the annual compensation of an employee that may be taken into account under the plan. In the case of a qualified plan that is top heavy, the annual compensation of an employee taken into account under the plan may not exceed $200,000.	(a) *Qualified plans*.—No provision.	(a) *Qualified plans*.—Limits the amount of compensation that may be taken into account under any qualified plan whether or not top heavy. The limit for all qualified plans is 7 times the defined contribution dollar limit (under the bill, for 1986, 7 times $25,000, or $175,000). The limit will be increased as the defined contribution plan dollar limit is increased. This limit applies for all qualification purposes including testing for discrimination (secs. 401(a)(4) and 401(k)(3)).	(a) *Qualified plans*.—Limits the amount of compensation that may be taken into account under any qualified plan, whether or not top heavy. The limit for all qualified plans is set initially at $200,000 and is indexed by reference to percentage increases in the social security wage base. The limit applies for all qualification purposes including testing for discrimination (e.g., secs. 401(a)(4) and 401(k)(3)).

Item	Present Law	President's Proposal	House Bill	Senate Amendment
7. Includible compensation (sec. 1103 of the House bill and sec. 1206 of the Senate amendment) (cont.)	(b) *SEPs*.—In the case of a simplified employee pension (SEP), the annual compensation of an employee taken into account under the plan may not exceed $200,000.	(b) *SEPs*.—No provision.	(b) *SEPs*.—No provision. *Effective date*.—Generally effective for years beginning after December 31, 1985.	(b) *SEPs*.—Same as present law, but the $200,000 amount is indexed by reference to percentage increases in the social security wage base. *Effective date*.—Generally effective for years beginning after December 31, 1988, with respect to benefits accrued after that date.
8. Benefit forfeitures (sec. 1116 of the House bill and sec. 1219 of the Senate amendment	Forfeitures in a money purchase pension plan may not be reallocated to remaining participants, but must be used to reduce future employer contributions or to offset plan administrative expenses.	The proposal would permit forfeitures to be reallocated to remaining participants. *Effective date*.—The proposal would apply to plan years ending after December 31, 1985.	Same as President's proposal. *Effective date*.—Same as President's proposal.	Same as President's proposal and House bill. *Effective date*.—Same as President's proposal and House bill.
9. Vesting (sec. 1213 of the Senate amendment)	(a) *In general*.—Present law requires that a participant's employer-provided benefits be vested— (1) upon attainment of normal retirement age; (2) at all times in the benefit derived from employee contributions; and (3) with respect to employer-provided benefits, at least as rapidly as under one of the following 3 alternative minimum vesting schedules: (i) full vesting is required upon completion of 10 years of service (no vesting is required before the end of the 10th year); (ii) vesting begins at 25 percent after completion of 5 years of service and increases gradually to 100 percent after completion of 15 years of service. (iii) requires 50-percent vesting after 5 years of service, and when the sum of age and years of service is 45, and an additional 10-percent vesting for each additional year of service and 2 point increases in the sum of age and years of service until 100-percent vesting is attained after 15 years of service. Faster vesting is required under present law for top-heavy plans.	(a) *In general*.—No provision.	(a) *In general*.—No provision.	(a) *In general*.—Requires that a participant's employer provided benefit under any qualified plan (other than a multiemployer plan) vest at least as rapidly as under one of the following 2 alternative vesting schedules— (1) full vesting would be required upon completion of 5 years of service. (2) vesting begins at 20 percent after completion of 3 years of service and increases by 20 percent for each subsequent year of service, until 100 percent vesting is obtained after 7 years of service. Present-law rules for top-heavy plans are retained. Conforming amendments are made to ERISA. (Floor amendment by Senators Kennedy and Hatch, adopted by voice vote.)
	(b) *Application to multiemployer plans*.—The vesting requirements apply to multiemployer plans.	(b) *Application to multiemployer plans*.—No provision.	(b) *Application to multiemployer plans*.—No provision.	(b) *Application to multiemployer plans*.—Requires that a participant's employer provided benefit under a multiemployer plan be 100 percent vested no later than upon the participant's completion of 10 years of service.

Item	Present Law	President's Proposal	House Bill	Senate Amendment
9. Vesting (cont.)	(c) *Class-year vesting.*—Special vesting rules also apply to "class year plans." A class year plan is a profit-sharing or stock bonus plan that provides for the separate vesting of employee rights to amounts derived from employer contributions on a year-by-year basis. The minimum vesting requirements are satisfied if the plan provides that a participant's right to amounts derived from employer contributions with respect to any plan year are nonforfeitable not later than the close of the fifth plan year following the plan year for which the contribution was made.	(c) *Class-year vesting.*—No provision	(c) *Class-year vesting.*—No provision.	(c) *Class-year vesting.*—Class-year vesting is not permitted to the extent it is inconsistent with the 2 alternative permitted vesting schedules. *Effective dates.*—Generally effective for plan years beginning after December 31, 1988. In the case of certain collectively bargained plans, the provision is not effective for years beginning before the earlier of— (1) the later of January 1, 1989, or the termination of the collective bargaining agreement, or (2) January 1, 1991.

C. Withdrawal of Benefits **1. Uniform minimum distribution rules (sec. 1121 of the House bill and sec. 1221 of the Senate amendment)**	Tax-favored retirement arrangements are subject to certain minimum requirements concerning the timing and amount of before-death and after-death distributions. Under these rules, distribution of a participant's benefits must commence when the participant— (1) attains age 70½, or (2) with respect to participants who are not 5-percent owners, the taxable year in which the participant retires, if later. Distributions from an IRA are required to commence when the owner attains age 70½. The first annual required distribution may be delayed until April 1 of the calendar year following the calendar year in which the individual attains age 70½ or retires, whichever is applicable. A qualified plan failing to satisfy the minimum distribution rules may be disqualified. A 50-percent excise tax applies to amounts required to be distributed from an IRA that are not distributed.	The proposal would retain the present law rules relating to benefit commencement date and would subject all qualified plans, tax-sheltered annuities and IRAs to uniform minimum distribution rules. Certain simplifying modifications would be made to those rules. Under the proposal, the uniform sanction for failure to satisfy the minimum distribution rules would be a nondeductible excise tax equal to 50 percent of the amount by which the minimum amount required to be distributed exceeds the amounts actually distributed. The recipient of the distribution would be primarily liable with a right, where appropriate, to recover the tax from the plan. The current disqualification sanction would be eliminated. *Effective date.*—The proposal generally applies for distributions made after December 31, 1985.	A uniform benefit commencement date applies to qualified plans, IRAs and tax-sheltered annuities. Distributions are required to commence no later than April 1 of the calendar year following the calendar year in which the participant attains age 70½. Subjects all qualified plans, tax-sheltered annuities, and IRAs to uniform minimum distribution rules. The sanction for failure to satisfy the minimum distribution rules in operation is a nondeductible excise tax equal to 50 percent of the amount by which the minimum amount required to be distributed exceeds the amounts actually distributed. The recipient of the distribution is liable for the tax. The current disqualification sanction for operational defects is eliminated. *Effective date.*—Effective for distributions made after December 31, 1985. An exception from the uniform commencement date is provided for individuals who are not 5-percent owners and who have attained age 70½ by January 1, 1988.	Same as House bill, except that the provision requiring that distributions from a qualified plan commence no later than April 1 of the year following the year in which a participant attains age 70½ applies only to a participant who is a highly compensated employee for any plan year ending in a calendar year after the calendar year in which the employee attains age 65½. The definition of highly compensated employee is the same as the definition for coverage and nondiscrimination purposes (See Item B.5., above). The provisions do not apply to distributions under tax-sheltered annuities. *Effective date.*—Effective for distributions made after December 31, 1986.
2. Withdrawals before age 59½ ***a. Additional income tax on early withdrawals (secs. 1111 and 1123 of the House bill and sec. 1223 of the Senate amendment)***	(a) An additional income tax is imposed on certain early withdrawals from qualified plans with respect to five-percent owners who have not attained age 59½, unless the early withdrawal is made on account of the employee's disability or death. A similar tax also applies to early withdrawals made from an IRA. *Waiver of tax.*—Present law does not provide an exception to the additional tax on early withdrawals for distributions in the form of a life annuity.	(a) The proposal would conform the early withdrawal rules for qualified plans to the rules for IRAs. Thus, an additional income tax would apply to any participant in a qualified plan or tax-sheltered annuity who receives a distribution before age 59½, death, or disability unless the distribution is made in the form of a qualifying annuity. *Waiver of tax.*—A qualifying annuity would be an annuity commencing after the participant attains age 50, payable as one of a scheduled series of substantially nonincreasing payments under— (1) an annuity for the life of the participant (or the joint lives of the participant and the participant's beneficiary), or (2) an annuity for a term certain of at least 180 months commencing upon retirement under the plan.	(a) Conforms the early withdrawal rules for qualified plans to the rules for IRAs. Thus, an additional income tax applies to any participant in a qualified plan, tax-sheltered annuity, or IRA who receives a distribution before age 59½, death, or disability, unless the distribution is made in the form of a qualifying annuity. *Waiver of tax.*—A qualifying annuity which is not subject to the additional income tax is an annuity commencing at any age and payable in substantially equal periodic payments (made not less frequently than annually) for the life of the participant (or the joint lives of the participant and the participant's beneficiary).	(a) Same as the House bill, except that— (1) the early withdrawal tax does not apply to distributions from or under a tax-sheltered annuity, (2) the tax is waived under certain additional circumstances, and (3) the rate of the tax varies depending on the character of the contribution to which the distribution relates. *Waiver of tax.*—Exempts from the additional income tax on early withdrawals— (1) any distribution that is part of a scheduled series of substantially equal periodic payments for the life (or life expectancy) of the participant (or the joint lives of the participant and the participant's beneficiary), (2) any distribution from a qualified plan to an employee (other than a 5-percent owner) who has attained age 55, separated from service, and satisfied the requirements for early retirement under the plan,

a. Additional income tax on early withdrawals (cont.)				(3) certain hardship distributions (medical, casualty, and cessation of unemployment benefits) from a qualified plan (other than to a 5-percent owner), and (4) certain distributions from an employee stock ownership plan
	Rate of tax.—The rate of tax under present law is 10 percent.	*Rate of tax.*—The rate of tax generally would be 20 percent of the amount includible in income. The tax would be reduced to ten percent if the distribution is made on account of— (1) the purchase of the individual's first principal residence, (2) the payment of college expenses for a dependent of the individual, or (3) unemployment during the period following the cessation of unemployment benefits.	*Rate of tax.*—The rate of tax is 15 percent of the amount includible in income.	*Rate of tax.*—The tax generally is increased from 10 to 15 percent for distributions from all qualified retirement plans and IRAs. In the case of— (1) the distribution of income and matching contributions (plus income) attributable to after-tax employee contributions to a qualified plan, and (2) withdrawals of income attributable to nondeductible IRA contributions, the amount of the tax is 10 percent of the amount of the distribution includible in income.
b. Tax-sheltered annuities (sec. 1122 of the House bill)	(b) Withdrawals under a tax-sheltered annuity invested in a custodial account may not commence prior to the time an employee attains age 59½, dies, becomes disabled, separates from service, or encounters financial hardship. Other tax-sheltered annuities are not subject to these withdrawal restrictions or the 10-percent additional income tax on early distributions.	(b) The proposal would eliminate financial hardship as a ground for distributions from tax sheltered annuities invested in custodial accounts and would extend the modified withdrawal restrictions applicable to tax-sheltered annuities invested in a custodial account to all tax-sheltered annuities.	(b) Extends the withdrawal restrictions currently applicable to tax-sheltered custodial accounts to all tax-sheltered annuities. Withdrawals on account of hardship from a tax-sheltered annuity or custodial account are permitted only to the extent of contributions made pursuant to a salary reduction agreement (but not earnings on those contributions). The present-law standards defining "hardship" for purposes of a CODA apply.	(b) Retains present law.
		Effective dates.—The provisions would apply for taxable years beginning after December 31, 1985. However, the early withdrawal restriction would not apply to annuities with respect to which no additional contributions were made after December 31, 1985.	*Effective dates.*—Years beginning after December 31, 1985. The provisions relating to restrictions on distributions from tax-sheltered annuity or custodial accounts do not apply to amounts contributed to tax-sheltered annuities or custodial accounts before December 31, 1985. The bill contains exceptions to the tax on early withdrawals for— (1) individuals who, as of November 6, 1985, had separated from service and had commenced receiving benefits pursuant to a written election designating a specific schedule of benefit payments, and (2) the total distribution of a participant's accrued benefit on account of a plan termination before December 31, 1985.	*Effective dates.*—Years beginning after December 31, 1986. Provides an exception to the tax on early withdrawals for individuals who, as of March 1, 1986, had separated from service and had commenced receiving benefits pursuant to a written election designating a specific schedule of benefit payments.

c. *Direct transfer option (sec. 1223 of the Senate amendment)*	(c) Under present law, if an employee's benefits are paid as a qualifying rollover distribution, all or any portion of the distribution may be rolled over, within 60 days of the date of the distribution, to an IRA or to another qualified plan If a rollover is made, tax is deferred on the portion of the distribution rolled over, and no early withdrawal tax is imposed When a qualifying rollover distribution is made, the plan administrator is required to provide notice to the recipient that— (1) the distribution will not be taxed currently to the extent transferred to another qualified plan or an IRA, and (2) the transfer must be made within 60 days of receipt in order to qualify for this tax-free rollover treatment.	(c) No provision	(c) No provision	(c) If an employee separates from service and is to receive a distribution that could be rolled over to another qualified plan or IRA, the employer is required to offer the employee the option of electing a direct transfer of the employee's accrued benefit to an IRA or to another qualified plan The notice of rollover treatment is to be revised to include a statement that the employee's distribution may be subject to an additional income tax if not rolled over to an IRA or to another qualified plan *Effective date.*—Years beginning after December 31, 1986.
3. **Uniform tax treatment of distributions (sec. 1122 of the House bill and sec. 1222 of the Senate amendment)** a. ***10-year forward income averaging and pre-1974 capital gains treatment***	(a)(1) *Averaging*—Certain lump sum distributions received under a qualified plan may qualify for special 10-year forward averaging treatment.	(a)(1) *Averaging.*—The proposal would repeal the special 10-year forward averaging treatment.	(a)(1) *Averaging.*—Substitutes 5-years for 10-year forward averaging and permits only one election of forward averaging with respect to a single lump sum distribution received after the individual attains age 59½ (except as provided under the transition rule) Effective for taxable years beginning after December 31, 1985.	(a)(1) *Averaging*—Same as House bill, effective for taxable years beginning after December 31, 1986.
	(2) *Capital gain.*—A participant may elect to treat the pre-1974 portion of any lump sum distribution from a qualified plan or tax-sheltered annuity as long-term capital gain.	(2) *Capital gain.*—The proposal would repeal the special pre-1974 capital gain treatment.	(2) *Capital gain.*—Phases out the capital gain character, of the pre-1974 portion of a lump-sum distribution over a 6-year period beginning on January 1, 1986	(2) *Capital gain.*—Same as House bill, effective on January 1, 1987

a. 10-year forward income averaging and pre-1974 capital gains treatment (cont.)		(3) *Transition rule.*—However, the repeal of capital gain treatment and 10-year forward averaging would be phased in over a 6-year period for individuals who will have attained age 55 before January 1, 1987 During the transition period, 10-year forward averaging calculations would use the present-law rate schedules	(3) *Transition rule* Any participant who attained age 50 by January 1, 1986, is permitted— (1) to make one election of 5-year forward averaging with respect to a single lump sum distribution received before age 59½, and (2) to retain the capital gain character of the pre-1974 portion of such a distribution under the 6-year phase out. An individual who separates from service during December 1985 and receives a lump sum distribution in January or February of 1986 may elect to treat the distribution as if it were received in 1985, so that it could qualify for 10-year forward averaging, and capital gain treatment, if that treatment would have been applicable to a 1985 distribution	(3) *Transition rule* Any participant who attained age 50 by January 1, 1986, is permitted— (1) to make one election of 5-year forward averaging or 10-year forward averaging (at present-law tax rates) with respect to a single lump sum distribution without regard to the attainment of age 59½, and (2) to retain the capital gain character of the pre-1974 portion of such a distribution An election under this transition rule is treated as an election of forward averaging under the general rule permitting only one such election
b. Constructive receipt	(b) Under a tax-sheltered annuity, unlike a qualified plan, a participant is taxed when benefits are received or made available.	(b) The proposal would tax participants under a tax-sheltered annuity only when benefits are received, effective for distributions after December 31, 1985.	(b) Same as President's proposal.	(b) Same as House bill and President's proposal, effective for distributions after December 31, 1986
c. Basis recovery	(c)(1) *Pre-annuity starting date.*—Distributions prior to the annuity starting date are treated as being made first out of nontaxable employee contributions and then out of taxable amounts (employer contributions and income)	(c)(1) *Pre-annuity starting date.*—With respect to distributions before the annuity starting date, the proposal would reverse the ordering rules—treating the distributions as being made first out of taxable amounts (employer contributions plus interest) and then out of nontaxable employee contributions.	(c)(1) *Pre-annuity starting date.*—Same as President's proposal	(c)(1) *Pre-annuity starting date*—Modifies the basis recovery rules for pre-annuity starting date distributions to provide for the pro rata recovery of employee contributions
	(2) *Post-annuity starting date*—Distributions after the annuity starting date are treated under the following rules (1) In general, each payment is treated as part a payment of income and part a recovery of employee contributions (2) Under a special rule, if an individual will receive all employee contributions within the first three years after the annuity starting date, then all distributions are considered a return of employee contributions until the individual's basis has been recovered	(2) *Post-annuity starting date.*—The proposal would repeal the special 3-year basis recovery rule and treat each distribution as part a payment of income and part as recovery of employee contributions, under modified basis recovery rules.	(2) *Post-annuity starting date*—Same as President's proposal	(2) *Post-annuity starting date*—Same as House bill and President's proposal

d. Effective dates		(d) *Effective dates.*—The provisions generally would apply to distributions made after December 31, 1985. In addition, the basis recovery rule applicable to distributions made before the annuity starting date would not apply to benefits accrued prior to January 1, 1986. The repeal of the 3-year basis recovery rule and the modification of the exclusion ratio would not apply to any amount received as an annuity if the annuity was in pay status on January 1, 1986	(d) *Effective dates.*—The provisions generally apply to distributions made after December 31, 1985. However, the basis recovery rule applicable to distributions made before the annuity starting date does not apply to benefits accrued prior to January 1, 1986, and such pre-1986 benefits are treated as distributed before any post-1985 benefits. The repeal of the 3-year basis recovery rule does not apply to any individual whose annuity starting date is on or before July 1, 1986.	(d) *Effective dates.*—The basis recovery rule applicable to distributions made before the annuity starting date applies to amounts received after December 31, 1986. However, in the case of a plan that, on May 5, 1986, permitted the withdrawal of employee contributions before separation from service, distributions are treated as made first out of nontaxable employee contributions made before December 31, 1986. The repeal of the 3-year basis recovery rule is fully effective with respect to an individual whose annuity starting date is after January 1, 1989 If the annuity starting date is after January 1, 1988, but on or before January 1, 1989, 50 percent of the basis is recovered under the 3-year rule, and the remaining 50 percent would be recovered under the new basis recovery rule.
4. Loans under qualified plans (sec. 1134 of the House bill and sec. 1233 of the Senate amendment) *a. Amounts treated as distributions*	(a) Subject to certain exceptions, a loan to a participant from a qualified plan is treated as a taxable distribution of plan benefits. An exception is provided to the extent that the loan, when added to the outstanding balance of all other plan loans, does not exceed the lesser of— (1) $50,000, or (2) the greater of $10,000 or one-half the participant's accrued benefit.	(a) Under the proposal, a loan would be treated as a distribution to the extent that the loan exceeds the lesser of— (1) $50,000, reduced by the highest outstanding loan balance during the prior 12 months, or (2) the greater or $10,000 or one-half of the employee's accrued benefit.	(a) Same as President's proposal	(a) Same as House bill and President's proposal
b. Repayment period	(b) The exception applies only if the loan must, by its terms, be repaid within five years, or within a reasonable period if the loan is used to acquire or improve a personal residence of the participant or family member	(b) The proposal provides an exception to the five-year repayment period only for those loans applied to the first-time purchase of the participant's principal residence.	(b) Provides an exception to the 5-year repayment period only for those loans applied to the purchase of the participant's principal residence (whether or not a first-time purchase). Requires that a plan loan be amortized in level payments, made not less frequently than quarterly over the term of loans.	(b) Provides an exception to the 5-year repayment period only for those loans applied to the purchase of the participant's principal residence or the principal residence of a descendant of the participant

c. Interest paid on plan loans	(c) Interest paid on a loan from a qualified plan is deductible.	(c) No provision *Effective date.*—The provision would be effective for amounts received as a loan after December 31, 1985.	(c) Defers the deduction for interest paid by— (1) all employees with respect to loans secured by elective deferrals under a qualified cash or deferred arrangement or tax-sheltered annuity, and (2) key employees with respect to loans from any qualified plan, by denying a deduction for the interest and increasing a participant's basis under the plan by the amount of nondeductible interest paid. *Effective date.*—Effective for amounts received as a loan after December 31, 1985.	(c) No provision (See, also, Item V C., relating to limitations on nonbusiness interest deductions.) *Effective date.*—Effective for amounts received as a loan after December 31, 1986

. Tax Deferral Under Qualified Plans **1. Overall limits on contributions and benefits (secs. 1103 and 1133 of the House bill and sec. 1206 of the Senate amendment)**				
a. Defined contribution plans	(a)(1) *Limits on contributions.*—Annual additions on behalf of a participant under a qualified defined contribution plan are limited to the lesser of (i) 25 percent of compensation, or (ii) $30,000.	(a)(1) *Limits on contributions.*—No provision.	(a)(1) *Limits on contributions.*—Reduces the dollar limit to the greater of $25,000 or 25 percent of the limit for defined benefit plans. The $25,000 limit is frozen until the dollar limit on annual benefits under a defined benefit plan reaches $100,000. After that, the dollar limit is indexed in the same manner as the dollar limit for defined benefit plans (by reference to percentage increases in the primary insurance amount under social security) so that the ratio of the defined benefit plan dollar limit to the defined contribution plan dollar limit will remain at 4/1.	(a)(1) *Limits on contributions.*—The $30,000 limit on annual additions to a defined contribution plan is frozen until the dollar limit on annual benefits under a defined benefit plan reaches $120,000. After that, the dollar limit for defined contribution plans is indexed in the same manner as the dollar limit for defined benefit plans (by reference to percentage increases in the social security wage base) so that the ratio of the defined benefit plan dollar limit to the defined contribution plan dollar limit will remain at 4/1.
	(2) *Definition of annual additions.*—Annual additions include employer contributions, forfeitures, and if employee contributions exceed six percent of compensation, the lesser of (i) one-half the employee contributions, or (ii) total employee contributions in excess of six percent of compensation.	(2) *Definition of annual additions.*—One-half of all employee contributiona would be treated as annual additions.	(2) *Definition of annual additions.*—Treats all employee contributions as annual additions.	(2) *Definition of annuol additions.*—Same as House bill.
		Effective date.—Years beginning after December 31, 1985. For collectively bargained plans, the modifications would apply to limitation years beginning after termination of the collective bargaining agreement.	*Effective date.*—Years beginning after December 31, 1985. For certain collectively bargained plans, the provision does not apply to years beginning before the earlier of— (i) the termination of the agreement, or (ii) January 1, 1991.	*Effective date.*—Years beginning after December 31, 1986. For certain collectively bargained plans, the provision does not apply to years beginning before the earlier of— (i) the termination of the agreement, or (ii) January 1, 1991.
b. Defined benefit plans	(b)(1) *Limits on benefits.*—Annual benefits commencing at any time after attainment of age 62 and payable on behalf of a participant from a qualified defined benefit plan are limited to the lesser of (i) 100 percent of compensation or (ii) $90,000. If benefits commence before age 62, the dollar limit is reduced to the acturaial equivalent of an annual benefit of $90,000 commencing at age 62. In no event, however, is the dollar limit applicable to benefits comencing at or after age 55 less than $75,000.	(b)(1) *Limits on benefits.*—No provision.	(b)(1) *Limits on benefits.*—Reduces the dollar limit for benefits commencing at ages 62 to 65 to $77,000, indexed for inflation after 1987. Provides that the limit for benefits commencing at or after age 55 is not lower than $65,000.	(b)(1) *Limits on benefits.*—Retains present law limits on benefits commencing at normal retirement age and indexes those limits by reference to the percentage increases in the social security wage base. The normal retirement age for purposes of the limit on benefits under a defined benefit plan is conformed to the social security retirement age. If the retirement benefit under a defined benefit plan begins before the social security retirement age (presently, age 65) then the $90,000 limitation on annual benefits generally is reduced so that it is the actuarial equivalent of an annual benefit of $90,000 beginning at the social security retirement age. Under tran-

b. Defined benefit plans (cont.)	If benefits under a defined benefit plan begin after age 65, the $90,000 limit is increased to the actuarial equivalent of an annual benefit of $90,000 beginning at age 65.			sition rules, benefits already accrued by a plan participant under an existing plan are not affected by the reductions for actuarial equivalence If benefits commence after the social security retirement age, the $90,000 limit is increased to the actuarial equivalent of a $90,000 benefit commencing at the social security retirement age
	(2) *Phase-in of limit.*—This limit is proportionately reduced for participants with less than ten years of service	(2) *Phase-in of limit.*—The overall limit would be reduced for participants with less than ten years of plan participation	(2) *Phase-in of limit.*—Same as President's proposal	(2) *Phase-in of limit.*—Same as House bill and President's proposal.
	(3) *Special rule for police, firefighters, and pilots.*—None	(3) *Special rule for police, firefighters, and pilots.*—No provision	(3) *Special rule for police, firefighters, and pilots.*—The limit applicable to police and firefighters is not reduced below $50,000 at any age. For airline pilots, the limit at age 60 is $77,000.	(3) *Special rule for police, firefighters, and pilots.*—Same as House bill, except that, for pilots, the limit at age 60 is $90,000, indexed to the percentage increases in the Social Security wage base. Also extends the special rule for police and firefighters to correctional officers.
	(4) *Cost-of-living arrangements.*—No special rules.	(4) *Cost-of-living arrangements.*—No provision.	(4) *Cost-of-living arrangements.*—An employer is permitted to offer employees a qualified cost-of-living arrangement that supplements benefits under a defined benefit pension plan	(4) *Cost-of-living arrangements.*—Same as House bill.
		Effective date.—The provision phasing in the requirement that the defined benefit plan dollar limit be reduced for participants with less than 10 years of participation would be phased in, becomming fully effective for years beginning after December 31, 1993.	*Effective date.*—Years beginning after December 31, 1985. For collectively bargained plans, the bill does not apply to years beginning before the earlier of— (1) the termination of the agreement, or (2) January 1, 1991.	*Effective date.*—Years beginning after December 31, 1986 For collectively bargained plans, the bill does not apply to years beginning before the earlier of— (1) the termination of the agreement, or (2) January 1, 1991 The limit phase in does not apply to benefits accrued before the effective date
c. Limit on benefits from more than one plan	(c) A combined plan limit is applied to an individual who participates in both a defined contribution plan and a defined benefit plan of the same employer equal to the lesser of (i) 125 percent of the separate plan dollar limits, or (ii) 140 percent of the separate plan percentage limits. A lower combined plan limit applies for individuals participating in a top-heavy plan. No overall limit is placed on the amount of benefits payable to an individual under plans of unrelated employers	(c) An additional 10-percent excise tax would be imposed on all participants receiving annual benefits in excess of a specified amount. To the extent that aggregate annual distributions made with respect to any individual from qualified plans, IRAs, and tax-sheltered annuities exceed that dollar amount, an excise tax equal to 10 percent of the excess would be imposed. Under the proposal, the dollar amount would be 1.25 times the defined benefit dollar limit (e.g., 1.25 times $90,000 would equal $112,500 for 1985 through 1987).	(c) Same as President's proposal, but applies a 15-percent excise tax on aggregate annual distributions from all tax-favored retirement arrangements in excess of the greater of— (1) $112,500 or (2) 1.25 times the indexed dollar limit for defined benefit plans. Applies a special higher ceiling for purposes of calculating the excess distribution for any calendar year in which the individual receives a lump distribution that is subject to long-term capital gains or 5-year averaging. The higher ceiling is the lesser of (1) the portion of the lump sum that is eligible for capital gains treatment or 5-year averaging, or (2) 5 times the otherwise applicable ceiling for such year.	(c) No provision.

c. Limit on benefits from more than one plan (cont.)			The bill also contains a special rule for post-death distributions. In lieu of subjecting post-death distributions to the annual tax on excess distributions, the bill adds an additional estate tax equal to 15 percent of the individual's excess retirement accumulation "Excess retirement accumulation" is defined as the excess of the decedent's interest in all tax-favored retirement arrangements over the present value of annual payments equal to the annual ceiling over a period equal to the life expectancy of the individual immediately before death	
		Effective date.—Years beginning after December 31, 1985.	*Effective date.*—Years beginning after December 31, 1985.	
d. Tax-sheltered annuities	(d) In the case of a tax-sheltered annuity, special one-time elections increase the overall defined contribution plan limit. The special elections allow certain catch-up contributions in a year, to the extent permitted by the section 403(b) exclusion allowance. An additional election permits a church employee to elect to increase the overall limit by up to $10,000 for any year, not to exceed a lifetime amount of $40,000 for an employee. The catch-up elections are available to employees of an educational organization, a hospital, a home health service agency, or a church, convention, or association of churches.	(d) The special catch-up elections would be repealed *Effective date.*—Years beginning after December 31, 1985.	(d) Retains special catch-up elections	(d) The special catch-up elections are retained and extended to employees of certain health and welfare service agencies *Effective date.*—Years beginning after December 31, 1986
2. Deductions for contributions to qualified plans (sec. 1131 of the House bill and sec. 1231 of the Senate amendment)				
a. Profit-sharing and stock bonus plans	(a)(1) *Coordination with social security integration.*—In the case of a profit-sharing or stock bonus plan that is integrated with social security, the limit on deductible employer contributions is not reduced by the employer share of social security taxes taken into account under the plan. (2) *Limit carryforward*.—Employer contributions in excess of the deduction limits may be carried over and deducted in later years. If the contribution for a particular year is lower than the deduction limit, the unused limit may be carried over and used in later years	(a)(1) *Coordination with social security integration.*—No provision. (2) *Limit carryforward.*—The present-law carryforward for unused deduction limits would be repealed except under certain "retirement type" profit-sharing plans. A profit-sharing plan would be treated as a "retirement type" plan with respect to an individual if, for each of the preceding 10 years— (1) the individual is an active participant in the plan,	(a)(1) *Coordination with social security integration.*—In the case of a profit-sharing or stock bonus plan integrated with social security, reduces the deduction limit by the employer share of social security taxes taken into account under the plan (2) *Limit carryforward.*—Repeals the limit carryforward for all profit-sharing and stock bonus plans (including retirement-type plans).	(a)(1) *Coordination with social security integration.*—Retains present law (2) *Limit carryforward*.—Same as House bill

a. Profit-sharing and stock bonus plans (cont.)		(2) the individual is not a participant in any other profit-sharing or stock-bonus plan maintained by the employer, (3) contributions are based on a formula using a reasonable year-of-service factor, (4) certain benefits are not available before separation from service, death or disability, and (5) the plan is not top-heavy.		
b. Combination of pension and other plan	(b) Employer contributions to a money purchase pension plan are generally deductible under rules applying to pension plans The amount required under the minimum funding standard is t he contribution rate specified by the plan, which cannot exceed 25 percent of a participant's compensation If an employer maintains a pension plan (defined benefit or money purchase) and either a profit-sharing or stock bonus plan for the same employee, then the employer's deduction for contributions for that year is generally limited to the greater of— (1) the amount needed to satisfy the minimum funding requirements of the pension plan, or (2) 25 percent of the aggregate compensation of covered employees This limit does not apply when an employee participates in both a defined benefit and a money purchase pension plan of the same employer	(b) The proposal would extend the 25-percent of aggregate compensation limit to all combinations of defined benefit and money purchase pension plans	(b) Same as President's proposal.	(b) Same as House bill and President's proposal
c. Nondeductible contributions	(c) Employer contributions in excess of the deduction limit may be carried over and deducted in later years	(c) Employer contributions in excess of the deductible limits would be subject to a ten percent annual nondeductible excise tax until the excess is eliminated *Effective dates.*—The proposals generally would be effective for years beginning after December 31, 1985. Special transition rules would maintain certain limit carryforwards and permit the deduction of excess contributions carried forward from years before the effective date.	(c) Same as President's proposal. *Effective dates* —Effective for years beginning after December 31, 1985. Under a special rule, an employer may use pre-1986 limitation carry forwards.	(c) Retains present law *Effective dates* —Effective for years beginning after December 31, 1986. Under a special rule, an employer may use pre-1987 limitation carryforwards.

3. Asset reversions under qualified plans (sec. 1132 of the House bill and sec. 1232 of the Senate amendment)	Prior to the satisfaction of all liabilities with respect to employees and beneficiaries, assets held under a qualified plan generally may not be used for, or diverted to, purposes other than the exclusive benefit of employees. However, assets remaining in the plan upon plan termination generally may be paid to the employer after plan benefits, accrued to the date of the plan termination, have been provided. Assets reverted to the employer are includible in the employer's gross income.	To recapture a portion of the tax benefits of deferral of tax on earnings on previously deducted plan contributions, the proposal would impose a nondeductible excise tax equal to 10 percent of the plan funds reverting to the employer upon plan termination. *Effective date.*—The 10 percent recapture tax would apply to qualified plan assets reverting to an employer pursuant to a plan termination occurring after December 31, 1985.	Same as President's proposal *Effective date.*—Same as President's proposal.	Same as House bill and President's proposal, except— (a) the excise tax applies to any direct or indirect recovery of assets by the employer, and (b) a special rule applies in the case of an amount transferred from a defined benefit pension plan to an ESOP The excise tax is waived in the case of a reversion (pursuant to a termination within 1 year of the date of enactment) by a certain corporation *Effective date.*—Same as House bill and President's proposal, unless the reversion is attributable to a plan termination occurring on or before December 31, 1985.

Item	Present Law	President's Proposal	House Bill	Senate Amendment
E. Miscellaneous Pension and Deferred Compensation Provisions				
1. Discretionary contribution plans (sec. 1112 of the House bill and sec. 1235 of the Senate amendment)	Under certain types of plans, including profit-sharing plans, the level of employer contributions to the plan may vary from year to year at the discretion of the employer. An employer's discretion over the level of contributions to a profit-sharing plan is limited by the requirement that the employer's contribution to the plan in any given year may not exceed the employer's current or accumulated profits.	No provision.	Employer contributions to a profit-sharing plan that satisfy the immediate vesting and withdrawal restrictions applicable to elective deferrals under a cash or deferred arrangement (CODA) are not limited to the employer's current or accumulated profits (whether or not the plan contains a CODA). *Effective date.*—Years beginning after December 31, 1985.	Employer contributions to a profit-sharing plan are not limited to the employer's current or accumulated profits. *Effective date.*—Years beginning after December 31, 1986.
2. Requirement that collective bargaining agreement be bona fide (sec. 1138 of the House bill and sec. 1236 of the Senate amendment)	Under present law, many of the nondiscrimination standards of the Code applicable to qualified plans apply separately to plans or programs maintained pursuant to an agreement that is found to be a collective bargaining agreement if there is evidence that retirement benefits were the subject of good faith bargaining between the employer and employee representatives. Similar exclusions are provided with respect to certain welfare benefits provided to employees. Present law provides no clear definition of a collective bargaining agreement.	No provision.	No agreement is treated as a collective bargaining agreement unless it is a bona fide agreement between bona fide employee representatives and one or more employers. *Effective date.*—Date of enactment.	Same as House bill. *Effective date.*—Same as House bill.
3. Penalty for overstatement of pension liabilities (sec. 1139 of the House bill)	A penalty may apply if deductions are based on a significant overstatement of the value of an item (such as a charitable deduction). The level of the penalty varies, depending on the degree of the overstatement. A similar penalty applies to underpayments of estate or gift tax due to valuation understatements. There is no current penalty for an overstatement of liabilities under a pension plan.	No provision.	Provides a new penalty on actuaries for underpayments of tax due to overstatements of liabilities under a pension plan. New penalty would be similar to the current overvaluation penalty. *Effective date.*—Overstatements with respect to 1986 and later returns.	No provision.

Item	Present Law	President's Proposal	House Bill	Senate Amendment
4. Treatment of certain fishermen as self employed (sec. 1237 of the Senate amendment)	Under present law, certain fishermen who otherwise would be treated as common-law employees under the usual rules for determining an employer-employee relationship are treated as self-employed individuals for purposes of employment taxes (secs 3121(b)(20) and 3306(c)(20)). The IRS has held that, although these fishermen are treated as self-employed individuals for employment tax purposes, they are treated as employees for purposes of determining whether a pension, profit-sharing, or stock bonus plan maintained by the owner or operator of the boat (or boats) on which the fishermen work is a qualified plan under section 401(a).	No provision	No provision.	Members of fishing boat crews (described in sec 3121(b)(20)) are treated as self-employed individuals for purposes of the rules relating to qualified pension, profit-sharing, or stock bonus plans *Effective date* —Taxable years beginning after December 31, 1986
5. Cash out of certain accrued benefits (sec. 1238 of the Senate amendment)	A pension, profit-sharing, or stock bonus plan may not immediately distribute any portion of a participant's benefit without the participant's consent, if the present value of the participant's accrued benefit exceeds $3,500. The interest rate used in determining the present value of a benefit may not exceed the interest rate that would be used by the Pension Benefit Guaranty Corporation (PBGC) for purposes of determining the present value of a lump sum distribution upon termination of the plan.	No provision.	No provision.	A plan is required to compute the first $3,500 of the present value of a benefit by using an interest rate no greater than the interest rate (deferred or immediate, whichever is appropriate) that would be used by the PBGC upon the plan's termination The remaining portion of the present value of the benefit is required to be determined using an interest rate no greater than 120 percent of the interest rate (deferred or immediate, whichever is appropriate) that would be used by the PBGC upon the plan's termination. A conforming amendment is made to ERISA (floor amendment by Senators Kennedy and Hatch, adopted by voice vote). *Effective date.*—Distributions after December 31, 1984 The amendment does not apply to distributions that were made after December 31, 1984, and before the date of enactment, if such distributions were made in accordance with the requirements of regulations issued under the Retirement Equity Act of 1984

6. Time required for plan amendments; issuance of regulations and development of sec. 401(k) model and master and prototype plans (sec. 1137 of the House bill and secs. 1239–1241 of the Senate amendment)	(a) *Time required for plan amendments.*—If the requirements applicable to qualified plans are changed, present law generally requires that conforming plan amendments be adopted no later than the last day of the first plan year after the effective date of the change, and the amendments must be effective, for all purposes, not later than the first day of that plan year.	(a) No provision	(a) Provides that a plan will not fail to be a qualified plan on account of changes made in the bill for any year beginning before January 1, 1988, provided— (1) the plan complies, in operation, with the changes as of any separately stated effective date; (2) the plan is amended to comply with the changes no later than the last day of the first plan year beginning after December 31, 1987; and (3) the amendment applies retroactively to the first day of the first plan year beginning on or after the separately stated effective date In addition, collectively bargained plans will not fail to be qualified plans for any year beginning before the later of— (1) January 1, 1988, or (2) the earlier of (a) January 1, 1991, or (b) the first plan year beginning after the termination of the collective bargaining agreement.)	(a) Provides that a plan will not fail to be a qualified plan on account of changes made in the bill for any year beginning before January 1, 1989, provided— (1) the plan complies, in operation, with the changes as of any separately stated effective date, (2) the plan is amended to comply with the changes no later than the last day of the first plan year beginning after December 31, 1988, and (3) the amendment applies retroactively to the separately stated effective date. In addition, collectively bargained plans will not fail to be qualified plans for any year beginning before the later of— (1) January 1, 1991, or (2) the earlier of (a) January 1, 1989, or (b) the first plan year beginning after the termination of the collective bargaining agreement.
	(b) *Issuance of regulations.*—No provision.	(b) No provision.	(b) No provision	(b) Provides that the Secretary is to issue final regulations by February 1, 1988, with respect to— (1) the rules relating to the integration of benefits under qualified plans, (2) the coverage requirements applicable to qualified plans, (3) the amendments applicable to qualified cash or deferred arrangements (sec. 401(k) plans), and (4) the new nondiscrimination rules for employer matching and employee contributions (sec. 401(m)).
	(c) *Development of section 401(k) model and master and prototype plans.*—The Secretary is not required under present law to publish a section 401(k) model plan or to issue opinion letters with respect to master and prototype section 401(k) plans	(c) No provision.	(c) No provision	(c) Provides that the Secretary is to publish, no later than May 1, 1987, a model plan document for qualified plans that include cash or deferred arrangements. By May 1, 1987, the Secretary is to begin issuing opinion letters with respect to section 401(k) master and prototype plans.
			Effective date.—Date of enactment.	*Effective date.*—Date of enactment

Item	Present Law	President's Proposal	House Bill	Senate Amendment
7. Retirement Equity Act of 1984 (REA) effective date (sec. 1243 of the Senate amendment)	Under REA, a pension plan is to provide automatic survivor benefits— (1) in the case of a participant who retires under the plan, in the form of a qualified joint and survivor annuity, and (2) in the case of a vested participant who dies before the annuity starting date (the first period for which an amount is received as an annuity, whether by reason of death or disability, under the plan) and who has a surviving spouse, in the form of a qualified preretirement survivor annuity. The qualified joint and survivor and preretirement survivor annuity provisions apply to any participant who performs at least one hour of service under the plan on or after the date of enactment. REA provided a special transition rule for participants who separated from service before the date of enactment and whose benefits were not in pay status as of the date of enactment. This provision applies if— (1) a participant completed at least 1 hour of service under the plan after September 1, 1974, (2) the participant separated from service before the first day of the first plan year beginning on or after January 1, 1976, and (3) the plan is required to provide a qualified joint and survivor annuity. Under the special rule, the participant is to be provided the right to elect to receive benefits in the form of a qualified joint and survivor annuity.	No provision	No provision.	Exempts a plan from the survivor benefits requirements of REA if— (1) the plan was established prior to January 1, 1954, as a result of an agreement between employee representatives and the Federal Government during a period of Government operation, under seizure powers, of a major part of the productive facilities of the industry, and (2) under the plan, participation is substantially limited to participants who, before January 1, 1976, ceased employment covered by the plan. (Floor amendment by Senator Byrd, adopted by voice vote.) *Effective date.*—Date of enactment.

F. Employee Benefits				
1. Statutory employee benefit exclusions (secs. 121 and 1161 of the House bill and secs. 1261 and 1262 of the Senate amendment)				
a. Exclusions from income *(1) Prepaid legal services*	(a) *Exclusions from income.*—Present law provides specific income tax and employment tax exclusions with respect to the following benefits provided by an employer to employees.	(a) *Exclusions from income.*—The President's proposal would make the following changes in the tax treatment of employer-provided employee benefits	(a) *Exclusions from income.*—The House bill makes the following changes in the treatment of employer-provided employee benefits.	(a) *Exclusions from income.*—The amendment makes the following changes in the treatment of employer-provided employee benefits
(1) Prepaid legal services	(1) Benefits under prepaid legal services plans (expired after 1985).	(1) The exclusion for prepaid group legal services would be made permanent. The exclusion would be available only to the extent that employer contributions to the plan are fixed before the beginning of the year for which benefits are provided.	(1) Extends the exclusion for prepaid legal services for 2 years through 1987.	(1) The exclusion is made permanent.
(2) Employer-provided transportation	(2) Commuting through use of a van pool (expired after 1985).	(2) The exclusion for employer-provided transportation would be allowed to expire at the end of 1985, as scheduled under present law	(2) Same as President's proposal, i.e., the exclusion for employer-provided transportation is not reinstated.	(2) Same as House bill and President's proposal.
(3) Employee educational assistance	(3) Up to $5,000 annually of employee educational assistance (expired after 1985).	(3) The employee educational assistance exclusion would be made permanent. The $5,000 annual cap on educational assistance would be repealed	(3) Extends the exclusion for educational assistance for 2 years through 1987, and retains the $5,000 cap on annual benefits.	(3) Makes the exclusion for employee educational assistance permanent, and provides that the cap on the annual exclusion equals $5,250, indexed by reference to percentage increases in the social security taxable wage base.
(4) Dependent care assistance	(4) Dependent care assistance	(4) Present law would be retained.	(4) Limits the exclusion for dependent care assistance to $5,000 a year ($2,500 for a married individual filing separately).	(4) Retains present law
b. Effective date		(b) *Effective date*.—Effective for taxable years beginning after December 31, 1985.	(b) *Effective date.*—Effective for taxable years beginning after December 31, 1985.	(b) *Effective dates*.—Effective for taxable years beginning after December 31, 1986, except that the provisions relating to prepaid legal services and employee educational assistance are effective for years after December 31, 1985.

2. **Nondiscrimination requirements for employee benefit plans (sec. 1151 of the House bill and sec. 1251 of the Senate amendment)** *a. General rule*	(a) Under present law, exclusions for most of the statutory employee benefits are conditioned on compliance with various rules prohibiting discrimination in favor of certain employees. Nondiscrimination rules are provided for— (1) group-term life insurance, (2) self-insured medical reimbursement plans, (3) qualified tuition reduction, (4) group legal services, (5) cafeteria plans, (6) educational assistance, (7) dependent care assistance, (8) nonadditional-cost services, qualified employee discounts, and subsidized eating facilities, and (9) welfare benefit funds. These nondiscrimination rules generally prohibit discrimination as to eligibility to participate and as to benefits provided. In addition, certain benefits are subject to concentration tests, which limit the exclusion if more than a specified percentage of total benefits are provided to certain owners.	(a) The President's proposal would establish uniform nondiscrimination rules for eligibility and benefits and a uniform concentration test for— (1) group-term life insurance, (2) health plans (whether or not insured), (3) group legal services, (4) employee educational assistance, (5) dependent care assistance, (6) cafeteria plans, (7) qualified employee discounts, no-additional-cost services, and subsidized eating facilities, (8) qualified tuition reductions, and (9) welfare benefit funds.	(a) Establishes uniform nondiscrimination rules as to eligibility and benefits for— (1) group-term life insurance, (2) health plans (whether or not insured), (3) group legal services, (4) educational assistance, (5) dependent care assistance, (6) cafeteria plans, and (7) welfare benefit funds.	(a) The following modifications (as more fully described below) to the present-law nondiscrimination rules are made— (1) extends nondiscrimination rules to health plans (whether or not insured) and applies the same requirements to group-term life insurance plans; (2) applies a concentration test to health plans and group-term life insurance plans; (3) establishes, for all employee benefit plans, a uniform definition of highly compensated employees (i.e., employees in whose favor discrimination is prohibited); (4) establishes, for all employee benefit plans, a uniform definition of employees who can be excluded from consideration in testing whether a plan is discriminatory; (5) with respect to all employee benefit plans, requires that the employer provide reasonable notification to all eligible employees of their eligibility to participate in the plan; and (6) with respect to employee benefit plans other than health and group-term life insurance plans, establishes alternative nondiscrimination rules that a plan may satisfy in lieu of the present-law tests.

Item	Present Law	President's Proposal	House Bill	Senate Amendment
b. Definition of employees in whose favor discrimination is prohibited	(b) Under present law, benefits under the following plans may not discriminate in favor of officers, shareholders (or owners), or highly compensated employees: (1) qualified tuition reductions, (2) group legal services, (3) educational assistance, (4) dependent care assistance, and (5) no-additional-cost services, qualified employee discounts, and subsidized eating facilities. A group-term life insurance plan may not discriminate in favor of key employees, which includes— (1) officers, (2) top-10 owner-employees, (3) 5-percent owners, and (4) 1-percent owners who earn more than $150,000. A self-insured medical reimbursement program may not discriminate in favor of— (1) the 5 highest paid officers, (2) 10-percent shareholders, or (3) the 25-percent highest paid of all employees (excluding employees who may be excluded from consideration under the eligibility test). For purposes of the cafeteria plan nondiscrimination rules, a definition is provided for highly compensated individuals and for key employees. Highly compensated individuals include— (1) officers, (2) 5-percent shareholders, (3) highly compensated employees, and (4) spouses or dependents of such individuals. Key employees include the same employees as provided for group-term life insurance. Under a welfare benefit fund, a highly compensated employee means— (1) one of the 5 highest paid officers, (2) 10-percent shareholders, and (3) employees who are among the highest paid 10 percent of all employees (other than excludable employees).	(b) The proposal would provide a uniform definition of highly compensated employees.	(b) Provides a uniform definition of highly compensated employees, in whose favor discrimination is prohibited (See the description in Item B.5., above.) Provides that a former employee is a highly compensated employee if such employee was highly compensated at separation from service or at any time after attainment of age 55. The definition of "highly compensated employees" applies for purposes of the nondiscrimination rules for— (1) group-term life insurance, (2) health plans, (3) group legal services, (4) cafeteria plans, (5) educational assistance, (6) dependent care assistance, and (7) welfare benefit funds.	(b) Provides a uniform definition of highly compensated employees, in whose favor discrimination is prohibited (See the description in Item B.5., above.) Provides that a former employee is a highly compensated employee if such employee was highly compensated at separation from service or at such other times as prescribed in regulations. The definition of "highly compensated employees" applies for purposes of the nondiscrimination rules for— (1) group-term life insurance, (2) health plans, (3) qualified tuition reduction, (4) group legal services, (5) cafeteria plans, (6) educational assistance, (7) dependent care assistance, (8) no-additional-cost services, qualified employee discounts, and subsidized eating facilities, and (9) welfare benefit funds.

c. Excludable employees	(c) Under present law, for purposes of testing whether a plan is nondiscriminatory, certain employees can be disregarded In the case of a group legal services plan, educational assistance plan, or a dependent care assistance plan, employees covered under a collective bargaining unit may be disregarded if the benefit was the subject of good faith bargaining Under a group-term life insurance plan, the following employees may be disregarded— (1) employees who have less than 3 years of service, (2) part-time or seasonal employees, (3) collective bargaining employees (if the benefit was the subject of good faith bargaining), and (4) nonresident aliens.	(c) Certain classes of employees would be disregarded in applying the 125-percent eligibility test. Thus, under the proposal, the following employees need not be taken into account in testing whether a plan provides nondiscriminatory coverage— (1) if the plan so provides, employees with less than one year of service (30 or 90 days, in the case of an employer-maintained health plan), (2) if the plan so provides, part-time and seasonal employees, (3) employees covered by certain collective bargaining agreements, and (4) nonresident aliens who have no U.S. earned income.	(c) The following employees generally may be disregarded in testing whether the nondiscriminatory eligibility test is satisfied— (1) employees who have not completed 180 days of service, (2) employees who work less than 20 hours per week, (3) employees who normally work fewer than 1000 hours a year (seasonal employees), (4) employees included in a collective bargaining unit if benefits were the subject of good faith bargaining, (5) employees who have not attained age 21, and (6) nonresident aliens.	(c) The following employees generally may be disregarded in testing whether the nondiscriminatory eligibility test is satisfied— (1) in the case of core health plans, employees who have not completed 180 days of service, (2) in the case of a plan (other than core health), employees who have not completed 1 year of service, (3) employees who work less than half time, (4) employees who normally work fewer than 6 months a year (seasonal employees), (5) employees included in a collective-bargaining unit if the benefits were the subject of good faith bargaining, (6) employees who have not attained age 21, and (7) nonresident aliens
	Under a self-insured medical reimbursement plan, the following employees may be excluded from consideration— (1) employees with less than 3 years of service, (2) part-time and seasonal employees, (3) employees who have not attained age 25, (4) collective bargaining employees (if the benefit was the subject of good faith bargaining), and (5) nonresident aliens. For purposes of the cafeteria plan nondiscrimination rules, employees with less than 3 years of service may be disregarded. Under a welfare benefit fund, the following employees may be disregarded— (1) employees who have not completed 3 years of service, (2) employees who have not attained age 21, (3) seasonal or less than half-time employees, (4) collective bargaining employees (if the benefits were the subject of good faith bargaining), and (5) nonresident aliens.		The definition applies for purposes of the nondiscrimination rules for— (1) group-term life insurance, (2) health plans, (3) group legal services, (4) cafeteria plans, (5) educational assistance, (6) dependent care assistance, and (7) welfare benefit funds	The definition applies for purposes of the nondiscrimination rules for— (1) group-term life insurance, (2) health plans, (3) qualified tuition reduction, (4) group legal services, (5) cafeteria plans, (6) educational assistance, (7) dependent care assistance, (8) no-additional-cost services, qualified employee discounts, and subsidized eating facilities, and (9) welfare benefit funds

d. Rules for health plans	(d) Under present law, no nondiscrimination rules apply to insured health plans. In the case of self-insured medical reimbursement plans, present law provides a nondiscriminatory eligibility test and a nondiscriminatory benefits test. *Eligibility test*.—The eligibility test for a self-insured health plan is satisfied if the plan— (1) benefits 70 percent of all employees; (2) benefits 80 percent of eligible employees and 70 percent of all employees are eligible; or (3) benefits a nondiscriminatory classification of employees.	(d) The President's proposal would provide a uniform eligibility, benefits, and concentration test applicable to all employee benefit plans *Eligibility test*.—Under the President's proposal, the percentage of highly compensated employees benefiting under a health plan could not exceed 125 percent of the percentage of all other employees benefiting under the plan. Under certain very limited circumstances in the case of compelling business reason (such as a merger), the IRS could waive the 125 percent test in favor of a more liberal test for a period of time.	(d) The House bill provides a uniform eligibility and benefits test to all employee benefit plans, including health plans. *Eligibility test*.—Under the eligibility test, 90 percent of all employees must be eligible to participate in a plan. In addition, a plan may not contain a provision relating to eligibility that discriminates in favor of highly compensated employees.	(d) The amendment extends uniform nondiscrimination requirements to health plans. *Eligibility test*.—Under the eligibility test, a plan must— (1) benefit at least 80 percent of all employees, (2) benefit a reasonable classification of employees that does not discriminate in favor of highly compensated employees, (3) meet an alternative reasonable classification test, or (4) meet an average income exclusion test. *Reasonable classification test*.—A plan meets the reasonable classification test if the Secretary of the Treasury determines that it covers a reasonable classification of employees that is found not to discriminate in favor of highly compensated employees. The Secretary of the Treasury is directed that the disparity between the coverage percentage of highly compensated employees and the coverage percentage of nonhighly compensated employees permitted under Rev. Rul. 83-58 is excessive. In addition, the amendment clarifies that reasonable disparities between the coverage percentage of highly compensated employees and the coverage of nonhighly compensated employees are permitted if justified by the attendant facts and circumstances. The test may be applied on a line of business or operating unit basis.

d. Rules for health plans (cont.)				*Alternative reasonable classification test.*—A plan satisfies the alternative reasonable classification test if— (1) the plan satisfies the present-law fair cross-section test but not the reasonable classification test, and (2) the average benefit as a percentage of compensation for employees not covered under the plan is at least 60 percent of the average benefit percentage for employees covered under the plan, and (3) in the case of a health plan, at least 80 percent of the employer's nonhighly compensated employees are eligible to participate in a plan providing average benefits equal to at least 40 percent of the average benefits provided to employees covered by the plan being tested. The test may be applied on a line of business or operating unit basis *Average income exclusion test.*—A plan meets the requirements of the average income exclusion test if— (1) the employer elects the application of the test with respect to all health plans, and (2) the average amount provided under the plans for nonhighly compensated employees of that employer is at least 80 percent of the average amount provided for highly compensated employees The test may be applied on a line of business or operating unit basis
		Line of business.—The eligibility test could not be satisfied on a line of business or operating unit basis.	*Line of business.*—Under certain circumstances, the eligibility test may be applied separately with respect to employees in a separate line of business or operating unit of the employer. The bill requires that in order for the line of business or operating unit exception to apply— (1) the line of business must have at least 100 employees, and (2) at least 5 percent, but not more than 25 percent, of the employees in the line of business or operating unit are highly compensated.	*Line of business.*—The reasonable classification test, the alternative reasonable classification test, and the average income exclusion test may be applied separately to a line of business or operating unit of the employer if the employer demonstrates to the satisfaction of the Secretary that such line of business or operating unit is operated separately for bona fide business reasons A separate line of business or operating unit is treated as operated for bona fide business reasons if such line of business or operating unit is a separate self-sustaining unit and (1) such line of business or operating unit has at least 50 employees, (2) the percentage of highly compensated employees within such line of business or operating unit is not less than 50 percent of the percentage of highly compensated employees of the employer or at least 10 percent of the

d. Rules for health plans (cont.)				highly compensated employees of the employer perform services solely for the line of business or operating unit, and (3) the percentage of highly compensated employees within such line of business or operating unit is not more than 200 percent of the percentage of highly compensated employees of the employer Such separate testing on a line of business or operating unit basis does not apply to a plan that does not satisfy the present-law fair cross-section test applicable to qualified pension plans.
	Benefits test.—Under the benefits test for self-insured health plans, the contributions or benefits provided may not discriminate in favor of highly compensated employees.	*Benefits test.*—The proposal would require that all types and levels of benefits available to any highly compensated employee must be available to all nonhighly compensated participants. Similarly, any condition for receipt of a benefit would be required to be applied in a nondiscriminatory manner	*Benefits test.*—The benefits test requires that the coverage provided under a health plan be the same for each participant in the plan A limited exception to this requirement is provided for employees who normally work fewer than 30 hours per week In addition, in the case of a health plan in which more than 25 percent of the participants are highly compensated, the plan is considered discriminatory unless— (1) the plan actually covers at least 75 percent of those employees eligible to participate in the plan; or (2) the plan, when aggregated with a comparable plan (or plans), satisfies the 25-percent test. Two or more plans are considered comparable if the average employer cost per participant in the plan or plans is at least 80 percent of the average employer cost per participant in a plan that would otherwise fail the nondiscrimination test.	*Benefits test.*—No separate benefits test is provided for health plans because the eligibility test also operates as a benefits test
		Concentration test.—Under the concentration test, the contributions provided to the top 20 (by pay) highly compensated employees could not exceed 25 percent of the total contributions provided under the plan for any year.	*Concentration test.*—No provision.	*Concentration test* —No more than 40 percent of the employees benefiting under a health plan may be highly compensated employees A plan is not treated as failing to meet this requirement if it benefits all employees of the employer
e. Eligibility test for plans other than health plans	(e) Under present law, the following benefits must be available to a classification of employees that does not discriminate in favor of officers, shareholders (or owners), highly compensated employees, or dependents of any such employees: (1) qualified tuition reduction, (2) educational assistance, (3) dependent care assistance, and	(e) Under the President's proposal, the percentage of highly compensated employees benefiting under a plan could not exceed 125 percent of the percentage of all other employees benefiting under the plan Under certain very limited circumstances in the case of compelling business reason (such as a merger), the IRS could waive the 125	(e) Under the eligibility test, 90 percent of all employees must be eligible to participate in a plan. In addition, a plan may not contain a provision relating to eligibility that discriminates in favor of highly compensated employees.	(e) Retains present law eligibility tests applicable to employee benefit plans other than group-term life insurance, but provides the average income exclusion test (see the description in d., above) as an alternative test to certain eligibility tests Applies the same nondiscrimination tests to group-term life insurance plans as the tests for health plans

Item	Present Law	President's Proposal	House Bill	Senate Amendment
e. Eligibility test for plans other than health plans (cont.)	(4) no-additional-cost services, qualified employee discounts, and subsidized eating facilities Group legal services plans, cafeteria plans, and welfare benefit funds must benefit (rather than merely be available to) a classification of employees that does not discriminate in favor of officers, shareholders, and highly compensated employees. A cafeteria plan maintained pursuant to a collective bargaining agreement is treated as nondiscriminatory. A group-term life insurance plan must meet one of the following eligibility tests— (1) the plan benefits 70 percent of all employees, (2) at least 85 percent of the participants are not key employees, (3) the plan benefits a nondiscriminatory classification of employees, or (4) if the plan is part of a cafeteria plan, the requirements relating to cafeteria plans are met. In applying the nondiscrimination tests to certain statutory fringe benefits, all employees of employers that are under common control are aggregated and treated as if employed by a single employer.	percent test in favor of a more liberal test for a period of time.	Under certain circumstances, the eligibility test may be applied separately with respect to employees in each separate line of business or operating unit of the employer. The bill requires that, in order, for the line of business or operating unit exception to apply— (1) the line of business or operating unit must have at least 100 employees, and (2) at least 5 percent, but not more than 25 percent, of the employees in the line of business or operating unit are highly compensated.	
f. Benefits tests for plans other than health plans	(f) Under present law, the contributions or benefits provided under a group legal services plan may not discriminate in favor of highly compensated employees. Under a group-term life insurance plan, the type and amount of benefits available under the plan may not discriminate in favor of key employees. The test is satisfied if the benefits bear a uniform relationship to compensation. A cafeteria plan may not discriminate in favor of highly compensated participants as to contributions or benefits, which requires that nontaxable benefits and total benefits (or employer contributions for total benefits) be nondiscriminatory. A special rule applies to health benefits. Under a welfare benefit fund, the benefits provided under each class may not discriminate in favor of highly compensated employees. Life insurance, disability, severance pay, and supplemental unemployment compensation benefits are not considered nondiscriminatory merely be-	(f) Under the President's proposal, all types and levels of benefits available to any highly compensated participant must also be available to all nonhighly compensated participants. Similarly, any condition for receipt to a benefit would be required to be applied in a nondiscriminatory manner. The proposal would apply a nondiscriminatory benefits test to group-term life insurance, health benefits, and group legal services benefits provided under a permanent and enforceable plan. This test would apply whether or not the benefit was provided through insurance or self-insured by an employer. Certain benefits would be permitted to vary by compensation level. Under the proposal, employee educational assistance benefits, dependent care assistance, miscellaneous fringe benefits, and qualified tuition reductions would also be subject to a nondiscriminatory benefits test under which the average amount of benefits provided to highly compensated employees could not exceed 125 percent of the average amount of benefits provided to other em-	(f) Requires that the coverage provided under a group-term life insurance plan or group legal services plan be the same for each participant in the plan, regardless of whether the benefit is provided through insurance or self-insured by the employer. In the case of group-term life insurance plans and group legal services, 75 percent of all employees who are eligible to participate in the plan must actually be covered by the plan. An educational assistance plan or dependent care assistance plan is considered discriminatory unless (a) all benefits available to highly compensated employees are available on the same terms and conditions to all other employees eligible to participate in the plan; and (b) the average benefit provided to nonhighly compensated employees is at least 80 percent of the average benefit provided to highly compensated employees.	(f) Retains present law benefits tests applicable to group-term life insurance, group legal services, cafeteria plans, and welfare benefit funds, but provides the average income exclusion test as an alternative test.

	Present Law	President's Proposal	House Bill	Senate Amendment
	cause the benefits bear a uniform relationship to compensation	ployees In the case of educational assistance benefits, only amounts expended for degree programs would be required to be tested under this nondiscrimination rule.		
g. Concentration tests for plans other than health plans	(g) Under present law, not more than 25 percent of the benefits under a group legal services plan or a dependent care assistance plan may be provided during a year to 5-percent shareholders or owners (or their spouses or dependents). No more than 25 percent of the nontaxable benefits under a cafeteria plan can be provided annually to key employees No more than 5 percent of the amounts paid or incurred under an educational assistance program may be provided annually for 5-percent shareholders or owners (or their spouses or dependents).	(g) The proposal would modify the utilization test of present law applicable to group legal services, employee educational assistance, and dependent care assistance. Under the modification, the contributions provided to the top 20 highly compensated employees (by pay) could not exceed 25 percent of the total contributions provided under the plan for any year. This rule would apply to each employee benefit otherwise excludable from income.	(g) Retains present law	(g) Retains present law concentration tests In addition, provides that no more than 25 percent of the benefits under a group-term life insurance plan may be provided to 5-percent owners This rule would not apply if the plan provides equal coverage (in a dollar amount rather than as a percentage of pay) to each plan participant In addition, provides that no more than 40 percent of the employees benefiting under a group-term life insurance plan may be highly compensated employees. A plan is not treated as failing to meet this requirement if it benefits all employees of the employer
h. Sanctions for discrimination	(h) Under present law, if a plan fails to meet the applicable nondiscrimination requirements, all employees are required to include the value of the benefits provided in gross income. A special rule applies in the case of a discriminatory self-insured medical reimbursement plan under which only the highly compensated employees are required to include in income the portion of their reimbursements that are discriminatory In the case of group-term life insurance, only key employees are required to include the value of the benefit in income under a discriminatory plan.	(h) Under the proposal, if a plan is found to be discriminatory in coverage, benefits, or utilization, the benefits provided to highly compensated employees would not be eligible for exclusion from gross income. The amount to be included in gross income in the case of insurance-type benefits would be the value of the coverage provided to a highly compensated employee and not reimbursements received under the plan for expenses.	(h) A highly compensated employee who is a participant in a discriminatory statutory fringe benefit plan is required to include in income an amount equal to the discriminatory portion of the employee's employer-provided benefit under the plan. No benefits are includible in income for nonhighly compensated employees	(h) A highly compensated employee who is a participant in a discriminatory employee benefit plan is required to include in income an amount equal to the employee's employer-provided benefit under the plan No benefits are includible in income for nonhighly compensated employees
i. Reporting requirements	(i) Under present law, an annual reporting requirement applies with respect to group legal services plans, educational assistance plans, and cafeteria plans. Under this requirement, each employer that maintains a plan is required to file a return showing the number of employees participating in the plan, the total cost of the plan for the taxable year, and specified employer identification information	(i) Retains present law	(i) Extends present-law reporting requirements to all employee benefit plans In addition, the bill imposes a reporting requirement for any employee benefit plan in any year in which benefits are includible in the income of a highly compensated or key employee. The provision is effective for years beginning after December 31, 1986.	(i) Retains present law reporting requirements
j. Study		(j) No provision.	(j) Requires that the Treasury Department conduct a study of abuses of the health insurance provisions and make recommendations for changes in the nondiscrimination rules No later than July 1, 1986, Treasury is required to report the result of the study, together with any recommendations it deems advisable, to the Committee on Ways and Means, the Com-	(j) No provision

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			mittee on Finance, and the Joint Committee on Taxation.	
k. Effective dates		(k) The proposal relating to uniform nondiscrimination rules generally would be effective for plan years beginning after December 31, 1985, except that, in the case of a health plan, the proposal would be effective for plan years beginning after December 31, 1986. The proposal would provide a delayed effective date for collectively bargained plans	(k) The provisions are effective for years beginning after December 31, 1986	(k) Same as House bill, except that the nondiscrimination rules for an insured health plan do not apply to a church plan until years beginning after December 31, 1988.
3. Benefits provided under a cafeteria plan (sec. 1162 of the House bill)	Under a cafeteria plan, an employee is offered a choice between cash and one or more employee benefits. If certain requirements are met, then the mere availability of cash or certain permitted taxable benefits under a cafeteria plan does not cause an employee to be treated as having received the available cash or taxable benefits for income tax purposes. A highly compensated employee is treated as having received available cash and taxable benefits if the cafeteria plan discriminates in favor of highly compensated individuals as to eligibility or as to benefits and contributions In addition, if more than 25 percent of the total excludable benefits for a plan year are provided to employees who are key employees (certain officers and owners), then the key employees will be taxed as though they received all available taxable benefits under the plan. In addition, each benefit provided under a cafeteria plan must separately satisfy any nondiscrimination rule applicable to that benefit.	The proposal would apply a special rule to reimbursements of medical, legal, or dependent care expenses under a reimbursement account, under which the reimbursements would be deemed to be nondiscriminatory if the average reimbursements for highly compensated employees does not exceed 125 percent of the average reimbursements for all other participants in the cafeteria plan. In addition, the contributions provided to the top 20 highly compensated employees could not exceed 25 percent of the total contributions under the plan for any year. Under the proposal, reimbursements of insurance premiums would not be permitted from a reimbursement account. *Effective date*.—The proposal would be effective for plan years beginning after December 31, 1985.	Extends to cafeteria plans, for years beginning after December 31, 1986, nondiscrimination rules similar to those applicable to statutory employee benefit plans. Also modifies the rule governing the year in which benefits under a discriminatory cafeteria plan must be included in income by highly compensated and key employees Clarifies that full-time life insurance salesmen may elect benefits under a cafeteria plan that they are otherwise permitted to exclude from income. *Effective date*.—Effective for taxable years beginning after December 31, 1986	Retains present law, but (1) modifies the definition of highly compensated employees and excludible employees to conform to the new uniform definition, and (2) provides the average income exclusion test as an alternative test to the present-law benefits test
4. Faculty housing (sec. 1263 of the Senate amendment)	Several court cases have held that on-campus housing furnished to faculty or other employees by an educational institution does not quality for the exclusion under Code section 119 (certain lodging furnished for the convenience of the employer), and that therefore the rental value of the housing (less any amounts paid by the employee) is includible in income and wages The Deficit Reduction Act of 1984 prohibited Treasury from issuing, prior to 1986, regulations treating as income the excess of the value of qualified campus lodging over the greater of—	No provision.	No provision.	The rental value of qualified campus lodging for a year is treated as no greater than five percent of the appraised value for the year of the lodging, provided that an independent appraisal is obtained by a qualified appraiser. Thus, the value of the lodging is excluded from the employees' income and wages if the rent paid by him or her to the educational institution equals or exceeds (on an annualized basis) five percent of the appraised value Also, rents charged by an educational institution to nonemployees for comparable lodging may be used to define fair rental value.

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	(1) the operating cost paid in furnishing the lodging, or (2) the rent received, in the case of such lodging furnished in 1984 or 1985.			*Effective date.*—Taxable years beginning after 1985. For prior years, the IRS would follow the valuation rule, except that the assessed valuation of the property for local real estate tax purposes would be treated as meeting the requirement of a qualified appraisal
5. Deductibility of health insurance costs of self employed (sec. 1261 of the Senate amendment)	Under present law, a self-employed individual is not permitted to deduct (or exclude) the cost of health benefits, group-term life insurance, or cafeteria plan benefits for the self-employed individual	No provision.	No provision.	A self-employed individual is permitted to deduct (for income tax purposes) 50 percent of the amounts paid for health insurance (but not in excess of net earnings from self-employment), unless the health insurance is available through other employment of the self-employed individual or such individual's spouse. The deduction is not allowable unless provided through a nondiscriminatory health plan applicable to all unincorporated trades or businesses in which the self-employed individual is a 5-percent owner *Effective date.*—Taxable years beginning after December 31, 1986.
6. Health benefits for retirees (sec. 1263 of the Senate amendment)	Under present law, an employer generally is entitled to deduct contributions (within limits) to a welfare benefit fund to provide post-retirement medical benefits for employees The limits allow amounts reasonably necessary to accumulate reserves under a welfare benefit plan so that funding of post-retirement medical benefits or post-retirement life insurance benefits (including death benefits) with respect to an employee can be completed upon the employee's retirement However, these amounts may be accumulated no more rapidly than on a level basis over the working life of an employee with the employer of that employee. Each year's computation of contributions with respect to retiree medical benefits is to be made under the assumption that the medical benefits provided to future retirees will have the same cost as medical benefits currently provided to retirees. Because the reserve is to be computed on the basis of current medical costs, future inflation is not taken into account.	No provision.	No provision.	(a) An employer is permitted to take into account projected increases in medical costs in calculating the amount deductible for contributions to a welfare benefit fund for post-retirement medical benefits The amount taken into account is limited by reference to projected increases in medical costs under a specified index (b) Extends the due date of the study (mandated in DEFRA) relating to minimum standards for welfare benefit plans and a review of the funding levels of such plans to 1 year from the date of enactment of the bill. *Effective date.*—Taxable years beginning after December 31, 1986

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7. **Accrued vacation pay (sec. 907 of the House bill and sec. 325 of the Senate amendment)**	Under present law, an accrual method taxpayer generally is permitted a deduction no earlier than the taxable year in which the all-events test is met and economic performance occurs. In the case of the deferred benefits for employees (such as vacation pay earned in the current taxable year, but paid more than 2½ months after the close of the current year), an employer generally is entitled to claim a deduction only when the benefit is includible in an employee's gross income. Under a special rule of present law, an employer may make an election under section 463 to deduct an amount representing a reasonable addition to a reserve account for vacation pay (contingent or vested) earned by employees in the current year and expected to be paid by the close of that year or within 12 months thereafter.	No provision.	Revises the special provision under present law relating to accrued vaction pay to limit the deduction for accrued vacation pay to amounts expected to be paid during the current year or within 8½ months thereafter *Effective date*.—Taxable years of the employer beginning after December 31, 1985.	Same as House bill *Effective date*.—Taxable years beginning after December 31, 1986.

G. Employee Stock Ownership Plans (ESOPs) 1. ESOPs as employee benefit plants (secs. 1171 and 1173-1176 of the House bill and secs. 1271, 1272, 1275, and 1276 of the Senate amendment) *a. Status as retirement plans*	(a) An Employee Stock Ownership Plan (ESOP) (either a stock bonus plan or a combination stock bonus and money purchase pension plan) must be invested primarily in employer securities ESOPs are subject to special qualification requirements in addition to the requirements generally applicable to qualified plans.	(a) Under the proposal, any employer with 15 or more employees would be eligible to create a qualified Employee Stock Ownership Trust (ESOT). If the ESOT qualifies, then (1) the trust would be exempt from income tax, (2) employers would be allowed deductons (of up to 25 percent of compensation) for principal payments made on a securities acquisition loan, or for amounts contributed to an ESOT; even though participants would not be currently taxed on such contributions, and (3) participants would not be taxed until the employer securities were sold or exchanged. Parallel rules would be provided for certain nonleveraged ESOTs to which the employer had committed a stream of contributions. All eligible securities acquisition loans would require either (a) annual principal payments not greater than 20 percent or less than 8.3 percent of the original principal balance, or (b) equal annual payments and a term of ten years of less. The ESOT trust agreement would be required to provide that (1) the securities distributed or allocated during the year, and (2) dividends on undistributed and unallocated securities, be apportioned among all employees (or, those empolyees with 1000 hours of service) on the basis of each employee's compensation for the year not in excess of $50,000.	(a) No provision	(a) Adds to the Code a statement of Congressional policy, describing the belief of Congress (reflected in a series of applicable laws) that ESOPs should be used in a wide variety of corporate financing transactions in order to encourage the participation of employees as beneficiaries of such transactions. The statement expresses Congressional concern that this policy will be made unattainable by regulations and rulings that— (1) characterize ESOPs as conventional retirement plans, (2) reduce the freedom of ESOPs and employers to take the necessary steps to use ESOPs in a wide variety of corporate financing transactions, and (3) impede the establishment and success of these plans.
b. Vesting	(b) Under present law, ESOPs are subject to the vesting rules generally applicable to qualified plans	(b) The proposal would require full vesting upon either the allocation of employer securities to a participant's account or upon distribution of such securities.	(b) Any ESOP that is not top heavy is required to provide that a participant's right to his account balance derived from employer contributions must become nonforfeitable no more slowly than the following 10-year graded vesting schedule. 20 percent vesting after completion of 6 years of service, and an additional 20-percent vesting for each additional year of service until 100 percent vesting is attained after 10 years of service.	(b) See Item B 9, above, describing the provisions in the Senate amendment that require all single-employer qualified plans, including ESOPs, to satisfy one of two alternative vesting schedules Under the first schedule, a participant must be 100-percent vested upon completion of 5 years of service. Under the second schedule, a participant must vest no more slowly than under the following 7-year graded vesting schedule 20 percent after 3 years of service, and an additional 20 percent for each year of service until 100 percent vesting is attained after 7 years of service

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c. Nondiscrimination	(c)(1) *In general.*—ESOPs are subject to the nondiscrimination rules applicable to qualified plans. These standards prohibit discrimination as to eligibility, contributions or benefits, in favor of employees who are officers, shareholders, or highly compensated employees.	(c)(1) *In general.*—No provision.	(c)(1) *In general.*—Requires that no more than one-third of the employer's contributions for a year be allocated to the group of employees consisting of officers, 10-percent shareholders, or highly compensated individuals. Individuals are considered highly compensated if they have compensation in excess of 200 percent of the dollar limits on annual additions to a defined contribution plan (i.e., for 1985, 200 percent of $30,000 equals $60,000).	(c)(1) *In general.*—Retains present law, but ESOPs generally are subject to the changes made by the amendment to qualified plans.
	(2) *Compensation taken into account.*—For any year for which a qualified plan is a top-heavy plan, present law provides that only the first $200,000 of compensation may be taken into account under the plan for purposes of applying the nondiscrimination tests.	(2) *Compensation taken into account.*—The ESOT trust agreement would be required to provide that (1) the securities distributed or allocated during the year, and (2) dividends on undistributed and unallocated securities, be apportioned among all employees (of those employees with 1,000 hours of service) on the basis of each employee's annual compensation not in excess of $50,000.	(2) *Compensation taken into account.*—Reduces the limit on includible compensation from $200,000 to an amount equal to 7 times the defined contribution plan dollar limit ($175,000 for 1986) and applies the limit to all plans, including ESOPs, whether or not top heavy.	(2) *Compensation taken into account.*—Extends the $200,000 limit on includible compensation to all plans, including ESOPs, whether or not top heavy
d. Diversification	(d) No provision.	(d) No provision.	(d) Requires that a "qualified employee" be entitled annually during the participant's "qualified election period" to direct diversification of up to 25 percent of the participant's account balance (50 percent after attainment of age 60). Any employee who has attained at least age 55 and completed 10 years of participation is a qualified employee. An employee's qualified election period commences with the year following the year in which the employee attains age 55 and completes 10 years of participation. The period ends in the year following the year in which the participant attains age 60. The ESOP is required to offer at least 3 investment options, to provide an annual 90-day diversification election period, and to complete the diversification within a specified period	(d) Retains present law
e. Voting rights	(e) A stock bonus or money purchase pension plan (including an ESOP) maintained by an employer whose securities are not publicly traded must provide the full pass-through of voting rights to participants with respect to securities allocated to such participants on major corporate issues if the plan holds more than ten percent of its assets in employer securities. In addition, an ESOP maintained by an employer that has registration-type securities must provide pass-through voting with respect to allocated securities on any issue.	(e) Under the proposal, the new ESOT would be required to provide pass-through voting (1) on all issues with respect to allocated securities and (2) on major corporate issues with respect to unallocated securities.	(e) Requires that if an employer does not have registration-type securities, then (1) participants with more than 10 years of service have the right to direct the trustee to vote allocated securities on all issues, (2) participants with fewer than 10 years of service have the right to direct the trustee to vote allocated securities with respect to any corporate matter that must be decided by more than a majority vote. As under present law, no pass-through of voting rights is required with respect to unallocated securities. Retains present-law requirements applicable to employers with registration-type securities	(e) Eliminates the pass-through voting requirements of present law in the case of employer securities issued by certain small newspapers whose stock is not readily traded. (Floor amendment by Senators Stevens and Dixon, adopted by voice vote.)

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f. Overall limits on contributions	(f) The usual dollar limit on annual additions ($30,000) is increased to the lesser of (1) $60,000 or (2) the amount of employer securities contributed to, or acquired by, the plan In addition, deductible ESOP contributions applied by the plan to the payment of interest on a securities acquisition loan, as well as forfeitures of certain employer securities, may be disregarded in applying this limit. These increased limits apply only if the ESOP provides that no more than one-third of the employer contributions for the year are allocated to the group of employees consisting of officers, shareholders and highly compensated employees	(f) The proposal would equal the increased ESOP limits applicable under qualified plans Allocations of employer securities under an ESOT would be permitted without regard to the qualified plan limits on annual additions.	(f) Retains present law (See c , above, which applies the ⅓ allocation restriction to all ESOPs.)	(f) Modifies the definition of an employee who is subject to the one-third allocation limit for purposes of the special limitation on annual additions to ESOPs The definition is modified to conform to the new definition of highly compensated employee added to the Code for purposes of qualified pension, profit-sharing, and stock bonus plans, and for purposes of employee benefit plans. (See item B 5 , above.)
g. ESOP tax credits	(g) An electing employer is allowed an income tax credit for contributions to a payroll-based tax credit ESOP. The credit is limited to one-half of one percent of compensation paid or accrued in 1985, 1986, or 1987. No credit would be allowed after 1987.	(g) The proposal would allow the payroll-based tax credit to expire after 1987, as scheduled under present law.	(g) Repeals the payroll-based tax credit, effective for compensation paid or accrued after December 31, 1985.	(g) Repeals the payroll-based tax credit, effective for compensation paid or accrued after December 31, 1986

		President's Proposal	House Bill	Senate Amendment
h. Distribution restrictions	(h)(1) *Put options.*—A participant in an ESOP generally must have the right to demand distribution of employer securities rather than cash and, if the securities are not readily tradeable, the employer must provide a put option Each distributee, upon separation from service, must be given at least 60 days after receipt of the employer securities to require the employer to repurchase the securities at their fair market value. If the distributee does not exercise the initial option, the option will temporarily lapse. After the close of the taxable year in which the option lapses, the distributee must be given another 60 days to put the securities to the employer.	(h)(1) *Put options.*—The proposal would repeal the special put option rules relating to qualified plans	(h)(1) *Put options.*— *In general.*—Retains the put option requirement of present law (modified in manner described below).	(h)(1) *Put options.*— *In general.*—Retains the put option requirements of present law (modified in manner described below) and extends the put option requirements to distributions of non-readily traded securities from stock bonus plans
	Payment upon exercise of put option.—If employee "puts" securities to the employer, payment of the put option price may be deferred provided that the terms of the deferral are reasonable and the employer provides adequate security and a reasonable rate of interest. The terms of deferral are generally considered reasonable if they require periodic payments commencing within 30 days after the date that the put option is exercised and ending within 5 years of the date of exercise of the option. However, the deferral period may be extended to a date no later than the earlier of (1) 10 years from the date that the put option is exercised or (2) the date that the securities acquisition loan with which the securities were acquired is repaid.		*Payment upon exercise of option.*—Requires that in the case of a lump sum distribution of employer securities, if employee "puts" securities to employer, put option price be paid in substantially equal installments over a period not exceeding 5 years and beginning not more than 30 days after the close of the 60 day option period The employer must provide security for the installment payments and reasonable interest. In the case of a put option exercised with respect to distribution of employer securities other than a lump sum, requires that the employer pay option price 90 days after exercise of option.	*Payment upon exercise of option.*—Same as House bill, except that (a) the 5-year period during which the employer must purchase a lump-sum distribution of securities with respect to which a participant has exercised a put option begins 30 days after the date of exercise of the put option; (b) the employer need not provide security with respect to the put option installment payments, and (c) in the case of a put option exercised with respect to a distribution other than a lump sum, the employer must pay the full option price to the participant within 30 days after the close of the 60-day option period.
	(2) *Distribution restrictions.*—Distributions from an ESOP generally must satisfy the distribution rules applicable to stock bonus or money purchase plans. Under these rules, an ESOP is not required to make distributions to a participant, until the participant has attained normal retirement age In addition, employer securities allocated to a participant's account under a tax-credit ESOP generally may not be distributed before the end of 84 months	(2) *Distribution restrictions.*—The new ESOT generally would be required to distribute annually that portion of the securities held by the ESOT equal in value to the scheduled principal payments on the securities acquisition loan, as well as dividends paid on allocated and unallocated stock Alternatively, the ESOT could retain nominal ownership of the allocated securities provided the employees had all rights of direct ownership. In addition, the employer would be required to grant employees the right to put distributed or allocated securities within three years after receipt or allocation and for a specified period every year thereafter until the year following the employee's separation from service The 84-month rule would be repealed with respect to qualified plans.	(2) *Distribution restrictions.*—Requires that, unless an employee otherwise elects in writing, the payment of benefits from an ESOP must begin no later than 60 days after the end of the plan year in which occurs (1) the first anniversary of the date on which the participant separates from service, or (2) the repayment of the securities acquisition loan, if later. However, if the participant attains normal retirement age in an earlier year, benefits must commence no later than 60 days after the year in which the participant attains normal retirement age, absent a contrary election by the participant.	(2) *Distribution restrictions.*—Requires that, unless an employee otherwise elects in writing, the payment of benefits from an ESOP must begin no later than one year after the later of the plan year (a) in which the participant terminates employment due to retirement, disability, or death, (b) which is the fifth plan year following the year in which the participant separates from service, or (c) which is the first anniversary of the date on which the securities acquisition loan was repaid However, if the participant attains normal retirement age in an earlier year, benefits must commence no later than 60 days after the year in which the participant attains normal retirement age, absent a contrary election by the participant. The Senate amendment also accelerates the period over which the distribution of an employee's benefit must be made

h. Distribution restrictions (cont.)	(3) *Distributions upon termination.*—Distributions may not be made from a tax credit ESOP upon the termination of the ESOP except in the case of employer securities that have satisfied the 84 month requirement	(3) *Distributions upon termination.*—Distributions would be permitted on the termination of an ESOT.	(3) *Distribution upon termination.*—Amends the tax credit ESOP provisions to permit certain distributions upon plan termination. Thus, the 84-month rule generally will not apply with respect to distributions made on account of the termination of the tax credit ESOP	(3) *Distributions upon termination.*—Same as House bill
i. Effective dates		(i) *Effective dates.*—The proposal would generally apply to securities acquisition loans made after December 31, 1985. The treatment of additional contributions made pursuant to loans outstanding on December 31, 1985, would continue to be governed by existing law	(i) *Effective dates.*—The repeal of the payroll-based tax credit generally applies with respect to compensation paid or accrued after December 31, 1985 The provision permitting the distribution of assets upon the termination of an ESOP is effective for termination distributions made after December 31, 1984 The remaining provisions apply to ESOP adopted after December 31, 1985. In addition, for ESOPs in existence prior to January 1, 1986, the requirements apply to amounts contributed after December 31, 1985, for securities purchased with those amounts.	(i) *Effective dates.*—The repeal of the payroll-based tax credit generally applies with respect to compensation paid or accrued after December 31, 1986. The provision permitting distributions upon plan termination generally is effective for termination distributions made after December 31, 1984 The distribution requirements and the extension of the put option requirement to stock bonus plans are effective with respect to distributions attributable to stock acquired after December 31, 1986 The put option requirements are effective for distributions attributable to stock acquired after the date of enactment. The modified definition of highly compensated employees is effective for years beginning after December 31, 1988.
2. Incentives for ESOP financing (sec. 1172 of the House bill and secs. 1273 and 1274 of the Senate amendment) *a. Deduction for dividends paid*	(a) An employer may deduct the amount of any dividends paid in cash with respect to employer-securities held by an ESOP and allocated to participants' accounts, provided the dividends are paid out currently to participants and beneficiaries	(a) The proposal would modify the provision providing a deduction for dividends paid (1) by permitting the deduction only with respect to employer securities held by the new Employee Stock Ownership Trust (ESOT) (and not an ESOP); (2) by making the deduction available with respect to dividends paid on all allocated and unallocated employer securities held by the ESOT; and (3) by conditioning the deduction on the employer's making and additional nondeductible payment (equal to the resulting tax savings) to employees receiving the dividends	(a) Repeals the present law provision effective for dividends paid after December 31, 1988.	(a) Expands the deduction for dividends paid on ESOP stock to apply to dividends used to repay ESOP loans that were used to acquire the securities on which the dividends are paid The provision is effective for taxable years beginning after the date of enactment

b. Exclusion of interest earned on securities acquisition loans	(b) A bank, insurance company, or a corporation actively engaged in the business of lending money may exclude from gross income 50 percent of the interest received on loans to a leveraged ESOP, the proceeds of which are applied by the plan to acquire employer securities.	(b) The proposal would apply the 50-percent interest exclusion to transactions involving ESOTs rather than ESOPs, effective for loans made after December 31, 1985	(b) Repeals the present law provision for loans made after December 31, 1988	(b) Modifies the 50-percent exclusion in two respects First, expands the definition of a lender eligible for the exclusion to include a regulated investment company Second, makes exclusion available with respect to a loan (with an original commitment period of 7 or fewer years) to the employer, to the extent that, within 30 days, employer securities are transferred to the plan in an amount equal to the proceeds of the loan, and such contributions are allocated to participants' accounts The provision is effective for loans used to acquire employer securities after the date of enactment.
c. Tax-deferred rollover of gain derived from sales of stock to an eligible employee organization	(c) An individual may elect to defer recognition of gain on the sale of certain qualified securities to an ESOP or eligible worker-owned cooperative to the extent that the proceeds are reinvested in qualified replacement property within a replacement period	(c) The proposal would permit an individual to elect to defer recognition with respect to qualifying sales made to an ESOT rather than an ESOP or eligible worker-owned cooperative, effective for sales occurring after December 31, 1985.	(c) Repeals the present law provision for loans made after December 31, 1988.	(c) Retains present law.
d. Payment of estate tax by an employee organization	(d) If qualified employer securities are (1) acquired from a decedent by an ESOP or an eligible worker-owned cooperative, (2) pass from a decedent to an ESOP or worker-owned cooperative, or (3) are transferred by the decedent's executor to an ESOP or worker-owned cooperative, then the executor is relieved of estate tax liability to the extent the ESOP or cooperative is required to pay the liability	(d) The proposal would repeal this provision, effective for decedents dying after December 31, 1985.	(d) Repeals the present law provision for loans made after December 31, 1988.	(d) Retains present law
e. Estate tax exclusion for sales to ESOPs	(e) No provision.	(e) No provision.	(e) No provision.	(e) The bill permits an exclusion from the gross estate of 50 percent of the qualified proceeds from the sale of employer securities by the executor of the estate to an ESOP, before the due date (including extensions) of the estate's tax return The provision is effective for sales after the date of enactment by the executor of an estate required to file a return after that date

A. Foreign Tax Credit (secs. 601-604 of the House bill and secs. 901-905 of the Senate amendment)				
1. Separate foreign tax credit limitations				
a. Overall limitation	(a) The foreign tax credit is determined on an "overall" basis: a taxpayer adds up its net income and net losses from all sources outside the United States and calculates one aggregate limitation based on the total. The credit is limited to the pre-credit U.S. tax multiplied by a fraction, the ratio of foreign source income to worldwide income	(a) Determine the foreign tax credit limitation on a per country basis instead of on an overall basis. That is, a taxpayer could credit taxes paid on income derived from a particular country only up to the amount of U.S. tax that would be owed on *that* income.	(a) Does not adopt the per country limitation	(a) Does not adopt the per country limitation
b. Separate limitations for different types of income	(b) Overall foreign tax credit limitations are calculated separately for certain categories of income that frequently bear either high (e g , oil extraction income) or low (e.g., FSC dividends) rates of foreign tax or that can easily be earned in low-tax countries rather than in the United States in order to inflate the foreign tax credit limitation. The reason for the separate limitations is to prevent distortion of the foreign tax credit.	(b) Generally retain the present law separate limitations, but apply them on a country-by-country basis if the per country limitation is adopted.	(b)(1) Establishes a separate limitation for banking and insurance income.	(b)(1) No provision.
			(2) Establishes a separate limitation for shipping income, that is, income of a kind which would be foreign base company shipping income as that category of subpart F income is expanded by the House bill (see C.1.a. below).	(2) No provision
			(3) Establishes a separate limitation for foreign currency translation gains.	(3) No provision.
		The application of the separate limitation for passive interest income would be extended to certain other types of income.	(4) Replaces the separate limitation for passive interest income with a separate limitation for passive income generally	(4) Replaces the separate limitation for passive interest income with a separate limitation for passive income generally.
			(i) Passive income, for this purpose, generally is any income of a kind which would be subpart F foreign personal holding company (FPHC) income as that category of income is expanded by the House bill (see C.1.a below) except that foreign currency transaction gains of dollar taxpayers are passive income without regard to the business needs exception generally provided in the new subpart F rules for currency gains	(i) Passive income, for this purpose, generally is any income of a kind which would be subpart F foreign personal holding company (FPHC) income as that category of income is expanded by the Senate amendment (see C.1.a. below).
			(ii) Foreign personal holding company inclusions (under sec. 553) and passive foreign investment company inclusions (discussed in item D 8., below) are also passive income.	(ii) Same as House bill

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b. Separate limitations for different types of income (Cont.)			(iii) The separate limitation for passive income does not apply to: (A) banking and insurance income (which is subject to its own separate limitation (see (b)(1), above)); (B) shipping income (which is subject to its own separate limitation (see (b)(2), above)); (C) foreign oil and gas extraction income; or (D) active business rents and royalties from unrelated parties.	(iii) The separate limitation for passive income does not apply to: (A) same as House bill, except that passive banking and insurance income is subject to the separate limitation; (B) same as House bill, with no separate limitation for shipping income; (C) same as House bill; (D) same as House bill; (E) high withholding tax interest (which is subject to its own separate limitation (see A.2. below)); (F) interest on working capital (as under current law); or (G) dividends on working capital received from a regulated investment company.
			(iv) High-taxed income is excluded from the separate limitation for passive income.	(iv) Treasury may prescribe anti-abuse rules to prevent manipulation of the character of income the effect of which is to avoid the purposes of the separate limitations.
		Dividends generally would be subject to the various separate limitations in proportion to the types of income out of which the dividends were paid.	(5) In applying the new separate limitations, certain payments from, and inclusions with respect to, related persons are subject to look-through rules that take into account the income of the payor.	(5) Same as House bill, except that the look-through rule for payments by related persons with passive income treats payments as first attributable to the payor's passive income.

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c. Foreign tax credit carry forwards and carrybacks	(c) Foreign taxes in excess of the foreign tax credit limitation may be carried back two years and then carried forward five years.	(c) If the per country limitation is adopted, extend the foreign tax credit carryover period from 5 to 10 years for post-effective date excess credits.	(c) Retains present law	(c) Same as House bill (retains present law).
		Effective date.—Generally, taxable years beginning after 1985.	*Effective date.*—Taxable years beginning after 1985.	*Effective date.*—In general, taxable years beginning after 1986
		Transitional rule for shift from an overall to a per country limitation:	Transitional rule for new separate limitations	Transitional rule for new separate limitations (including that for high withholding tax interest discussed in item A.2. below):
		Carryforwards.—Pre-effective date excess credits can be carried forward under an overall limitation	*Carryforwards.*—Carryforwards from a pre-effective date year to a post-effective date year can offset U.S. tax on only the same kind of income, determined under the House bill's new rules, as the income on which the foreign taxes were actually paid. For example, pre-effective date foreign taxes on portfolio dividend income that are carried to a post-effective date year can offset the U.S. tax on only passive income in that later year	*Carryforwards.*—Pre-effective date excess credits can be carried forward to post-effective date years only to reduce U.S. tax on income of the old-law limitation category they had been in. For example, pre-effective date foreign taxes on portfolio dividend income that are carried to a post-effective date year can offset U.S. tax on only overall limitation in that later year.
		Carrybacks.—Post-effective date excess credits cannot be carried back to pre-effective date years.	*Carrybacks.*—Carrybacks from a post-effective date year to a pre-effective date year can offset U.S. tax on only the same kind of income, determined under the House bill's new rules, as the income on which the foreign taxes were actually paid	*Carrybacks.*—Post-effective date excess credits can be used in pre-effective date years to reduce the U.S tax on overall limitation income only Post-effective date credits that are excess credits solely because of the Senate amendment's rate reductions cannot be carried back to higher-rate years An additional, targeted transitional rule is provided in the case of the separate limitation for passive income.

Item	Present Law	President's Proposal	House Bill	Senate Amendment
2. Credit for high withholding taxes on interest	The foreign tax credit is available for income, war profits, and excess profits taxes paid to a foreign country or a U.S possession. In certain cases, a tax other than an income tax is creditable if it serves as a substitute for an income tax. Under the overall limitation, U.S. lenders can use foreign tax credits for high gross withholding taxes on a loan—the economic burden of which may be borne primarily by the borrower—to reduce the lenders' U.S. tax liability on other loan proceeds and other income.	No provision.	(a) A foreign tax credit is allowed for gross-basis taxes on interest paid to a bank, insurance company or other financial institution (or any related person) only to the extent of the U.S tax on the associated interest income. *Effective date.*— (i) In general, the provision applies to taxable years beginning after 1985. (ii) The provision does not apply until 1989 in the case of foreign taxes imposed on interest paid on pre-November 17, 1985 loans and restructurings thereof (adjusted upward by 3 percent per year) to borrowers in 15 less developed countries.	(a) Creates a separate foreign tax credit limitation for foreign interest earned by a bank or other financial institution or an insurance company (or a related person) in the case of interest that is subject to a foreign gross-basis tax of 5 percent or more (b) Provides exceptions for: (i) interest earned by a related person if the interest is directly related to that person's active business, and (ii) interest earned by a finance company in connection with export financing of products manufactured in the United States by a related person. (c) In applying the new separate limitation, certain payments from, and inclusions with respect to, related persons are subject to look-through rules that take into account the income of the payor *Effective date.*— (i) In general, the provision applies to taxable years beginning after 1986 (ii) The provision does not apply (without time limit) in the case of foreign taxes imposed on interest received or accrued on pre-November 17, 1985 loans to borrowers in 15 less developed countries. In general, the amount of a lender's foreign tax credits protected by this exemption is increased by 3 percent annually through 1990, and the less developed country loans can be restructured until that date without any loss of the exemption (iii) The provision also does not apply to interest received or accrued in taxable years before 1997 on other loans held by the taxpayer on November 16, 1985.

3. Deemed-paid credit	A U.S. corporation that owns at least 10 percent of a foreign corporation's voting stock and that has dividend income from the foreign corporation may generally take a "deemed-paid" credit for a share of the foreign taxes that the foreign corporation paid on the earnings out of which the dividend is paid A similar credit applies when a 10-percent U.S. corporate shareholder includes in income a portion of a controlled foreign corporation's undistributed earnings under subpart F A dividend or subpart F inclusion is considered paid first from earnings and profits of the current year and then from accumulated profits of each preceding year Actual distributions made in the first 60 days of a taxable year are treated as made from the prior year's earnings and profits Earnings and profits may be computed in a different manner for actual dividend distributions than for subpart F inclusions.	A U.S. corporation's share of foreign taxes paid by a foreign corporation would depend on the percentage of the foreign corporation's multi-year pool of accumulated earnings and profits represented by the dividend, including current year earnings and profits The 60-day rule would be repealed Earnings and profits would be computed in the same manner for actual distributions and for subpart F inclusions, generally following the subpart F rules However, the rules for translating foreign currency would be modified *Effective date.*—Taxable years beginning after 1985. Future dividends would be treated as paid first out of accumulated profits of the payor derived after the effective date. Dividends in excess of that amount would be treated as paid out of pre-effective date accumulated profits under present-law ordering rules.	Same as President's proposal *Effective date*—Same as President's proposal	Same as President's proposal and House bill, except draws taxes and earnings and profits from a moving 10-year pool. *Effective date.*—Same as President's proposal and House bill, but effective for taxable years beginning after 1986 rather than 1985.
4. Effect of foreign and U.S. losses on foreign tax credit	(a) Under the overall foreign tax credit limitation, a taxpayer first uses a net loss incurred in any foreign country to reduce its income from other foreign countries. If a taxpayer's net foreign losses subject to one separate limitation exceed its foreign income subject to that limitation, the excess arguably reduces the taxpayer's U.S source taxable income (b) An overall U.S loss first reduces foreign income earned in the loss year and hence pre-credit U.S. tax in that year	(a) If the per country limitation is adopted, a net loss incurred in any foreign country would reduce taxable income earned in all other countries, including the United States, in proportion to the shares of worldwide taxable income earned in each of those other countries. (b) An overall U.S loss would continue to reduce foreign income. If the per country limitation is adopted, the U.S. loss would be prorated against income earned by the taxpayer in different foreign countries in proportion to the shares of worldwide taxable income earned in each of the countries In addition, if a per country limitation is adopted, the proposal would add an overall U.S loss recapture rule Under this rule, a portion of U.S income earned after an overall U.S. loss year would be treated as foreign income. *Effective date.*—Generally, taxable years beginning after 1985. Pre-effective date overall foreign losses would be recaptured from post-effective date income under the pre-effective date foreign loss recapture rules	(a) Provides that foreign losses first reduce income in the other foreign income baskets before they reduce U.S income Provides a recapture rule. (b) Retains present law *Effective date.*—The changes are effective with respect to losses incurred in taxable years beginning after 1985.	(a) Same as House bill (b) Generally, same as House bill, but provides that U.S losses reduce categories of foreign income pro rata *Effective date*—The changes are effective with respect to losses incurred in taxable years beginning after 1986

5. Subsidies	Under a Treasury regulation, a tax is not creditable if it is used directly or indirectly as a subsidy to the taxpayer or certain related persons	No provision	Codifies the Treasury regulation that denies a foreign tax credit for taxes used as a subsidy to the taxpayer or certain related persons. *Effective date*.—Applicable to foreign taxes paid or accrued in taxable years beginning after 1985.	Generally, codifies the regulation to treat direct or indirect subsidies, including a subsidy to a party to a related transaction, as a reduction of creditable taxes *Effective date*.—Applicable to foreign taxes paid or accrued in taxable years beginning after 1986
B. Source Rules				
1. Sales of personal property (sec. 611 of the House bill and sec. 911 of the Senate amendment)				
a. Income derived from purchase and sale of inventory property	(a) Generally sourced where title to the property passes The title passage rule allows taxpayers to obtain foreign sourcing for sales income by passing title to the property sold offshore regardless of where the economic activity generating the income took place.	(a) Eliminate the title passage rule. Generally source in the country of residence of the seller. If the seller has a fixed place of business outside the country of residence that participates materially in the sale, source where that fixed place of business is located. The fixed place of business exception would not apply in the case of sales to related foreign persons	(a) Generally follows the President's proposal. Anti-abuse rules are provided to prevent manipulation of the basic residence-of-the-seller source rule. The bill provides that, for purposes of the fixed place of business exception, no fixed place of business exists in a country with respect to income which that country is barred by treaty from taxing	(a) Retains present law for U.S. persons, but generally follows House bill for foreign persons by providing that income earned by a foreign person attributable to a fixed place of business within the United States is U.S. source (except for foreign tax credit purposes).
b. Income from manufacture and sale of inventory property	(b)(1) The sales portion of such income is sourced where the title to the property passes.	(b)(1) Eliminate the title passage rule for the sales portion of such income and source that portion of the income generally in the country of residence of the seller, with an exception for foreign material participation in unrelated party sales.	(b)(1) For the sales portion of such income, generally follows the President's proposal. Anti-abuse rules are provided to prevent manipulation of the basic residence-of-the-seller source rule. It is provided that no fixed place of business exists in a country with respect to income which that country is barred by treaty from taxing. Provides a special rule for foreign sales by U.S. companies to ensure foreign source for sales of foreign-produced property.	(b)(1) Retains present law for U.S. persons, but generally follows House bill for foreign persons by providing that income earned by a foreign person attributable to a fixed place of business within the United States is U.S source (except for foreign tax credit purposes).
	(b)(2) Generally, under Treasury regulations, half of the income is treated as manufacturing and sourced in the country of manufacture and half is treated as sales income and sourced in the country of sale. The division of such income between manufacturing and sales must be made on the basis of an independent factory price instead if one exists.	(b)(2) Source the manufacturing portion of such income as under present law Retain the 50/50 formula and independent factory price rules for allocating such income between manufacturing and sales activity	(b)(2) Requires that at least 50 percent of such income be allocated to manufacturing activity under regulations	(b)(2) Retains present law

c. Income from the sale of intangible property (other than inventory)	(c) Generally, income from sales of intangible property is sourced where the title to the property passes Some income from sales of intangible property for an amount contingent on the use of the property is sourced where the property is used	(c) Income from sales of intangibles would have its source at the place of use	(c) Sources income from sales of intangibles (except sales for amounts contingent on the use of the intangibles) generally in the country of residence of the seller Provides anti-abuse rules to prevent manipulation of the basic residence-of-the-seller source rule, and provides that no fixed place of business exists in a country with respect to income which that country is barred by treaty from taxing Sources income from sales of goodwill where the goodwill is developed	(c) Generally, same as House bill, except sales by U.S persons attributable to a fixed place of business maintained outside the United States yield foreign source income (if such income is subject to at least a 10-percent foreign tax).
d. Income derived from sale of other property (other than inventory)	(d) Generally sourced where the title to the property passes	(d)(1) Income derived from sales of personal property used by the seller in his business would be sourced where the property was used	(d)(1) Sources recapture income derived from sales of personal property used by the seller in his business where deductions with respect to such property previously offset income, to the extent of such deductions Sources any sales income exceeding previous deductions generally in the country of residence of the seller, provides anti-abuse rules to prevent manipulation of the basic residence-of-the-seller source rule, and provides that no fixed place of business exists in a country with respect to income which that country is barred by treaty from taxing	(d)(1) For recapture income, same as House bill. For gain in excess of recapture income and for other income from sales of personal property used by the seller in his business, present law is retained for U S persons, same as House bill for foreign persons
		(d)(2) Income derived from sales of other personal property, including passive investment property such as securities and commodity futures contracts, would be sourced in the country of residence of the seller	(d)(2) Same as President's proposal	(d)(2) Generally, same as House bill, except. (i) sales by U.S persons attributable to a fixed place of business maintained outside the United States yield foreign source income (if such income is subject to at least a 10-percent foreign tax); and (ii) gain (in excess of sec. 1248 recapture) from sales by U.S persons of stock in 80 percent-owned corporations are foreign source if the corporation derives a substantial amount of its business income in the country where the sale occurs
		Effective date—Generally, taxable years beginning after 1985. Transitional rules would be provided for sales made under unrelated party contracts entered into before 1986.	*Effective date*—Generally, taxable years beginning after 1985 Transitional rules are provided for sales during 1986 made under unrelated party contracts entered into before 1986	*Effective date* For U.S persons and controlled foreign corporations, taxable years beginning after 1986. For other foreign persons, transactions entered into after March 18, 1986

Item	Present Law	President's Proposal	House Bill	Senate Amendment
2. Transportation income (sec. 613 of the House bill and sec. 913 of the Senate amendment)				
a. Source of income	(a) Treasury regulations generally allocate transportation services income between U.S. and foreign sources in proportion to the expenses incurred in providing the services Expenses incurred outside the three-mile limit to the territorial waters of the United States are treated as foreign for this calculation Income and losses from transportation that begins and ends in the United States are sourced in the United States Income and losses from transportation that begins in the United States and ends in a U.S. possession (or vice versa) generally is treated as 50-percent U.S. source and 50-percent possessions source.	(a) Reassess the rule allocating transportation income to U.S and foreign sources in proportion to where expenses are incurred, possibly substitute for it a 50-percent rule similar to that for U.S-U.S. possessions transportation income	(a) Sources transportation income and loss attributable to U S -foreign and foreign-U S routes as 50-percent U.S and 50-percent foreign.	(a) Same as House bill, but the amendment excludes income from personal services performed as an employee from transportation income on U S -foreign and foreign-U S. routes (other than routes to and from U.S. possessions).
b. Special rules for vessels and aircraft	(b)(1) Under a special rule, income and expenses associated with the lease or disposition of a vessel or aircraft that is constructed in the United States and leased to U.S. persons are sourced in the United States, regardless of where the vessel or aircraft may be used	(b)(1) Repeal special rule.	(b)(1) Repeals special rule.	(b)(1) Same as President's proposal and House bill
	(2) A similar rule applies to transportation income and expenses associated with the lease of an aircraft (wherever constructed) to a regularly scheduled U S. air carrier, to the extent the aircraft is used on U.S - U S possessions routes	(2) Retain present law	(2) Repeals special rule.	(2) Same as House bill
c. Reciprocal exemption	(c) The United States does not tax foreign persons' earnings from the operation of ships and aircraft registered in foreign countries that grant equivalent exemptions to U.S. citizens and U.S corporations	(c) Retain present law	(c)(1) Modifies the exemption for foreign persons' shipping and aircraft income so that its availability turns on whether a foreign person's *residence* country gives U.S citizens and U.S corporations an equivalent foreign tax exemption, not on whether the country where the ship or aircraft is registered gives such an exemption. (2) Persons are not considered residents of countries that exempt U.S. carriers unless 75 percent or more of the ultimate owners are U.S. persons who are currently taxable on the income or residents of countries that exempt U.S. carriers from tax.	(c)(1) Same as House bill, but provides that rental income on a full or bareboat basis is eligible for the reciprocal exemption, and the Secretary can apply the reciprocal exemption separately to different types of transportation income (2) Persons are not considered residents of countries that exempt U.S. carriers unless 50 percent or more of the ultimate owners are U.S shareholders or residents of countries that exempt U.S. carriers from tax

d. Gross-basis withholding tax	(d) The United States (in contrast with a number of countries) does not impose a gross-basis tax on domestic source shipping income of foreign persons	(d) Retain present law	(d)(1) Imposes a four-percent gross-basis tax on U.S. source transportation income of foreign persons, unless prohibited by treaty or reciprocal exemption (with anti-conduit rules to prevent flag shopping)	(d)(1) Same as House bill, but limits its application only to residents of countries that impose gross tax on transportation income of U.S persons (with anti-conduit rules to prevent flag shopping). Residents of other countries are taxed as under present law and can elect to be taxed on a net basis for noneffectively connected income.
			(2) Collects the tax through a withholding requirement.	(2) Collects the tax through return filing.
			(3) Transportation income is effectively connected only in limited cases	(3) Retains present law's definition of effectively connected income.
			(e) Reciprocal exemptions do not apply in treaty shopping cases	(e) Same as House bill
		Effective date.—Generally, taxable years beginning after 1985. The repeal of the special U.S. sourcing rules for certain leasing income would not affect income attributable to an asset owned on January 1, 1986, if that asset was first leased before that date	*Effective date.*—Same as President's proposal.	*Effective date.*—Generally, taxable years beginning after 1986. The repeal of the special U.S. sourcing rules for certain leasing income does not affect income attributable to an asset owned on January 1, 1986, if that asset is leased before that date. Provides a targeted transitional rule.
3. Other offshore income and income earned in space (sec. 615 of the House bill and sec. 915 of the Senate amendment)	Generally, treated as foreign source income. Some taxpayers treat certain space-related income as U.S source income.	No provision.	Sources certain offshore income and income earned in space in the recipient's country of residence Treats U.S.-controlled foreign corporations as U.S. residents for purposes of this rule	Same as House bill, but sources income from the transmission of communications or data from the United States to any foreign country (or vice-versa) as 50 percent U.S source and 50 percent foreign source
			Effective date.—Taxable years beginning after 1985.	*Effective date.*—Taxable years beginning after 1986.

Item	Present Law	President's Proposal	House Bill	Senate Amendment
1. Dividend and interest income (sec. 612 of the House bill and sec. 912 of the Senate amendment)				
a. 80/20 entities	(a) Generally sourced in the residence country of the payor (in the case of a corporation, its country of incorporation). However, if a U.S. corporation earns more than 80 percent of its income from foreign sources (such a corporation is known as an "80/20 company)", dividends and interest paid by the corporation are treated as foreign source income.	(a) Repeal the exceptions to the general source rules for interest and dividends paid by 80/20 companies (i.e., treat as U.S. source).	(a)(1) Generally follows President's proposal. An exception is provided for interest paid by an 80/20 company engaged in the active conduct of a trade or business in a foreign country to an unrelated financial institution engaged in the active conduct of a banking business in a foreign country For withholding tax purposes only, treats interest paid by 80/20 companies as foreign source to the extent that the company's income is derived from foreign sources in the active conduct of a trade or business outside of the United States. However, U.S withholding tax is imposed if interest is paid to related persons by a foreign-controlled 80/20 company	(a)(1) Treats interest and dividends paid by 80/20 companies as foreign source to the extent that the company's income is derived from foreign sources.
			(2) Repeals 80/20 rule for interest paid by individuals.	(2) Interest paid by individuals is treated as foreign source to the extent the individual's income is derived from foreign sources
b. Interest not subject to U.S. tax	(b) Present law effectively exempts from U.S. tax some categories of interest income when earned by foreign persons (for example, interest earned on U.S. bank deposits) by treating the income as foreign source.	(b) Retain the present law exemptions but restructure some of them (including that for U.S. bank deposits) as overt exemptions and treat the interest subject to the restructured exemptions as U.S. source.	(b) Same as President's proposal	(b) Same as President's proposal and House bill
		Effective date.—Generally, taxable years beginning after 1985. The modification of the source rule for interest paid by 80/20 companies would apply to interest paid on debt obligations incurred after January 1, 1986	*Effective date.*—Generally, taxable years beginning after 1985. For interest paid by 80/20 companies, the provisions only apply to interest paid on debt obligations incurred after January 1, 1986, but interest on certain prior debt is resourced as if paid by a foreign corporation Provides a targeted transitional rule	*Effective date.*—Taxable years beginning after 1986.

5. Allocation of interest and other expenses (other than research and development) (sec. 611 of the House bill and sec. 911 of the Senate amendment)	(a) Under Treasury regulations, taxpayers generally allocate interest and other expenses between gross U.S and gross foreign income on a separate, company-by-company basis, even if they are members of an affiliated group The separate company allocation rule conflicts with a Court of Claims case, decided before the regulations became effective, which indicates that expenses that are not definitely allocable against U.S or foreign gross income should be deducted from gross income on a consolidated group basis.	(a) Corporations joining in filing a consolidated return (but not other corporate members of affiliated groups) would be required to allocate interest expense on a consolidated group basis rather than on a company-by-company basis.	(a)(1) Requires allocation of expenses other than interest on an affiliated group basis.	(a)(1) Same as House bill
			(2)(i) Requires all corporate members of U.S affiliated groups to allocate interest on a consolidated group basis. Permits some corporations that cannot join in filing consolidated returns to continue allocating expenses on a separate company basis	(2)(i) Corporate members of affiliated groups must allocate interest between U S and foreign income on the basis of an expanded affiliated group, which includes foreign and possessions corporations
				(ii) Provides exception for "qualified" debt (in general, unguaranteed debt) of lower-tier U.S. members Upon a group-wide election, such debt of any U.S. member is treated as supporting only that member's assets Under an equalization rule, other members' unqualified debt is allocated to foreign income to the extent necessary to reach the result under the general rule, if possible.
			(3) Permits financial institutions to continue allocating interest expense on a separate company basis if their activities are independent of other members	(3) No exceptions are made for financial institutions.
	(b) Generally, under Treasury regulations, interest expense is allocated between U S and foreign income on the basis of the value of the taxpayer's assets that generate U.S and foreign income For affiliates, only stock basis is taken into account.	(b) No provision.	(b) Modifies the asset method of allocating interest expense by looking to earnings and profits of foreign corporations as well as stock basis	(b) For purposes of the asset method of allocating interest expense, all assets of U.S., foreign, and possessions affiliates (including debt-financed assets) are taken into account.
	(c) Optional gross income methods for apportioning interest expense are also available under the regulations	(c) No provision	(c) Eliminates the optional gross income methods for apportioning interest expense	(c) Same as House bill
	(d) Taxpayers generally may take into account tax-exempt income and assets in allocating deductible interest and other expenses Since tax-exempt income and assets are generally U S-based, taxpayers can derive a second tax benefit (higher foreign income and, hence a higher foreign tax credit limitation) from ownership of tax-exempt assets.	(d) Tax-exempt income and assets generating tax-exempt income would not be taken into account for purposes of allocating interest expense.	(d) Same as President's proposal	(d) Same as President's proposal and House bill.
		Effective date —Generally, taxable years beginning after 1985. Tax-exempt obligations held before 1986, and income derived from such obligations, could continue to be taken into account for purposes of allocating interest expenses	*Effective date.*—Generally, taxable years beginning after 1985. The allocation of interest on pre-existing loans is phased in over a three-year period An alternative transitional rule permits up to a five-year phase-in of the consolidated group rule for recent loans, and a targeted transitional rule is provided	*Effective date* —Generally, taxable years beginning after 1986, but the allocation of interest on existing loans is phased in over 4 years Targeted transitional rules are provided

6. Allocation of research expenses to foreign source income (sec. 616 of the House bill and sec. 1303 of the Senate amendment)	A suspended Treasury Regulation (sec 1.861-8) rule requires taxpayers with foreign-source income from products in a product area in which the taxpayers do U.S research to allocate part of their U.S. research expense against the foreign-source income In 1981, the Congress suspended this rule for two years, so that all U.S. research expenditures generally offset U.S.-source income. In 1984, the Congress extended the moratorium for two additional years.	No provision	the first two taxable years beginning after July 31, 1985, is modified as follows (1) Taxpayers apportion automatically 50 percent of U.S.-incurred research expense to domestic income. (2) The remainder is apportioned on the basis of gross sales or gross income *Effective date.*—Generally, taxable years beginning after July 31, 1985 and on or before August 1, 1987.	cent of U.S.-incurred research expense is allocated to domestic income, and the extension is for one year beyond the extension provided by the Consolidated Omnibus Budget Reconciliation Act of 1985 *Effective date*.—Taxable years beginning after August 1, 1986 and on or before August 1, 1987

C. U.S. Taxation of Income Earned Through Foreign Corporations				
1. Tax haven income subject to current tax (secs. 621-624 of the House bill and secs. 921-924 and 989 of the Senate amendment)				
a. Tax haven income generally	(a)(1) In general, no current U.S. tax is imposed on the foreign income of a foreign corporation, and a U S investor in a foreign corporation is taxed only when income is distributed to him. However, the deferral of U.S. tax on the income of U.S.-owned foreign corporations does not apply to certain kinds of income that are suited to tax haven operations. Under the Code's subpart F rules, when a U.S.-controlled foreign corporation earns this tax haven income, the United States will generally tax the corporation's 10-percent U.S. shareholders currently. Subpart F income includes foreign personal holding company (FPHC) income, consisting generally of several types of passive income. Some passive income is not included in FPHC income, however.	(a)(1) None.	(a)(1) Adds the following passive types of income to FPHC income for subpart F purposes: (i) gain from the sale of any property that gives rise to passive types of income; (ii) income from commodities transactions generally (subject to exceptions for hedging transactions and for active producers, processors, merchants, or handlers of commodities); (iii) foreign currency gains generally (with a business needs exception); (iv) passive leasing income generally; (v) no provision; (vi) payments from related persons in the same foreign country that reduce the FPHC income of the payors; and (vii) income from rents and royalties routed through a related party in a country that is neither the country of creation nor of use.	(a)(1) Adds the following passive types of income to FPHC income for subpart F purposes: (i) gain from the sale of any noninventory property that gives rise to passive types of income or does not give rise to any income, with allowance for offsetting losses from such sales; (ii) same as House bill with allowance for offsetting losses from such transactions; (iii) foreign currency gains from transactions in financial assets and liabilities (with a business needs exception and an allowance for offsetting foreign currency losses); (iv) same as House bill; (v) income equivalent to interest, (vi) same as House bill, and (vii) retains present law
	(2) Subpart F income also includes foreign base company shipping income (which excludes shipping income reinvested in shipping operations)	(2) None.	(2) Repeals the reinvestment exception so as to tax shipping income currently	(2) Retains present law
	(3) Subpart F income does not generally include interest, dividends, and securities gains earned by banks. The banking exceptions apply to some corporations that are not bona fide, active banks	(3) None.	(3) The subpart F banking exceptions are repealed.	(3) Same as present law, except provides that the banking exceptions from subpart F apply only to bona fide, active banking operations.
	(4) Certain dividends from a 50-percent owned same country corporation are not treated as subpart F income	(4) None.	(4) No provision.	(4) The same country exclusion of present law is extended to dividends attributable to specified mining-related income from a less than 50-percent owned corporation

	Present Law	President's Proposal	House Bill	Senate Amendment
a. Tax haven income generally (Cont.)	(a)(5) Other categories of subpart F income include certain income from the insurance of U.S. risks and foreign base company income from certain sales and services (including insuring related persons' third-country risks). Foreign corporate earnings from insuring foreign risks of unrelated persons are not subject to current U.S. tax under subpart F	(a)(5) None	(a)(5) Amends the definition of tax haven insurance income to include income from the insurance of unrelated persons' risks outside of the insuring company's country of incorporation; repeals the 5-percent de minimis exception for income from the insurance of U.S. risks	(a)(5) Retains present law
	(6) Current U.S. tax is generally not imposed under subpart F if the IRS finds that a U.S.-controlled foreign corporation was not formed or availed of to avoid tax	(6) None.	(6) Replaces the subjective tax-avoidance test with an objective test that looks to the rate of foreign tax paid by a U.S.-controlled foreign corporation, allowing the IRS to determine whether income (otherwise subject to subpart F) is properly treated as tax-haven income.	(6) Retains present law
	(7) Controlled partnerships are not treated as related persons for purposes of the subpart F rules that tax certain transactions with related persons	(7) None	(7) Treats a partnership that is controlled by a controlled foreign corporation as a related person for purposes of subpart F *Effective date.*—Taxable years of foreign corporations beginning after 1985.	(7) Same as House bill *Effective date.*—Taxable years of foreign corporations beginning after 1986.
b. Determination of U.S. control of foreign corporation	(b) The rules that impose U.S. tax currently on tax haven income of a foreign corporation apply only if a U.S. ownership requirement is satisfied: more than 50 percent of the voting power of the corporation must belong to U.S. persons each of which owns at least 10 percent of the voting power Older, similar, but less extensive rules requiring current U.S. taxation—the foreign personal holding company (FPHC) rules—apply only if more than 50 percent of the value of the corporation belongs to five or fewer U.S. individuals	(b) None	(b) Amends the U.S. ownership requirements for imposition of the anti-tax haven and FPHC rules. For the anti-tax haven rules to apply, 50 percent or more (rather than more than 50 percent) of the vote or value (not merely vote) of a foreign corporation must belong to 10-percent U.S. shareholders Similarly, for the FPHC rules to apply, 50 percent or more (rather than more than 50 percent) of the vote or value of a foreign corporation must be owned by five or fewer U.S. individuals. *Effective date.*—Generally, taxable years beginning after 1985. The change to the "50-percent or more" test does not apply to taxable years of foreign corporations beginning during 1986	(b) Retains the more than 50 percent tests of present law and adopts the vote or value rules of the House bill *Effective date.*—Taxable years beginning after 1986. Under a transition rule, deficits in earnings and profits accrued, and U.S. property acquired, in taxable years beginning before 1987, are exempt from the application of the anti-tax haven rules that would otherwise result from the change made by the provision A special rule is provided for determining the portion of certain trust distributions that has been previously taxed under subpart F.

Item	Present Law	President's Proposal	House Bill	Senate Amendment
c. De minimis tax haven income rule	(c) The rules that impose current U.S tax on foreign base company income (a type of tax haven income) of a foreign corporation apply only if certain threshold requirements are met One such requirement is that 10 percent or more of the foreign corporation's gross income must be foreign base company income. If more than 70 percent of the foreign corporation's gross income is foreign base company income, all of its gross income is treated as foreign base company income.	(c) None	(c) Applies the de minimis and 70-percent tests for foreign base company income on the basis of net income instead of gross income *Effective date.*—Taxable years of foreign corporations beginning after 1985	(c) Reduces the de minimis test for foreign base company income from 10 percent or more of gross income to 5 percent or more of gross income *Effective date* Taxable years of foreign corporations beginning after 1986
d. Possessions corporations	(d) A corporation chartered in a U.S. possession with at least 80 percent of its income derived in the possessions and no more than 50 percent of its gross income from passive investments is not treated as a controlled foreign corporation; thus U.S. tax on its tax haven income is deferred	(d) This exception to the anti-tax haven rules would be repealed *Effective date.*—Taxable years beginning after 1985. Under a transition rule, deficits in earnings and profits accrued, and property acquired, in taxable years beginning before 1986, would be exempt from the application of the anti-tax haven rules that would otherwise result from the repeal of the exception for corporations chartered in the possessions.	(d) Same as President's proposal. *Effective date.*—Same as President's proposal.	(d) Same as President's proposal and House bill. *Effective date.*—Taxable years beginning after 1986 Under a transition rule, deficits in earnings and profits accrued, and U S property acquired, in taxable years beginning before 1987, are exempt from the application of the anti-tax haven rules that would otherwise result from the repeal of the exception for corporations chartered in the possessions
2. **Application of accumulated earnings tax and personal holding company tax to foreign corporations (sec. 626 of the House bill and sec. 926 of the Senate amendment)**	The accumulated earnings tax (AET) and personal holding company (PHC) tax are imposed on corporations that accumulate earnings rather than distributing them to their shareholders The taxes are imposed on "accumulated taxable income" and "undistributed personal holding company income," respectively Those amounts are calculated by making several adjustments to the regular taxable income of a corporation including deductions for capital gains (and certain capital losses)	None	For purposes of calculating the AET or PHC tax applicable to a foreign corporation, an adjustment is allowed for net capital gains only if they are effectively connected with the conduct of a U.S. trade or business *Effective date.*—The amendments apply to gains and losses realized on or after November 16, 1985.	Same as House bill. *Effective date*—The amendments apply to gains and losses realized on or after March 1, 1986
3. **Deduction for dividends received from foreign corporations (sec. 987 of the Senate amendment)**	A U.S corporation may deduct 85 percent of a fraction of dividends received from a foreign corporation that has at least 50 percent of its business in the United States The deductible fraction is the ratio, for a 3-year period, of gross income that is effectively connected with a U.S. trade or business to total gross income A U.S. corporation may deduct 100 percent of certain dividends from a foreign corporation all of whose gross income is effectively connected with a U.S trade or business and all of whose stock is owned by the U.S. corporation.	In Part VI.C., above, would increase 85-percent dividends received deduction to 100 percent in the case of eligible dividends from foreign corporations, in connection with the dividends paid deduction.	In Part VI B and C., above, reduces 85-percent dividends received deduction to 80 percent, and further reduces it to 70 percent (and the present law 100 percent deduction is reduced to 90 percent) in connection with the dividends paid deduction	Reduces 85-percent dividends received deduction to 80 percent (in part VI C, above) Allows deduction for dividends received from foreign corporations only to 10-percent or greater corporate owners Extends deduction to dividends from foreign corporations that are in turn attributable to dividends from U.S corporations 80 percent or more of whose voting stock (or value) the foreign corporation (or a wholly-owned foreign subsidiary) owns and eliminates the 50-percent business income threshold of present law Bases eligibility for deduction on net earnings of foreign corporation attributable to U.S sources All dividends eligible for the deduction are treated as U.S source *Effective date.*—Dividends received in taxable years beginning after 1986

Item	Present Law	President's Proposal	House Bill	
D. Special Tax Provisions for U.S. Persons				
1. Possession tax credit (sec. 641 of the House bill and sec. 941 of the Senate amendment)				
a. Income-based credit	(a) U S corporations meeting certain requirements are allowed to claim an income tax credit for U.S tax on U.S possession source income Similar rules apply to the U S. Virgin Islands To qualify, at least 80 percent of a possession subsidiary's income must be derived from the possessions, and no more than 35 percent of the income may be from passive investments. The possession tax credit is not allowed with respect to income generated from intangibles transferred to the possessions unless the taxpayer elects one of two optional methods of allocating intangible income. (1) the cost sharing method or (2) the 50/50 profit split method. The cost sharing payment need not be as great as an arm's-length royalty The two intangible income allocation methods are not allowed for any product unless (1) at least 25 percent of the value added to the product is a result of economic activity in the possessions, or (2) at least 65 percent of the direct labor cost for the product is incurred in the possessions. Income must be received in the possessions to be eligible for the credit	(a) The possession tax credit would be repealed, subject to a 5-year transition rule, and replaced with a tax credit based on wages paid by manufacturing establishments in the possessions (including the U.S. Virgin Islands) described at c., below *Effective date.*—Under a transition rule, corporations could elect to continue to use the present tax credit for 5 years, beginning with the first taxable year ending after 1985, with respect to possession source income from products that were manufactured or validly designated during the taxable year beginning in 1985.	(a) Retains present law except (1) Under the cost sharing method, the cost sharing payment is equal to the greater of (i) 110 percent of the payment required under present law or (ii) the royalty payment that would be required with respect to manufacturing intangibles if the possession corporation were treated as a foreign corporation; (2) under the profit split method, the amount of product area research expenditures is increased by 20 percent for purposes of computing combined taxable income; (3) the passive income limitation is reduced to 25 percent; (4) the credit is allowed for otherwise eligible income received in the United States; and (5) the rules granting the Virgin Islands treatment similar to that given to the other possessions are modified to grant the Virgin Islands treatment identical to the treatment given to the other possessions *Effective date.*—Generally, taxable years beginning after 1985 Under a transition rule, the passive income limitation is phased down to 30 percent for taxable years beginning in 1986, and to 25 percent for taxable years beginning in 1987	(a) Same as House bill except: (1) Under the cost sharing method, the cost sharing payment is equal to 110 percent of the payments required under present law, (2) Same as House bill, (3) Same as House bill, (4) The credit is allowed for otherwise eligible active business income received from unrelated parties in the United States, and (5) Same as House bill *Effective date*—Taxable years beginning after 1986.
b. Qualified possession source investment income (QPSII)	(b) Investment income eligible for the possessions tax credit (i e , QPSII) must be derived from investment within a possession in which the taxpayer conducts an active trade or business	(b) No provision	(b) QPSII is expanded to include income attributable to loans made by the Government Development Bank of Puerto Rico (GDB) for the acquisition or construction of active business assets in qualified Caribbean Basin Initiative (CBI) countries Compliance rules are provided Puerto Rico is expected to provide $100 million of loan funds for CBI countries *Effective date*—Taxable years beginning after 1985.	(b) Same as House bill except (1) loans by financial institutions other than the GDB are allowed, (2) loans may be used for development projects, and (3) additional compliance rules are provided No specific amount of CBI loan fund commitment by Puerto Rico is required. *Effective date*—Taxable years beginning after 1986

c. Wage credit	(c) No provision	(c) The credit for wages paid by manufacturing establishments in the possessions would equal 60 percent of wages up to the Federal minimum wage (currently $6,968 on an annual basis), plus 20 percent of wages in excess of the minimum wage, up to four times the minimum wage. *Effective date*.—The wage credit would be available for taxable years beginning after 1985	(c) Retains present law	(c) Retains present law
2. Other rules with respect to U.S. possessions (secs. 671–678 and 615 of the House bill and secs. 971–977 and 911 of the Senate amendment)				
a. U.S. Virgin Islands	(a)(1) The U S Virgin Islands (like Guam, the Commonwealth of the Northern Mariana Islands, and Samoa (see b., below)) generally uses the Code as it changes from time to time as its local tax code. For corporate tax purposes, the United States treats each of these possessions as a foreign country and each of these possessions treats the United States as a foreign country This system of taxation has acquired the name "mirror system" because the possession uses the Code (but substitutes its own name for the United States and. for some purposes, treats the United States as the United States treats a possession)	(a)(1) In general, clarify the operation of the U.S Virgin Islands' mirror system to prevent unintended results Treat any bona fide V I resident on the last day of the taxable year as taxable only in the Virgin Islands, and not in the United States. A U S individual (other than a V I. resident) who derives income from the Virgin Islands would file two identical returns, one with the United States and one with the Virgin Islands, and would pay a pro rata amount of tax to each. Provide for cooperation between the IRS and the Virgin Islands Bureau of Internal Revenue	(a)(1) Same as President's proposal, but provides anti-abuse rules and authorizes the Secretary to prescribe regulations for purposes of determining V I tax liability *	(a)(1) Same as President's proposal and House bill
	(2) The Virgin Islands may impose a surtax of up to 10 percent on the mirror tax The Virgin Islands can rebate its mirror tax on its resident individuals and on U S and V I corporations that operate primarily in the Virgin Islands	(2)(i) Permit the Virgin Islands to impose any nondiscriminatory local income taxes in addition to those it now imposes under the mirror system (ii) Permit the Virgin Islands to rebate tax on U.S corporations whatever the extent of their activities in the Virgin Islands. (iii) Consider authorizing the Virgin Islands to reduce or rebate V I tax on some foreign persons' V I income.	(2)(i) Same as President's proposal (ii) Same as President's proposal (iii) Allows reduction of V I tax on V I income of foreign persons *Due to clerical error, the House passed version of these rules is not contained in the version of the House bill transmitted to the Senate It may be found in the *Congressional Record* of December 10, 1985, at page H11721	(2)(i) Same as President's proposal and House bill (ii) Same as President's proposal and House bill (iii) Same as House bill, and allows reduction of V I tax on non-U S non-V I income of foreign corporations with less than 10 percent U S ownership

a. U.S. Virgin Islands (Cont.)	(3) An "inhabitant" of the Virgin Islands pays tax to the Virgin Islands on its worldwide income, but pays no U.S. tax. Certain corporations qualify for inhabitant status, including some U.S. corporations.	(3) Repeal the V.I. inhabitant rule.	(3) Same as President's proposal.	(3) Same as President's proposal and House bill.
	(4) A V.I. corporation is not subject to the U.S. 30-percent withholding tax on passive income so long as it meets criteria designed to prevent the use of V.I. corporations as conduits for third-country residents: the V.I. corporation must be less than 25 percent foreign-owned and earn at least 20 percent of its income from V.I. sources.	(4) Amend the rules that prevent foreigners from using V.I. corporations as conduits to avoid the U.S. 30-percent withholding tax by substituting a requirement that 65 percent of a corporation's income be effectively connected with a trade or business in a possession or in the United States, in place of the 20-percent source of income requirement in current law.	(4) Same as President's proposal.	(4) Same as President's proposal and House bill.
		Effective date.—Taxable years beginning after 1985.	*Effective date.*—Generally, taxable years beginning after 1985, but certain provisions are contingent upon implementation of a U.S.-V.I. agreement to coordinate the U.S.-V.I. tax systems.	*Effective date.*—Generally, taxable years beginning after 1986, except that repeal of the V.I. inhabitant rule applies to all open years. If an implementing agreement is not in place within one year after enactment, Treasury shall report on the status of negotiations.
b. Guam, the Northern Mariana Islands, and American Samoa	(b)(1) U.S. law requires that Guam use the Code as its local code. (See general description of the mirror system of taxation at a., above.) Individual residents of the United States or Guam need file a tax return only with the place where they resided on the last day of the year. Guamanian corporations are not subject to the U.S. 30-percent withholding tax, except Guamanian corporations that are conduits (under the rules that apply to V.I. corporations). The Commonwealth of the North Mariana Islands (CNMI) is required to use the mirror system in basically the same way as Guam. The latter treatment generally began on January 1, 1985.	(b)(1) Grant Guam and the CNMI full authority to determine their own income tax laws. This treatment would place them on a par with American Samoa. Require that Guam and the CNMI implement tax systems that would raise at least as much revenue as their current mirror systems. Residents of Guam and the CNMI who received income from outside those possessions would have to file U.S. tax returns. The United States would collect the tax on that non-possession income, but would transfer the money to the possession where the taxpayer resided. For the purpose of the U.S. 30-percent withholding tax, the proposal would modify the anti-conduit rule for Guam and the CNMI in the same way as proposed for the Virgin Islands.	(b)(1) Same as President's proposal.	(b)(1) Same as President's proposal and House bill.

b. Guam, the Northern Mariana Islands, and American Samoa (Cont.)	American Samoa has adopted its own income tax system. American Samoa has chosen to use the Code, with minor amendments, as its internal income tax system	For American Samoa, Guam, and the CNMI, implement anti-abuse provisions to prevent the use of corporations in these possessions to avoid U.S. tax Coordinate taxes among these possessions and exchange information between each possession and the United States Each possession would receive taxes withheld on compensation of U.S. Government personnel stationed there.	Same as President's proposal, and extends anti-abuse provisions to individuals resident in a possession	Same as President's proposal and House bill
	(2) Interest income on U.S. obligations held by the Bank of Guam is treated as effectively connected with the conduct of a U.S trade or business.	(2) No provision	(2) Provides that interest income on U.S. Government obligations held by the Bank of Guam is treated as not effectively connected with the conduct of a U.S. trade or business	(2) Same as House bill
		Effective date.—Generally, January 1, 1986 The mirror codes of Guam and the CNMI would continue to operate until and except to the extent that each possession took action to amend its own laws.	*Effective date.*—Taxable years beginning after 1985, but only if (and so long as) an agreement is in effect between a possession and the United States to coordinate the U.S and possession tax systems. The provision concerning Bank of Guam is effective for taxable years beginning after November 16, 1985.	*Effective date.*—Generally, taxable years beginning after 1986, but only if (and so long as) an agreement is in effect between a possession and the United States to coordinate the U.S. and possession tax systems If an implementing agreement is not in place within one year after enactment, Treasury shall report on the status of negotiations. The provision concerning bank of Guam is effective for taxable years beginning after November 16, 1985.
3. Taxation of U.S. employees of Panama Canal Commission (sec. 612 of the House bill and sec. 942 of the Senate amendment)	(a) An agreement between the United States and Panama entered into in conjunction with the Panama Canal Treaty specifies the rights and legal status of agencies and employees of the U.S. Goverment operating in Panama One article of the agreement provides an exemption from tax for U.S. employees of the Panama Canal Commission. In a diplomatic note, Panama has confirmed the United States' explanation that the exemption was intended to apply solely to Panamanian taxes. Courts have split on the question whether the exemption applies to U.S taxes.	(a) None.	(a) Clarifies that the Agreement in Implementation of the Panama Canal Treaty does not exempt U.S. taxpayers from U.S tax *Effective date.*—All open taxable years.	(a) Same as House bill *Effective date.*—Taxable years beginning on or after January 1, 1987.
	(b) Overseas employees of the U.S government are permitted to exclude certain allowances from gross income for U.S tax purposes Allowances paid to U.S employees of the Panama Canal Commission are not presently excludable under this rule.	(b) None	(b) Provides that U.S. government employees of the Panama Canal Commission may exclude allowances equivalent to those permitted to be excluded by State Department employees in Panama. *Effective date*—Taxable years beginning after 1985	(b) Same as House bill, and extends tax-free allowance treatment to Defense Department employees in Panama *Effective date*—Taxable years beginning after 1986

Item	Present Law	President's Proposal	House Bill	Senate Amendment
4. Foreign Sales Corporation (FSC's) (sec. 643 of the House bill)	The United States limits its tax on qualified income from exports when the exporter uses a "FSC"—a Foreign Sales Corporation. The FSC rules reduce taxable income by 16 percent of export income (15 percent for corporate shareholders). The Domestic International Sales Corporation (DISC) rules provide a similar benefit but only on the income from $10 million in export sales.	None.	Changes FSC rules to exempt 14 percent of export income (13 percent for corporate shareholders). Makes corresponding changes to DISC rules. *Effective date.*—Taxable years beginning after 1985.	Retains present law
5. Exclusion for private sector earnings of Americans abroad (sec. 644 of the House bill and secs. 943 and 988 of the Senate amendment)	U.S. citizens (other than U.S. Government employees) who live and work abroad and who satisfy certain physical presence or bona fide foreign residence tests may exclude from gross income their foreign earned income up to $80,000 per year, and may also exclude their foreign housing costs that exceed a base amount. The $80,000 ceiling on excludable foreign earned income is scheduled to increase $5,000 each year beginning in 1988, up to $95,000 for taxable years beginning in or after 1990. This schedule reflects a Deficit Reduction Act of 1984 freeze of the increases, which the Economic Recovery Tax Act of 1981 had scheduled to begin in 1984.	None.	(a) Reduces the foreign earned income exclusion ceiling to $75,000. (b) No provision. *Effective date.*—Taxable years beginning after 1985.	(a) Reduces the foreign earned income exclusion ceiling to $70,000. (b) Denies benefits to individuals violating Federal travel restrictions *Effective date.*—Taxable years beginning after 1986.
6. Transfers of intangibles to related parties outside of the U.S. (sec. 641 of the House bill)	Transfers to related foreign corporations as licenses or sales are subject to an "arm's-length" price standard. Uncertainty exists regarding what transfers are appropriate to treat as "arm's-length" comparables and regarding the significance of profitability, including major changes in profitability of the intangible after the transfer. Transfers to related foreign corporations as contributions to capital require the transferor to recognize annually, as U.S. source income, amounts that would have been received under an agreement providing for payments contingent on productivity, use, or disposition of the property. Special rules apply for transfers to related U.S. possessions corporations (see Possessions Tax Credit, above).	No provision.	Payments with respect to intangibles transferred to a foreign related party must be commensurate with the income attributable to the intangible. This standard also applies to determine the minimum cost-sharing payment with respect to intangibles transferred to a related U.S. possessions corporation that elects the cost-sharing option. (See item D.1.a.(1), above.) *Effective date.*—For transfers from U.S persons to foreign related parties, the bill applies to transfers after November 16, 1985 in taxable years ending after that date. For transfers to U.S. possessions corporations that elect the cost-sharing option, the bill applies for taxable years beginning after December 31, 1985.	Retains present law.

Item	Present Law	President's Proposal	House Bill	Senate Amendment
7. Compliance provisions applicable to U.S. persons resident abroad (sec. 986 of the Senate amendment)	U.S. persons resident abroad are required to file U.S tax returns, but a substantial percentage of foreign residents fails to do so.			
	(a) IRS formerly obtained some information from voluntary information returns filed with passport applications, but the return was discontinued because many taxpayers refused to file a voluntary return.	(a) No provision	(a) No provision.	(a) Requires that passport applicants and green card applicants complete an IRS information return disclosing foreign residence. Penalties for failure to file apply *Effective date* —Taxable years beginning after 1986.
	(b) U.S. pension payments to foreign residents, like all U.S. pension payments, are not subject to mandatory withholding such as that which applies to wage and salary payments.	(b) No provision.	(b) No provision	(b) Requires withholding with respect to pension payments to U.S. persons living outside the United States *Effective date.*—Taxable years beginning after 1986.
8. Foreign investment companies (sec. 625 of the House bill and sec. 925 of the Senate amendment)	Generally, no current U.S. tax applies to the foreign income of a foreign corporation that is not a controlled foreign corporation (under subpart F) or a foreign personal holding company (under the FPHC rules) even if all its income is passive income or other tax haven income, and even if all its shareholders are Americans When a U.S. person disposes of stock in a foreign investment company (FIC), however, the gain is not automatically subject to a favorable capital gains tax rate, even if the company is widely held The gain is subject to ordinary income treatment to the extent of the shareholder's share of the FIC's earnings and profits. This special ordinary income rule generally applies to a foreign corporation that is primarily in the business of investing in securities or commodities, if 50 percent or more of the corporation's stock (by vote or value) is held by U.S. persons.	No provision.	Amends the FIC rules as follows: (1) Applies the FIC rules to U.S investors in foreign funds without regard to the degree of U.S. ownership of such funds; (2) Requires current recognition of income by U.S. investors in FICs that are passive-investment vehicles, by looking through to the FIC's earnings and profits; (3) Tax is imposed on full amount of investor's share of the passive fund's earnings; (4) Allows U.S. investors in passive funds to defer tax upon agreement to pay tax plus interest on disposition of the investment; (5) Liberalizes the FIC rules to allow credits for foreign tax paid by a corporation that is both a FIC and a controlled foreign corporation; (6) The bill applies to passive FICs that had elected to distribute income currently (under sec. 1247); and (7) All income of a passive fund is taxed as ordinary income. *Effective date.*—Generally, taxable years of foreign corporations beginning after 1985.	Amends the FIC rules as follows: (1) Retains present law; (2) Imposes interest charge based on value of deferral for U.S. investors that invest in passive-investment vehicles (whatever the degree of U.S. ownership); (3) Tax is not imposed on an amount exceeding the investor's gain on disposition, (4) Allows election to pay tax currently; (5) Same as House bill; (6) The bill exempts passive FICs that had elected to distribute income currently (under sec. 1247); and (7) Provides look-through rules so that income earned by fund retains its character as capital gain or ordinary income upon showing by taxpayer *Effective date.*—Amounts received or accrued by foreign corporations on or after January 1, 1987.

Item	Present Law	President's Proposal	House Bill	Senate Amendment
E. Treatment of Foreign Taxpayers 1. Branch-level tax (sec. 651 of the House bill and sec. 951 of the Senate amendment)	Foreign corporations are subject to U.S corporate-level tax on income effectively connected with a U.S trade or business A shareholder-level tax also is imposed on some foreign corporate earnings: a 30-percent gross withholding tax applies to a pro rata portion of dividends paid by a foreign corporation if more than 50 percent of the corporation's income over a three-year period is effectively connected with a U.S. trade or business. A similar withholding tax applies to interest payments by foreign corporations. The withholding taxes are reduced or eliminated under a number of U.S. tax treaties. Some countries substitute a branch-level tax for a direct shareholder-level tax on domestic source earnings of foreign corporations.	(a) Impose a tax on remitted profits of U.S. branches of foreign corporations. (b) Impose a tax on foreign corporations' interest payments that are allocable to U.S branch operations (c) Tax would be imposed at a 30-percent rate, or at lower treaty rate that would apply to direct-investment dividends paid to the foreign corporation. (d) Repeal the withholding taxes on dividends and interest paid by foreign corporations. (e) Tax would not be imposed when existing U.S. treaties prohibit a tax on branch profits—some argue that a number of existing treaties do so. *Effective date.*—Taxable years beginning after December 31, 1985.	(a) Same as President's proposal. (b) Same as President's proposal (c) Same as President's proposal (d) In the case of countries with treaties that now allow a U.S. withholding tax, but not the branch profits tax, retains present law; otherwise same as President's proposal (e) Overrides treaties to the extent they allow treaty shopping (f) Allows a credit against a U.S. company's U.S. tax for any branch level tax imposed on a foreign corporation owned by the U.S. company on receipt of a dividend from the foreign corporation. *Effective date.*—Taxable years beginning after 1985.	(a) Same as President's proposal and House bill. (b) Imposes no branch tax on interest. (c) Imposes tax at lower of 30 percent or treaty branch tax rate (or, if none, treaty direct investment dividend rate). (d) For dividends, retains present law second-level withholding tax (but reduces the 50-percent income threshold to 10 percent) when treaties prohibit imposition of branch tax. Retains present law second-level withholding tax on interest but reduces income threshold to 10 percent and treats interest as U.S. source if it is deducted in the United States. (e) Same as House bill, except overrides treaties in treaty shopping cases with respect to the second-level withholding taxes also. (f) In Part C.3., above, expands the current deduction for dividends received from foreign corporations. *Effective date*—Taxable years beginning after 1986.
2. Retain character of effectively connected income (sec. 652 of the House bill and sec. 952 of the Senate amendment)	The United States taxes foreign persons' income that is effectively connected with a U.S. trade or business on a net basis at graduated rates, in the same manner that it taxes the income of U.S persons. Foreign persons may not be subject to U.S. tax if they receive income that was earned by a U.S. trade or business in a year after the trade or business has ceased to exist (e g., by selling property and recognizing the gain on the installment basis).	None.	Provides that income or gain is treated as effectively connected with a U.S. trade or business if it is attributable to another taxable year and would have been so treated if it had been taken into account in that other year. *Effective date.*—Taxable years beginning after 1985.	Same as House bill, and treats the removal of business assets from U.S jurisdiction as a disposition, with basis step-up for this purpose for business assets brought into the United States. A foreign person's sale of U.S assets that formerly were used in a U.S. business is taxable. *Effective date.*—Taxable years beginning after 1986.
3. Tax-free exchanges by expatriates (sec. 653 of the House bill and sec. 953 of the Senate amendment)	A U.S. citizen who gives up citizenship for a principal purpose of avoiding U.S. tax will generally continue for a period of ten years to be taxed as a citizen on U.S. source income, but not foreign source income. U.S. source income for this purpose includes gains from sales of U.S. property. Tax-avoidance expatriates may be able to avoid tax by making a tax-free exchange of U.S property for foreign property.	None.	Applies the tax-avoidance expatriate rules to gains on the sale of property the basis of which was determined by reference to property located in the United States, stock of a U.S. corporation, or a debt obligation of any U.S. person. *Effective date.*—The rule applies to sales of property acquired in tax-free exchanges after September 25, 1985.	Same as House bill. *Effective date*—The rule applies to sales of property acquired in tax-free exchanges after March 1, 1986.

4. Excise tax on insurance premiums paid to foreign insurers and reinsurers (sec. 654 of the House bill and sec. 954 of the Senate amendment)	Foreign insurers and reinsurers frequently are not subject to U.S. income tax, but rather to an excise tax on premiums paid to them for the direct insurance or reinsurance of U.S. risks. The excise tax rates are (per dollar of premium): four cents for casualty contracts, one cent for life contracts, and one cent for all reinsurance. The taxes are collected by return Payments to some insurers and reinsurers are exempt by treaty, but reinsurance premiums paid by treaty-protected insurers and reinsurers are subject to the tax (unless the recipient is exempt by treaty).	None.	Makes the excise tax on casualty reinsurance premiums paid to foreign insurers for U S risk coverage equal to that on similar casualty insurance premiums (four percent). Imposes an excise tax only once—on retained premiums received by foreign insurers or reinsurers. Makes the foreign insurer (or his agent) liable for the tax and requires the U.S. insured or broker obligated to transmit the premiums to withhold the tax *Effective date.*—The tax applies to premiums paid after December 31, 1985.	Requires the Treasury Department to study whether U.S. reinsurance corporations are at a significant competitive disadvantage vis-a-vis foreign reinsurance corporations by reason of U.S. treaties, and report before January 1, 1988. If U.S reinsurance corporations are at such a competitive disadvantage, the Senate believes that the Treasury Department should renegotiate the relevant treaties to eliminate that disadvantage. *Effective date.*—Date of enactment.
5. Reporting by foreign-controlled corporations (sec. 986(c) of the Senate amendment)	Foreign-controlled foreign corporations doing business in the United States and foreign-controlled U.S. corporations are required to report transactions with related foreign corporations.	No provision.	No provision	Requires foreign-controlled foreign corporations doing business in the United States and foreign-controlled U.S. corporations to report transactions with all related foreign persons, whether or not a corporation. *Effective date.*—Taxable years beginning after 1986.
6. Foreign investors in U.S. partnerships (sec. 985 of the Senate amendment)	Foreign persons who earn wages or investment income in the United States are generally subject to withholding requirements designed to ensure collection of applicable U.S. taxes. Foreign persons with investments in U.S partnerships, however, are not subject to a withholding tax	No provision	No provision.	Requires that partnerships withhold with respect to U.S. effectively connected income allocable to foreign partners. *Effective date.*—Taxable years beginning after 1986.
7. Income of foreign governments (sec. 982 of the Senate amendment)	Foreign governments are not subject to U.S. tax on income from their investments in the United States Treasury regulations specify that income from commercial activities is not investment income and therefore is not exempt from U.S. tax	No provision.	No provision	Codifies the rule taxing the commercial activities of foreign governments, and defines commercial activity to include ownership of a controlling interest in a corporation engaged in trade or business in the United States Clarifies that the determination of whether a government is engaged in commercial activities is to be made by reference to its activities worldwide. The foreign government exception does not apply to controlled entities if they or related entities engage in any commercial activities anywhere in the world *Effective date.*—July 1, 1986

Item	Present Law	President's Proposal		
8. Transfer prices for imports (sec. 981 of the Senate amendment)	Importers may claim a transfer price for customs purposes that is too low to be consistent with the transfer price they claim for income tax purposes (See Brittingham 66 T.C. 373; 79-2 USTC 9494).	No provision	No provision.	Importers cannot claim a transfer price for income tax purposes that is higher than would be consistent with the value they claim for customs purposes *Effective date.*—Transactions entered into after March 18, 1986
9. Dual resident companies (sec. 983 of the Senate amendment)	U.S. corporations that are "residents" of foreign countries may consolidate with profitable companies both here and abroad and obtain for related parties two deductions for one item of expense.	No provision.	No provision.	Does not allow a U.S corporation to consolidate with other U.S. corporations if related foreign parties benefit from its losses through foreign consolidation or group relief rules, unless the income of those related foreign parties is or will be subject to U.S tax. *Effective date.*—Taxable years beginning after 1986.
10. Interest paid to related tax-exempt parties (sec. 984 of the Senate amendment)	Certain taxpayers may unduly reduce their tax by deducting interest paid or accrued to related parties who do not pay U.S tax on the interest income	No provision.	No provision	Denies the deduction for interest paid or accrued to related, tax-exempt parties (other than ESOPs) to the extent net interest exceeds 50 percent of pre-net interest deduction taxable income. Provides carryover for disallowed amounts. This restriction also applies to back-to-back loans that might otherwise defeat the purpose of this rule. *Effective date.*—Taxable years beginning after September 30, 1986.

	Present Law	President's Proposal	House Bill	Senate Amendment
F. Foreign Currency Exchange Gain or Loss (sec. 661 of the House bill and sec. 961 of the Senate amendment)				
1. Functional currency concept	No provision	The determination of whether exchange gain or loss is recognized on a transaction-by-transaction basis, or in the aggregate on an annual basis, would be determined by reference to the economic environment in which a business entity operates.	Same as President's proposal.	Same as President's proposal and House bill
2. Identification of functional currency				
a. General rule	No provision.	(a) The functional currency of an entity generally would be the primary currency of the economic environment in which the entity operates.	(a) The functional currency is the U.S. dollar, except for a qualified business unit, in which case it is the currency used in keeping books and records and in which a significant part of business activities are conducted	(a) Same as House bill, except for a qualified business unit the functional currency of which is the currency of the economic environment in which a significant part of the unit's activities are conducted and which is used in keeping books and records
b. Activities primarily conducted in dollars		(b) No provision.	(b) A qualified business unit's functional currency is the U.S. dollar if activities are primarily conducted in U.S. dollars.	(b) Same as House bill.
c. Election to use U.S. dollar		(c) Taxpayers would always be allowed to elect to use the U.S. dollar as the functional currency.	(c) A taxpayer may elect to use the U.S. dollar as the functional currency of a qualified business unit if the unit keeps its books in U.S. dollars.	(c) Same as House bill, with regulatory authority to permit election if taxpayer uses a method of accounting that approximates a separate transactions method.
3. Change in functional currency as method of accounting	No provision.	Choice of a functional currency, including the election of the U.S. dollar, would be treated as a method of accounting that could be changed only with consent of the Secretary.	Same as President's proposal.	Same as President's proposal and House bill, with clarification that the Secretary may establish procedures for taxpayers whose functional currency changes
4. Foreign currency transactions				
a. Definition of foreign currency transactions	(a) No provision.	(a) Foreign currency denominated financial assets or liabilities.	(a) Acquisition of a debt instrument, becoming an obligor under a debt instrument, accruing or otherwise taking into account an item of expense or income in a nonfunctional currency or by reference to the value of a nonfunctional currency that is to be paid after the date of accrual or taking into account.	(a) Same as House bill, with addition of entering into or acquiring forward contracts, futures, options, or similar financial instruments that are not marked to market under section 1256. Also, it is clarified that items of gross income or receipts (not net income) are taken account of.
(1) Disposition of nonfunctional currency		(1) No provision.	(1) The disposition of nonfunctional currency generates exchange gain or loss	(1) Same as House bill.

(2) De minimis exceptions		(2) No provision.	(2) Any class of items the taking into account of which is not necessary to carry out the purposes of the provisions by reason of small amount, short periods, or regularity with which items occur	(2) Same as House bill, but no exception based on regularity with which items occur
b. Character of exchange gain or loss				
(1) General rule	(b)(1) No provision.	(b)(1) Exchange gain or loss would be treated as an increase or decrease in interest income or expense.	(b)(1) Except for specified purposes, and as otherwise provided in regulations, exchange gain or loss is treated as interest income or expense.	(b)(1) Exchange gain or loss is treated as ordinary income or loss, and treated as interest income or expense only as provided in regulations
(2) Special rule for certain investment products	(2) No provision.	(2) No provision.	(2) Investment products that are listed in section 1256 of the Code are not treated as generating exchange gain or loss, if they are not part of a hedging transaction.	(2) For forward contracts, futures, and options that are not subject to the mark-to-market rules of section 1256 and that constitute capital assets, a taxpayer can elect to identify the transaction and treat any exchange gain or loss as capital gain or loss
c. Source	No provision.	(c) Exchange gains would be sourced under same rules that apply to interest income; exchange losses would be allocated and apportioned under the rules applicable to interest expense.	(c) The source of exchange gain or loss is determined in the same manner as interest income or expense, except a payor's exchange gain is sourced in a manner consistent with the payor's interest expense, and a payee's exchange loss is allocated in a manner consistent with the payee's interest income	(c) Exchange gain or loss is sourced or allocated by reference to the residence of the taxpayer or qualified business unit on whose books the underlying asset or liability is reflected A special rule is provided for certain related-party loans
d. Current accrual				
(1) Financial assets and liabilities	(d) No provision.	(d)(1) For financial assets and liabilities providing for fixed or determinable payments, anticipated exchange gain or loss would be currently accrued.	(d)(1) No provision.	(d)(1) No provision
(2) Integrated hedged transactions		(2) Exchange gain or loss on a contract that offsets the risk of exchange rate fluctuations with respect to a financial asset or liability would be recognized on an accrual basis	(2) To the extent provided in regulations, exchange gain or loss in the case of hedging transactions would be currently accrued Such transactions are treated as substantially equivalent to U.S dollar transactions	(2) Same as House bill, but clarifies definition of integrated hedging transactions
(3) Other hedged transactions		(3) No provision	(3) No provision.	(3) There is regulatory authority to provide for consistent treatment of hedging transactions that are not entered into as an integrated package

	Present Law	President's Proposal	House Bill	Senate Amendment
e. Tax straddle provisions				
(1) Hedging transactions	(e)(1) No provision	(e)(1) No provision	(e)(1) No provision.	(e)(1) Neither the loss-deferral rule nor the mark-to-market rule applies to a foreign currency hedging transaction that is treated in regulations.
(2) Special rule for banks	(2) A bank's hedging transactions need not satisfy all of the statutory tests for other taxpayers.	(2) No provision	(2) The special rule for banks is repealed.	(2) Same as House bill
(3) Clarification of loss-deferral rule	(3) No provision.	(3) No provision	(3) No provision	(3) Clarifies that the loss-deferral rule applies to a straddle involving an obligor's interest in foreign currency denominated debt.
f. Application to transactions of a personal nature	(f) No provision.	(f) No provision.	(f) No provision.	(f) The rules for foreign currency transactions apply to transactions of a personal nature only to the extent that expenses attributable to such transactions would be deductible as trade or business expenses or as expenses of producing income.
5. Foreign currency translation				
a. Translation method				
(1) Branches	(a)(1) Taxpayers operating through branches can use a profit-and-loss method or a net worth method.	(a) A business entity (e.g., a branch or separate corporation) that uses a functional currency other than the U.S. dollar would be required to use a profit-and-loss translation method. Thus, a single set of rules would generally be provided for branches and foreign corporations.	(a) Same as President's proposal.	(a) Same as President's proposal and House bill.
(2) Foreign corporations	(2) Controlled foreign corporations are required to use a net worth method to calculate subpart F deemed dividends, other dividends can be calculated using a profit-and-loss method.			
b. Exchange gain or loss on distribution of earnings				
(1) Branches	(b)(1) When a foreign branch remits currency in excess of the current year's profits, the basis of the excess amount must be determined in order to calculate exchange gain or loss. Present law rules are unclear regarding the allocation of remittances between previously taxed earnings and contributions to branch capital, or whether capital is fully recovered before exchange gain or loss is recognized.	(b)(1) A taxpayer's U.S. dollar basis in a branch would be recovered before exchange gain or loss on remittances in excess of current profits would be recognized. When recognized, exchange gain or loss on remittances would be domestic source.	(b)(1) Exchange gain or loss is recognized on remittances, determined by assuming remittances are made on pro rato basis out of prior years' earnings, and treated as separate basket foreign income or allocable thereto.	(b)(1) Same as House bill, except exchange gain or loss is sourced or allocated by reference to residence of the home office.

Item	Present Law	President's Proposal	House Bill	Senate Amendment
(2) Foreign corporations	(2) Dividends and related taxes are translated at current exchange rates.	(2) Same as present law	(2) Exchange gain or loss with respect to distributed earnings (based on appropriate rate to be determined under regulations for the year in which earned) would be treated as separate basket-foreign source income or allocable thereto	(2) Same as President's proposal
c. Calculation of foreign taxes eligible for credit				
(1) Direct taxes	(c)(1) Direct taxes are translated at rate in effect on date paid or accrued. Adjustments are translated at rate in effect on date of adjustment.	(c)(1) A redetermined foreign tax would be translated at exchange rate in effect on payment date	(c)(1) Present law is retained, except a refund is translated at exchange rate for date tax was originally paid, and other adjustments at rate on date of adjustment	(c)(1) Same as House bill, except adjustments (including refunds) are translated at same rate that applied to related income
(2) Indirect taxes	(2) Indirect taxes on actual distributions are translated at rate in effect on date related dividend is distributed. Indirect taxes on amounts deemed distributed under subpart F are translated at average rate for the year in which the subpart F income is earned.	(2) Same as present law	(2) Taxes are translated at rate in effect on date actually paid or accrued by foreign corporation. Adjustments are subject to same rules that apply for purposes of direct credit.	(2) Same as President's proposal
d. Rule when accrued taxes when paid differs from amounts claimed as credits	(d) If the amount of foreign taxes accrued differs from the amount paid, or if a foreign tax is refunded, the allowable credit is redetermined	(d) No provision.	(d) No provision.	(d) Determination of whether amount accrued differs from amount claimed as credit is made in the functional currency of payor
e. Regulatory authority	(e) No provision	(e) No provision.	(e) General regulatory authority.	(e) Express regulatory authority relating to procedures for taxpayers using net worth method under current law, limiting recognition of exchange loss on remittances, and hyperinflationary currencies
6. Effective date		*Effective date.*—Generally, for taxable years beginning on or after January 1, 1986. For transactions, the proposals would be effective for financial assets acquired or liabilities incurred after January 1, 1986.	*Effective date.*—Taxable years beginning after 1985	*Effective date.*—Generally for taxable years beginning after 1986

Item	Present Law	President's Proposal	House Bill	Senate Amendment
A. Overview of Permitted Types of Tax-Exempt Bonds (secs. 701-703 of the House bill and secs. 1501-1518 of the Senate amendment)	Interest on bonds issued by or on behalf of State and local governments the proceeds of which are to be used to finance government operations is tax-exempt.	Same as present law	Same as present law	Same as present law
	Interest on bonds which satisfy a private trade or business use and security interest test (industrial development bonds (IDBs)), or which are to be used to make loans to private persons (private loan bonds), are taxable unless a specific exemption is provided in the Code	Interest on bonds used by any nongovernmental person (including use of loan proceeds) would be taxable.	Interest on bonds which satisfy a private trade or business use test or which are to be used to finance loans to nongovernmental persons (nonessential function bonds) is taxable unless a specific exception is provided in the Code.	Interest on bonds which satisfy a private trade or business use and security interest test (IDBs), or which are to be used to finance loans to private persons (private loan bonds) is taxable unless a specific exception is provided in the Code
	Exceptions are provided permitting tax-exemption for interest on the following categories of bonds to finance private activities, discussed in C., below—	No exceptions would be provided for bonds to finance nongovernmental activities (including activities of section 501(c)(3) organizations) Instead, interest on nongovernmental bonds would be tax-exempt only where the nongovernmental use occurred solely because—	Exceptions are provided allowing tax-exemption for interest on the following categories of bonds for nongovernmental activities (nonessential function bonds) discussed in C., below—	Exceptions are provided permitting tax-exemption for interest on the following categories of bonds for nongovernmental activities, discussed in C., below—
	(1) Tax-exempt IDBs (including exempt-activity IDBs and small-issue IDBs).	(1) Bond-financed property was leased to a person other than a State or local government for an initial period not exceeding 1 year after its completion; or	(1) Exempt-facility, small-issue, and qualified redevelopment bonds (similar to tax-exempt IDBs under present law).	(1) Tax-exempt IDBs (including exempt-activity, small-issue, and qualified redevelopment IDBs),
	(2) Mortgage subsidy bonds	(2) Bond-financed property was operated by a person other than a State or local government pursuant to a management contract the term of which did not exceed 1 year	(2) Mortgage subsidy bonds	(2) Mortgage revenue bonds (formerly mortgage subsidy bonds),
	(3) Student loan bonds.		(3) Student loan bonds	(3) Student loan bonds,
	(4) Bonds the proceeds of which are used by section 501(c)(3) organizations.		(4) Qualified 501(c)(3) bonds	(4) Qualified 501(c)(3) bonds

Item	Present Law	President's Proposal	House Bill	Senate Amendment
B. General Restrictions on Tax Exemption	Subject to exceptions below, interest on State and local government bonds is taxable if—	Interest on State and local government bonds would be taxable if more than 1 percent of the bond proceeds were used by any person other than a State or local government unit	Subject to exceptions below, interest on State and local government bonds is taxable if—	Subject to exceptions below, interest on State and local government bonds is taxable if—
	(1) The bonds are *IDBs*, i.e.— (a) More than 25 percent of the bond proceeds is to be used in a trade or business of a person other than a State or local government or section 501(c)(3) organization (the "trade or business use" test), and	(1) No tax exemption for nongovernmental bonds	(1) The greater of 10 percent or more or $10 million of the bond proceeds is to be used in a trade or business of a person other than a State or local government.	(1) The bonds are IDBs, i.e.— (a) 25 percent or more of the bond proceeds is to be used in a trade or business of a person other than a State or local government or section 501(c)(3) organization, and
	(b) More than 25 percent of the principal or interest on the bonds is secured by or to be derived from property to be used in such a trade or business (the "security interest" test).			(b) 25 percent or more of the principal or interest on the bonds is secured by or to be derived from property to be used in such a trade or business (Clarifies that direct or indirect payments made by private person with respect to use of bond-financed property may satisfy the security interest test whether or not formally pledged.)

B. General Restrictions on Tax Exemption (cont.)				
	(2) The bonds are *private loan bonds*, i.e. 5 percent or more of the bond proceeds is to used to finance direct or indirect loans to persons other than a State or local government or section 501(c)(3) organization.	(2) No tax exemption for nongovernmental bonds.	(2) The greater of 5 percent or $5 million of the bond proceeds is to be used to make or finance direct or indirect loans to persons other than States and local governments.	(2) The bonds are *private loan bonds*, defined as under present law.
	The following exceptions to the private loan bond rule are provided:		The following exceptions to the private loan bond rule are provided:	The following exceptions to the private loan bond rule are provided
	(a) IDBs, mortgage subsidy bonds, or student loan bonds for which tax-exemption specifically is provided in the Code;		(a) Same as present law	(a) Same as House bill.
	(b) Excluded loans (i.e., loans (other than for use in a trade or business) to finance governmental taxes or assessments of a general nature and for an essential governmental function); and		(b) Excluded loans, defined as under present law (except expanded to include loans to persons engaged in a trade or business).	(b) Same as House bill

B. General Restrictions on Tax Exemption (cont.)	(c) Bonds issued as part of the Texas Veterans' Land Bond program and an Oregon energy conservation program (The exception for the Texas program is limited to bonds issued before March 15, 1987.)		(c) Bonds issued as part of the Texas Veterans' Land Bond Program (sunset date deleted) (permitted to be issued as nonessential function bonds).	(c) Same as present law except the sunset date on Texas Veterans' Land Bond Program is deleted (as in House bill) and an exception is added for the Iowa Industrial New Jobs Training Program, subject to a $100 million ceiling on outstanding bonds
	(3) *Related use requirement.*—Up to 25 percent of bond proceeds may be used in private trades or businesses, without the bonds being considered IDBs. There is no requirement that such use be related to governmental facilities also financed with the bonds.	(3) No tax-exemption for nongovernmental bonds	(3) *Related use requirement.*—Up to 10 percent or $10 million of bond proceeds may be used by nongovernmental persons. Use by nongovernmental persons, in excess of $1 million, is counted toward State volume limits for nongovernmental bonds (*see* C., below), but there is no related use requirement	(3) *Related use requirement.*—Private trade or business use of governmental bond proceeds equal to or exceeding 5 percent of bond proceeds must be related to governmental facilities also being financed with the bonds
	Concept of use.—Use of bond-financed property is treated as use of bond proceeds. Use of bond-financed property or services by the general public is not treated as a private use if the property or services are available to all members of the general public on the same basis. (For example, the fact that one industrial customer uses more than 25% of a sewer system serving the general public does not result in the bonds being IDBs). Management contracts, output contracts, take-or-pay contracts, and leases, as well as actual ownership of property, are examples of situations where all members of the general public do not use property or services on the same basis.	*Concept of use.*—Use of bond-financed property or services on the same basis by all members of the general public would be treated as nongovernmental (i.e., taxable) use; however, an exception would be provided allowing tax-exempt financing in such cases	*Concept of use.*—Same as present law	*Concept of use.*—Same as House bill
	Treatment of management contracts.—The determination of whether a management contract is treated as trade or business use is made on a facts and circumstances basis. The IRS has stated that, under certain specified conditions, it will issue an advance ruling that a facility managed by a private management company is *not* considered to be used in that company's trade or business. Such a ruling will be issued only if— (i) the management services are provided for a reasonable, periodic flat fee, under a contract not exceeding 5 years' duration (including renewal options), with the exempt owner having the option to cancel the contract, without penalty, at the end of any 2-year period, or (ii) in the case of certain newly operational facilities, compensation is based on a percentage of gross revenues from the facility, for a period which generally may not exceed one year	*Treatment of management contracts.*—Use pursuant to management contracts would be treated as nongovernmental if the term of the contract exceeded 1 year.	*Treatment of management contracts.*—Same as present law	*Treatment of management contracts.*—Same as House bill, except the IRS is directed to liberalize its advance ruling guidelines to provide that use pursuant to management contracts not exceeding 5 years is not treated as private trade or business use *as long as* (a) compensation is not based on a share of net profits, and (b) the exempt owner of the bond-financed facility has the option to cancel the contract, without penalty, at the end of any 3-year period

B General Restrictions on Tax Exemption (cont.)	*Certain volunteer fire departments*—Certain volunteer fire departments are treated as qualified issuers of tax-exempt bonds To qualify under (i) or (ii) above, the owner of the facilities and the management company must not be subject to common control, with allowances for *de minimis* cases (Rev Proc 82-14, 1982-1 C.B. 459). Similar principles are applied in determining whether advance rulings will be issued where bond-financed hospitals or similar facilities are used by nonexempt individuals other than employees (e g., use of public or private, charitable hospitals by private physicians) (Rev Proc 82-15, 1982-1 C B 460)	*Certain volunteer fire departments.*—No provision	*Certain volunteer fire departments.*—Deletes special provision, allows bonds as small-issue bonds. *Effective date.*—Bonds issued after December 31, 1985 *Exceptions*.—(1) Obligations with respect to facilities— (a) The original use of which commences with the taxpayer and the construction, reconstruction, or rehabilitation of which began before September 26, 1985, and was completed on or after that date, (b) The original use of which commences with the taxpayer and with respect to which a binding contract to incur significant expenditures was entered into before September 26, 1985, and part or all of such expenditures were incurred on or after that date, or (c) Acquired after September 25, 1985, pursuant to a binding contract entered into on or before that date Significant expenditures are defined as expenditures in excess of 10% of the estimated cost of the facility Facilities eligible for the exception are defined as property for which bond financing was approved by a governmental unit (or by voter referendum) before September 26, 1985 (2) Current refundings of bonds (a) that were issued before January 1, 1986 (including a series of refundings); (b) that are governmental bonds under present law; and (c) that may not be originally issued under the House bill, if— (i) The amount of the refunding bonds does not exceed the outstanding amount of the refunded bonds, and (ii) The refunding bonds (or series of refundings) do not have a maturity date later than the date which is the later of (a) 120% of the reasonably expected economic life of the property identified as being financed with the original (refunded) bonds when issued, or (b) 17 years after issuance of the original bonds.	*Certain volunteer fire departments*—Retains present law *Effective date.*—Bonds issued after the date of enactment *Exceptions*.—(1) Same as House bill, except substitutes March 1, 1986, for September 25, 1985, and substitutes March 2, 1986, for September 26, 1985. (2) Same as House bill, except substitutes date of enactment for January 1, 1986

Item	Present Law	President's Proposal	House Bill	Senate Amendment
Tax-Exempt Bonds for Certain Nongovernmental Activities 1. Industrial development bonds *a. Exempt-activity IDBs*	(a) Exempt-activity IDBs are bonds the proceeds of which are to be used to finance—	(a) The President's proposal includes no exceptions to the governmental use requirement based on the activity being financed	(a) Present law is modified to permit interest on limited amounts of nonessential function (i.e., nongovernmental) bonds to continue to be tax-exempt if bond proceeds are used to finance the following exempt facilities—	(a) Exempt-activity IDBs are available to finance—
	(i) *Multifamily rental housing*	(i) No tax exemption;	(i) *Multifamily rental housing*—	(i) *Multifamily rental housing*—
	(A) At least 20 percent (15 percent in targeted areas) of the housing units must be occupied by persons whose income does not exceed 80 percent of the area median income when they first occupy the unit; and		(A) One of the following set-aside requirements is satisfied on a continuous basis (1) At least 25 percent of the housing units are occupied by persons whose income does not exceed 80 percent of the area median income, or (2) At least 20 percent of the housing units are occupied by persons whose income does not exceed 70 percent of the area median income Treasury Department is required to make annual reports on compliance with (A). If noncompliance with (A) is not corrected after it reasonably should have been discovered, interest on bond financing is nondeductible to project owner from first day of year in which noncompliance commenced until correction occurred	(A) Same as House bill;
	(B) Must be used as rental housing for a "qualified project period," generally 10 years or 50 percent of the term of the bonds with the longest maturity;		(B) Must be used for rental housing for a "qualified project period," generally the longer of 15 years or the date on which bonds are no longer outstanding with respect to the project,	(B) Same as House bill, except the qualified project period would last for a minimum of 12 years;
	(C) No provision.		(C) Operator of project must certify to Treasury annually that project currently is in compliance with Code requirements;	(C) Same as House bill,
	(D) No provision		(D) Existing low-income tenants continue to be counted as such unless their incomes increase to an amount in excess of 120% of the applicable low-income ceiling	(D) Same as House bill,
	(E) No provision		(E) If a project ceases to comply with the low-income set-aside because existing tenant incomes increase, no penalties are imposed if each available unit after the noncompliance occurs is rented to a new low-income tenant until the project again is in compliance;	(E) Same as House bill, except the requirement that available units be rented to new low-income tenants applies only to available units of comparable or smaller size than those occupied by the tenants whose income has increased;
	(F) No provision		(F) No provision, and	(F) A special rule is provided for projects charging significantly lower than market rents to low-income tenants and that elect to satisfy a stricter low-income set-aside requirement. Under this rule— (1) Low-income tenants continue to qualify as such, as long as their income

Tax-Exempt Bonds for Certain Nongovernmental Activities 1. Industrial development bonds a. *Exempt-activity IDBs (cont.)*				does not exceed 150% of the applicable low-income ceiling, and (2) If the project ceases to comply with the low-income set-aside because existing tenant incomes increase, no penalties are imposed if each available low-income unit after the noncompliance occurs is rented to tenants having 50% or less of area median income until the project again is in compliance; and
	(G) Proposed Treasury regulations require that the determination of low- or moderate-income be made with adjustments for family size, for bonds issued after 1985.		(G) Clarification is made that the determination for low- or moderate-income be made with adjustments for family size	(G) Same as House bill
	(ii) *Sports facilities;*	(ii) No tax exemption,	(ii) Same as President's proposal;	(ii) Same as President's proposal and House bill;
	(iii) *Convention or trade show facilities,*	(iii) No tax exemption;	(iii) Same as President's proposal;	(iii) Same as President's proposal and House bill,
	(iv) *Airports,* defined to include runways, terminals, and other public facilities, as well as certain airport hotels and commercial facilities, hangars for one or more airlines, other property not available for use by the general public, and related storage and training facilities.	(iv) No tax exemption;	(iv) *Airports,* defined as ground facilities directly related to the transportation by air of passengers and cargo (includes runways, air traffic control towers, terminal facilities, public parking, and airline hangers, but not airport hotels, food preparation facilities, and shops);	(iv) *Airports,* defined as under present law, except that tax-exempt financing is not available for hotels;
	(v) *Docks and wharves* and related storage and training facilities;	(v) No tax exemption;	(v) *Dock and wharf facilities* directly related to the transportation of passengers and cargo by water (excludes storage warehouses used other than in immediate transportation of goods);	(v) *Dock and wharf facilities,* defined as under present law;
	(vi) *Mass commuting facilities* and related storage and training facilities;	(vi) No tax exemption;	(vi) *Mass commuting facilities,* defined generally as under present law;	(vi) Same as President's proposal,
	(vii) *Parking facilities;*	(vii) No tax exemption;	(vii) Same as President's proposal;	(vii) Same as President's proposal and House bill;
	(viii) *Sewage disposal facilities,*	(viii) No tax exemption;	(viii) *Sewage disposal facilities,* defined generally as under present law;	(viii) *Sewage disposal facilities,* defined as under present law;
	(ix) *Solid waste disposal facilities.*	(ix) No tax exemption;	(ix) *Solid waste disposal facilities,* defined generally as under present law (includes repeal of targeted exemption for certain alcohol and steam facilities);	(ix) *Solid waste disposal facilities,* defined as under present law;
	(x) *Electric energy and gas furnishing facilities* serving areas not exceeding 2 contiguous counties or a city and one contiguous county;	(x) No tax exemption;	(x) Same as President's proposal;	(x) *Electric energy and gas-furnishing facilities,* defined as under present law;
	(xi) *Facilities for the furnishing of water* (including irrigation systems);	(xi) No tax exemption;	(xi) *Facilities for the furnishing of water,* defined generally as under present law except excluding irrigation systems;	(xi) *Facilities for the furnishing of water,* defined as under present law (including irrigation systems);
	(xii) *Certain hydroelectric generating facilities* (expired generally after December 31, 1985);	(xii) No tax exemption;	(xii) Same as President's proposal;	(xii) Same as President's proposal and House bill, except retains transition rule included in present-law sunset date.

a. Exempt-activity IDBs (cont.)				
	(xiii) *Local district heating or cooling facilities,*	(xiii) No tax exemption;	(xiii) Same as President's proposal,	(xiii) *Local district heating and cooling facilities,* defined as under present law.
	(xiv) *Air or water pollution control facilities, and*	(xiv) No tax exemption; and	(xiv) Same as President's proposal; and	(xiv) Same as President's proposal and House bill; and
	(xv) No tax-exemption	(xv) No tax exemption	(xv) Same as President's proposal;	(xv) *Hazardous waste treatment facilities,* as defined under sec. 1004 of the Solid Waste Disposal Act. (Facilities subject to permitting requirements under the Resource Conservation and Recovery Act (RCRA) generally qualify for financing.)
			Effective date.—Bonds issued after December 31, 1985. Transitional exceptions similar to those described in item B., above	*Effective date.*—Bonds issued after date of enactment. Transitional exceptions similar to those described in item B., above.
b. Miscellaneous restrictions on exempt-activity IDBs				
i. Use of bond proceeds for activity qualifying for tax-exempt financing	(b)(i)(A) Only 90 percent of IDB proceeds are required to be used for purpose of bond issue; the remaining 10 percent may be used for any purpose	(b)(i) No tax exemption for nongovernmental bonds	(b)(i)(A) All proceeds of nonessential function bonds for exempt facilities (other than costs of issuance and proceeds invested in a reasonably required debt service reserve fund) are required to be used for the activity qualifying the interest on the bonds for tax exemption	(b)(i)(A) Same as House bill, except 95 percent of IDB proceeds required to be used for purpose of issue rather than all proceeds
	(B) In the case of exempt-activity IDBs, all property that is "functionally related and subordinate to" the exempt activity may be financed with bond proceeds and counts toward satisfaction of the 90 percent requirement.		(B) Eliminates functionally related and subordinate test. *Effective date.*—Bonds issued after December 31, 1985.	(B) No provision. *Effective date.*—Bonds issued after date of enactment
ii. Ownership of property financed with nongovernmental bonds for exempt facilities	(ii) Property financed with IDB proceeds may be owned by persons other than State or local governmental units.	(ii) No tax exemption for nongovernmental bonds.	(ii) Airports, docks and wharves, and mass commuting facilities are required to be governmentally owned, determined using general Federal income tax rules. *Effective date.*—Bonds issued after December 31, 1985. Transitional exceptions similar to those provided for exempt-facility bonds (item B., above).	(ii) No provision.
c. Industrial park IDBs	(c) Interest is tax-exempt on IDBs to be used to finance acquisition or development of land as a site for an industrial park	(c) No tax exemption for nongovernmental bonds.	(c) Same as President's proposal. *Effective date.*—Bonds issued after December 31, 1985. Transitional exceptions similar to those described in item B., above	(c) Same as President's proposal and House bill. *Effective date.*—Bonds issued after date of enactment. Transitional exceptions similar to those described in item B., above.

d. Small-issue IDBs	(d) Interest on small-issue IDBs is tax exempt. Small-issue IDBs are issues not exceeding $1 million, the proceeds of which generally may be used to finance land or any depreciable property. The $1 million size limitation is increased to $10 million if an election is made to take certain capital expenditures into account. Ninety percent of small-issue bonds must be used for the purpose of the borrowing (i.e., 10 percent may be used for any purpose). A special rule allows small-issue IDBs to be used for first-time farmers to finance the purchase of farmland and for a *de minimis* amount of used equipment acquired in conjunction with the purchase of farmland by such farmers. No special restrictions are imposed with respect to bonds to finance depreciable farm property. This exception expires generally after December 31, 1986 (December 31, 1988, in the case of bonds to finance manufacturing facilities).	(d) No tax exemption for nongovernmental bonds.	(d) Generally, the same as present law, except (i) Scheduled sunset dates are deleted, (ii) All bond proceeds (other than costs of issuance and proceeds invested in a reasonably required debt service reserve fund) are required to be used for purpose of borrowing (iii) No provision (iv) No provision *Effective date.*—Bonds issued after December 31, 1985	(d) Same as House bill, except (i) Retains present law sunset dates, and bonds for first time farmers are treated as bonds for manufacturing facilities (and hence may be issued through December 31, 1988); (ii) Same as House bill, except 95 percent of bond proceeds must be used for purpose of borrowing rather than all proceeds (iii) The first-time farmer exception is expanded (*A*) to include farmers who qualify at the time of purchase except for prior ownership of land disposed of while insolvent, and (*B*) to increase the amount of used equipment that may be financed to 25% of the financing provided to a qualifying farmer; (iv) A $250,000 lifetime limit is imposed on the amount of depreciable farm property (including new and used property) for any principal user or related persons (Bonds issued prior to the effective date are not affected but count in determining the tax-exemption of any post-enactment issues.) *Effective date.*—Bonds issued after date of enactment, except the $250,000 limit on depreciable property used in farming (item (iv), above) is effective for bonds issued after April 17, 1986.
2. Student loan bonds	Tax-exemption is permitted for interest on student loan bonds issued in connection with the Department of Education's GSL and PLUS programs. Tax-exemption is not permitted for other student loan bonds (e.g., supplemental student loan bonds).	No tax exemption for nongovernmental bonds.	Same as present law except expanded to include certain non-GSL student loan bonds and all bond proceeds (other than costs of issuance and amounts invested in a reasonably required debt service reserve fund) required to be used to finance student loans. *Effective date.*—Bonds issued after December 31, 1985	Same as House bill, except 85% of bond proceeds must be used to make student loans. *Effective date.*—Bonds issued after date of enactment.

Item	Present Law	President's Proposal	House Bill	Senate Amendment
3. Mortgage subsidy bonds				
a. Qualified mortgage bonds and mortgage credit certificates	(a)(1) Qualified mortgage bonds must be used to finance mortgages on single-family, owner-occupied residences The targeting requirements for these bonds include the following: (i) At least 90 percent (0 percent in targeted areas) of the lendable proceeds of each issue must be used to finance loans to first-time homebuyers; (ii) The purchase price of bond-financed residences may not exceed 110 percent (120 percent in targeted areas) of the average area purchase price applicable to that residence; and (iii) Issuers must publish and submit to the Treasury annual reports of their policies on the use of bond proceeds	(a)(i) No tax exemption for nongovernmental bonds.	(a)(1) Same as present law except— (i) All bond proceeds (50% in targeted areas) other than issuance costs and amounts invested in reasonably required debt service reserve fund are required to be used to finance residences for first-time homebuyers; (ii) The purchase price of bond-financed residences may not exceed 90 percent (110 percent in targeted areas) of the average area purchase price applicable to that residence; (iii) Present-law requirement of annual Treasury reports is deleted; and (iv) At least 50 percent of the mortgage financing is required to be provided to borrowers whose family income does not exceed 90 percent of higher of area or Statewide median income and all such financing is required to be provided to borrowers whose income does not exceed 115 percent of area median income. In targeted areas, ½ of the financing could be provided to borrowers without regard to the above income limits; the balance of the financing must be provided to mortgagors having incomes not exceeding 140 percent of the higher of area or Statewide median income.	(a)(1) No provision, except mortgage subsidy bonds are renamed mortgage revenue bonds.
	(2) Issuers of qualified mortgage bonds may elect to exchange part or all of their bond authority for authority to issue Mortgage Credit Certificates (MCCs). The aggregate principal amount of MCCs may not exceed 20 percent of the exchanged bond authority MCCs generally are subject to the same targeting requirements as qualified mortgage bonds	(2) The MCC option would be repealed along with authority to issue qualified mortgage bonds.	(2) Authority to issue MCCs is continued The targeting requirements for MCCs are conformed to the revised targeting rules for qualified mortgage bonds	(2) Same as present law, except increases trade-in rate from 20 percent to 25 percent
	(3) Authority to issue both qualified mortgage bonds and MCCs terminates after December 31, 1987.		(3) Same as present law *Effective date.*—Bonds issued and MCCs issued with respect to bond authority exchanged after December 31, 1985. (Does not apply to mortgage loans made with the proceeds of bonds issued before January 1, 1986.)	(3) Same as House bill *Effective date.* Bonds issued after date of enactment, and exchanged bond authority for calendar years beginning after 1986

Item	Present Law	President's Proposal	House Bill	Senate Amendment
a. Qualified mortgage bonds and mortgage credit certificates (cont.)				
	(4) Tenant-shareholders of cooperative housing corporations are allowed a deduction for rents paid to the cooperative equal to their allocable share of interest and taxes paid by the cooperative. Cooperative housing corporations are eligible to use tax-exempt financing under the rules applicable to owner-occupied housing (i.e., qualified mortgage bonds).	(4) No tax exemption for nongovernmental bonds.	(4) No provision	(4) Limited equity cooperative housing corporations may elect to be eligible for tax exempt financing under the rules applicable to multi-family residential rental property (as modified by the amendment). If such an election is made— (1) The tenant-shareholders of the cooperative are not entitled to a deduction for interest and taxes paid by the cooperative (under sec. 216), and (2) The volume of such bonds counts toward the State ceiling applicable to qualified mortgage bonds. Bonds for limited equity cooperative housing are subject to the December 31, 1987, sunset date for qualified mortgage bonds. *Effective date.*—Bonds issued after date of enactment.
b. Qualified veterans' mortgage bonds	(b) Qualified veterans' mortgage bonds are bonds 90% or more of the proceeds of which are used to finance loans to veterans for the purchase of single-family, owner-occupied residences. Tax-exempt qualified veterans' mortgage bonds may be issued only by the five States that issued such bonds before June 22, 1984. Mortgage loans financed with those bonds may be made only to veterans who served on active duty before 1977 and who apply for a loan before 30 years after leaving active service.	(b) No tax exemption for nongovernmental bonds.	(b) Same as present law, except consistent with rules for other nongovernmental bonds, all bond proceeds (other than issuance costs and amounts deposited in a reasonably required debt service reserve fund) are required to be used for mortgage loans to qualified veterans. *Effective date.*—Bonds issued after December 31, 1985.	(b) Same as present law.
1. Tax-exempt bonds for section 501(c)(3) organizations	Interest on bonds for nonprofit organizations described in Code section 501(c)(3) generally is tax-exempt. Bonds the proceeds of which are to be used by these organizations generally are subject to similar requirements to those for bonds for general government operations.	No tax exemption for nongovernmental bonds.	Tax-exempt bonds for section 501(c)(3) organizations are permitted, as follows: (a) Only activities directly related to the exempt purpose of the organization may be financed and all bond proceeds (other than costs of issuance and proceeds invested in a reasonably required debt service reserve fund) are required to be used for such activities.	Tax-exempt bonds for section 501(c)(3) organizations are permitted, as follows: (a) Same as House bill, except 95% of proceeds is required to be used for qualified activities.

Item	Present Law	President's Proposal	House Bill	Senate Amendment
4. Tax-exempt bonds for section 501(c)(3) organizations (cont.)				
			(b) In the case of section 501(c)(3) organizations other than hospitals, the aggregate amount of outstanding bonds of which each organization is a beneficiary may not exceed $150 million. (Generally, rules of the present $40 million limitation on beneficiaries of IDB-financing are applied under this provision); and	(b) No provision
			(c) All property financed with proceeds of these bonds is required to be owned by a section 501(c)(3) organization or governmental unit (using Federal income tax concepts of ownership)	(c) Same as House bill
			Effective date.—Bonds issued after December 31, 1985. Transitional exception for item (c), similar to those provided for exempt-facility bonds (item 1.a., above).	*Effective date.*—Bonds issued after date of enactment
5. Qualified redevelopment bonds	No specific provision, but bonds violating IDB or private loan bond restrictions are taxable	No tax exemption for nongovernmental bonds	Treats bonds to finance certain land acquisition and redevelopment in blighted areas, for ultimate use by nongovernmental persons, as tax-exempt nonessential function bonds	Treats bonds to finance certain land acquisition and redevelopment in blighted areas, and for use by nongovernmental persons, as tax-exempt IDBs
a. General rule			(a) Qualified redevelopment bonds must be part of an issue: (i) All proceeds (other than costs of issuance and proceeds deposited in a reasonably required reserve fund) of which are used for redevelopment purposes in a locally designated blighted area, and (ii) With respect to which incremental property tax revenues (i.e., additional tax revenues attributable to increased property values by reason of bond-financed redevelopment) are reserved exclusively for debt service on the issue, to the extent necessary to cover such debt service Real property taxes in the designated area must be imposed at the same rate and in the same manner as for similar property located elsewhere in the jurisdiction. No additional fees or charges may be imposed in the designated area that are not imposed on other similar property elsewhere in the jurisdiction	(a) Same as House bill, except 95 percent of proceeds are required to be used for redevelopment purposes in a locally designated blighted area

Item	Present Law	President's Proposal	House Bill	Senate Amendment
5. Qualified redevelopment bonds *(cont.)*				
b. Uses of bond proceeds			(b)(1) The proceeds of qualified redevelopment bonds must be used for the following purposes.	(b)(1) The proceeds of qualified redevelopment IDBs must be used for the following purposes
			(i) To acquire by eminent domain or the threat thereof, clear, and prepare land in a designated blighted area for redevelopment, and transfer real property interests to nongovernmental persons for fair market value;	(i) Same as House bill, but clarifies that "fair market value" reflects covenants and restrictions relating to the use of the real property, and provides that actual threat of eminent domain is not required if acquiring agency has power of eminent domain and acquisition of property is one with respect to which power may be exercised;
			(ii) To rehabilitate the real property (acquired as above); and	(ii) Same as House bill, and
			(iii) To relocate occupants of structures on the acquired real property.	(iii) Same as House bill
			(2) Qualified redevelopment bond proceeds may not be used to construct buildings or other new structures for use by nongovernmental persons on the bond-financed property	(2) Same as House bill
c. Designation of blighted areas			(c)(1) Qualified redevelopment bonds may be issued only pursuant to— (i) a State law that authorizes the issuance of such bonds for permitted purposes in blighted areas, and (ii) a redevelopment plan adopted (before issuance of the bonds) by the governing body of the general purpose local governmental unit having jurisdiction over the blighted area	(c)(1) Same as House bill
			(2) Designation of blighted areas must be made by the general purpose local governmental unit having jurisdiction over the area and must be based on prescribed State statutory criteria.	(2) Same as House bill
			(3) The aggregate blighted areas designated by a local governmental unit may not contain real property, the assessed value of which is more than 10 percent of the assessed value of all real property within its jurisdiction	(3) Same as House bill, but increases limit to 25 percent
			(4) A designated blighted area must be larger than a contiguous ¼-square mile (160 acres).	(4) A designated blighted area may not be smaller than 10 contiguous acres

Item	Present Law	President's Proposal	House Bill	Senate Amendment
5. Qualified redevelopment bonds *(cont.)*				
d. Application of IDB limitations			(d)(1) Qualified redevelopment bonds are subject to the volume and other limitations applicable to nonessential function bonds, except the limitation on use of bond proceeds to finance nonagricultural land.	(d)(1) Qualified redevelopment bonds are IDBs and hence subject to all IDB restrictions, including the volume limitation for IDBs and student loan bonds. An exception is provided from the limitation on the use of bond proceeds to finance nonagricultural land (Floor amendment by Senator Baucus, adopted by voice vote.)
			(2) Owner-occupied housing rehabilitated with qualified redevelopment bond proceeds, or constructed on bond-financed land, is permitted only if— (i) the first purchaser of each residence reasonably expects it to be his or her principal residence, and (ii) the residence satisfies the purchase price limitation which would apply for qualified mortgage bonds in the same location.	(2) No provision.
			(3) Residential rental housing rehabilitated with qualified redevelopment bond proceeds, or constructed on bond-financed land, must satisfy all Code targeting requirements applicable to bond-financed multifamily residential rental housing, throughout the qualified project period as defined for bond purposes.	(3) No provision.
			(4) Facilities that may not be financed with exempt-facility bonds (including airplanes, skyboxes, health clubs, gambling facilities, and liquor stores), or the financing of which is restricted with respect to small-issue bonds (including retail food and beverage establishments, automobile sales and service, and various recreation and entertainment facilities) may not be located on land financed with qualified redevelopment bonds.	(4)(a) Except as provided in (b) up to 25 percent of bond proceeds may be used for facilities with respect to which IDB financing is restricted or for land on which such facilities are to be located. (b) The following facilities may not be financed with redevelopment bonds or located on land financed with such bonds: (i) Private or commercial golf courses; (ii) Country clubs, (iii) Massage parlors, hot tub facilities, or suntan facilities, and (iv) Racetracks and other facilities primarily used for gambling.

Item	Present Law	President's Proposal	House Bill	Senate Amendment
6. Miscellaneous restrictions on tax exempt bonds				
a. Restriction on maturity of nongovernmental bonds	(a) The weighted average maturity of IDBs may not exceed 120 percent of the reasonably expected economic life of the bond-financed property	(a) No tax exemption for nongovernmental bonds	(a) Extends present law restriction to all nonessential function bonds (other than mortgage subsidy bonds and student loan bonds) *Effective date.*—Bonds issued after December 31, 1985	(a) Extends present law restriction to section 501(c)(3) organization bonds, with an exception for mortgage loans insured under certain FHA programs In the case of certain pooled issues for multiple section 501(c)(3) organizations, the rule would be applied on a loan-by-loan (rather than a property by property) basis *Effective date.*—Bonds issued after date of enactment
b. Acquisition of land and existing property and prohibition on financing certain facilities	(b) Interest on IDBs generally is taxable if more than 25 percent of the proceeds of an issue is used for land. Acquisition of existing property may not be financed with tax-exempt IDBs unless a rehabilitation requirement is satisfied Luxury boxes and certain other facilities may not be financed with tax-exempt bonds.	(b) No tax exemption for nongovernmental bonds.	(b) Extends present-law restrictions to all nonessential function bonds (other than mortgage subsidy bonds and student loan bonds) *Effective date.*—Bonds issued after December 31, 1985. Transitional exceptions (for bonds not presently subject to these limitations) similar to those described in item C.1.a., above.	(b) No provision
c. Public approval requirement	(c) IDBs may be issued only after the issuer holds a public hearing and the bonds are approved by an elected official. Alternatively, issuance of the bonds may be approved by a voter referendum	(c) No tax exemption for nongovernmental bonds	(c) Extends present IDB requirements to all nonessential function bonds *Effective date.*—Bonds issued after December 31, 1985	(c) No provision
d. Change in use of nongovernmental bond-financed property	(d) Tax exempt bonds generally are not required to be redeemed if the use of bond-financed property changes from a use qualifying interest on the bonds for tax-exemption to a nonqualified use	(d) No tax exemption for nongovernmental bonds	(d) A change in use of property financed with nonessential function bonds, to a use not qualifying for tax-exempt financing, generally results in loss of income tax deductions for rent, interest, or equivalent amounts paid by the person using the property in the nonqualifying use. Section 501(c)(3) organizations realize unrelated business income with respect to such use. These consequences apply in addition to any loss of tax exemption on bond interest provided under present law. *Effective date.*—Changes in use occurring after December 31, 1985, with respect to financing provided (by loan, lease, or other arrangement) after that date	(d) Same as House bill *Effective date.*—Changes in use occurring after date of enactment, with respect to financing provided (by loan, lease, or other arrangement) after that date

Item	Present Law	President's Proposal	House Bill	Senate Amendment
D. Volume Limitations on Nongovernmental Bonds	*Volume Limitations* Three separate sets of volume limitations are imposed under present law with respect to certain types of nongovernmental bonds. *(1) Limitation on student loan bonds and most IDBs*	No tax exemption for nongovernmental bonds	*Unified Volume Limitation* A single volume limitation is imposed with respect to the following bonds issued by States and local issuers therein— (1) All nonessential function bonds with respect to which tax-exemption is permitted (except certain airport and port bonds, discussed below); and (2) The portion of a governmental bond issue in excess of $1 million that is used by persons other than a State or local government	*Volume Limitations* Three separate sets of volume limitations are imposed in a manner similar to present law— *(1) Limitation on student loan bonds and most IDBs* Same as present law, including the reduction to $100 per capita after 1986. (Hazardous waste and qualified redevelopment bonds are subject to this volume limitation, together with student loan bonds and other IDBs (subject to the exceptions below).)
	Aggregate volume.—The amount of student loan bonds and most IDBs that may be issued within a State during any calendar year is limited to the greater of $150 for each resident of the State or $200 million. The $150 per capita limitation is scheduled to be reduced to $100 after 1986.		*Aggregate volume*.—The annual volume of tax-exempt nonessential function bonds (including the nonessential portion of governmental bonds, discussed in (2), above) issued by each State and local issuers therein may not exceed the greater of $175 per resident of the State or $200 million. This per capita limitation is reduced to $125 per resident after 1987 to reflect the present-law scheduled sunset of tax exemption for qualified mortgage bonds. Current refunding bonds are not subject to the volume limitation to the extent the amount of the refunding bonds does not exceed the amount of outstanding refunded bonds and the bonds do not have a maturity date after expiration of 120% of the reasonably expected economic life of the bond-financed property (17 years for nonfacility bonda and 32 years for tax-exempt mortgage subsidy bonds).	
	Allocation rates.—Each State's volume limitation is allocated one-half to State issuers and one-half to localities within the State on the basis of relative populations unless the State adopts a statute providing a different allocation. Governors of each State are permitted to issue proclamations overriding the Federal rules during an interim period before State legislatures meet. Each person allocating bond authority must certify that the allocation is not made in consideration of any bribe, gift, or campaign contribution. (A special allocation rule applies for States having constitutional home rule cities.)		*Allocation rules*.—Each State's volume limitation is allocated one-half to State issuers and one-half to local issuers within the State on the basis of relative populations unless the State adopts a statute providing a different allocation. Governors of each State are permitted to issue proclamations overriding the Federal allocation rules, effective during an interim period until the end of the year in which the State legislature next meets in regular session. The present-law required certification by persons allocating bond authority is repealed. Other administrative provisions of the present IDB volume limitation (including the rules for determining the location of property receiving volume allocations, and the special rule for States having constitutional home rule cities) apply under the new volume limitation.	

Item	Present Law	President's Proposal	House Bill	Senate Amendment
D. Volume Limitations on Nongovernmental Bonds (cont.)	*Carryforward of bond authority.*—Bond issuers may elect to carry forward unused bond authority (for up to three years generally) for specific, identified exempt-activity IDB projects, or for the general purpose of issuing student loan bonds. Carryforward elections are not permitted for small-issue IDBs.		*Carryforward of bond authority.*—Bond issuers may elect to carry forward unused bond authority for up to three years for specific, identified projects and for the general purpose of issuing either (a) qualified mortgage bonds, (b) qualified veterans' mortgage bonds, or (c) student loan bonds. Carryforward elections are not permitted for small-issue bonds. *Permanent set-aside for section 501(c)(3) organization bonds.*—An annual amount equal to $25 per capita ($30 million for States having a $200 million limit) is set-aside permanently for qualified 501(c)(3) bonds. *Protection of qualified redevelopment bonds.*—Unless overridden by a State statute, at least $6 per capita ($8 million for States using the $200 million limit) must be set-aside for qualified redevelopment bonds in States that issued more than $25 million in tax-increment financing bonds between July 18, 1984, and January 1, 1986.	
	(2) Qualified mortgage bonds *Aggregate volume.*—The annual volume of qualified veterans' bonds that may be issued within a State is limited to the greater of (1) 9 percent of the average annual aggregate principal amount of mortgages executed during the three preceding years for single-family, owner-occupied residences located in the State, or (2) $200 million. *Allocation rules.*—Qualified mortgage bond authority is allocated among issuers in each State pursuant to rules like those applicable to student loan bonds and most IDBs. *Carryforward of bond authority.*—States may not carry forward unused qualified mortgage bond authority.		*Protection of housing bonds.*—Unless overridden by a State statute, at least 50% (reduced to 25% after 1987 to reflect the sunset of authority to issue qualified mortgage bonds) of each State's annual unified volume limitation is required to be used for— (i) multifamily rental housing bonds; (ii) qualified mortgage bonds; or (iii) qualified veterans' mortgage bonds. At least ⅓ of the housing portion must be used for multifamily housing and ⅓ for single-family housing, unless otherwise provided by the governor or a State statute.	*(2) Qualified mortgage bonds* Same as present law.
	(3) Qualified veterans' mortgage bonds *Aggregate volume.*—The five States permitted to issue qualified veterans' mortgage bonds are subject to volume limitations based on the volume in which they issued bonds during the period beginning on January 1, 1979, and ending on June 22, 1984. *Allocation rules.*—Qualified veterans' mortgage bonds are general obligation bonds of the issuing State. This bond authority is not allocated to any local governmental issuers. *Carryforward of bond authority.*—States may not carry forward unused qualified veterans' mortgage bond authority.			*(3) Qualified veterans' mortgage bonds* Same as present law.

Item	Present Law	President's Proposal	House Bill	Senate Amendment
D. Volume Limitations on Nongovernmental Bonds (cont.)	*Nongovernmental Bonds Not Subject to Volume Limitations* No volume limitations are imposed with respect to nongovernmental bonds the proceeds of which are to be used— (1) By section 501(c)(3) organizations (2) For multifamily rental housing (3) For governmentally owned airports, docks and wharves, mass commuting facilities, convention centers, and trade show facilities. For purposes of item (3), above, facilities are treated as governmentally owned if the lessee (if any) makes an irrevocable election not to claim depreciation on or investment tax credit with respect to the facility.		*Nonessential Function Bonds Not Subject to Volume Limitations* No volume limitations are imposed with respect to: (1) Bonds to finance airports (other than cargo handling facilities), and (2) Bonds to finance port facilities (other than storage facilities) (Tax-exempt financing for these facilities is not permitted unless the facilities are governmentally owned, determined by reference to general income tax concepts of ownership.) (*See*, item C.1.b ii, above.) (*See*, item B, above.)	*IDBs, etc. Not Subject to Volume Limitations* No volume limitations are imposed with respect to (1) Qualified 501(c)(3) bonds, (2) Bonds for multifamily rental housing, (3) Bonds for airports, docks and wharves, and sewage, solid waste disposal, and water-furnishing facilities, if the bond-financed property is governmentally owned Under a "safe harbor" rule, facilities described in (3), above, are treated as governmentally owned for purposes of this provision if— (i) the lessee (including a user pursuant to a management contract or similar agreement) makes an irrevocable election not to claim depreciation or an investment tax credit with respect to the facility, (ii) the term of any lease, management contract, or similar arrangement does not exceed 80% of the reasonably expected economic life of the property, and (iii) the lessee, etc. does not have an option to purchase the facility other than at fair market value The requirements of (ii) and (iii) above do not apply to bonds for solid waste disposal facilities.
			Effective date.—Bonds issued after December 31, 1985.	*Effective date.*—Bonds issued after date of enactment
			Transitional exceptions similar to those described in item B., above, are provided for: (1) Bonds presently allowed to be issued outside State volume limitations that are subject to the new unified limitation under the bill (2) Bonds presently subject to State volume limitations that also are subject to the new unified limitation if (a) the bonds are issued pursuant to a carryforward election allowed under the current private activity bond volume limitation filed before October 31, 1985, and (b) the bonds are issued with respect to facilities satisfying transitional exceptions similar to those described in item B., above	(1) Transitional exceptions similar to those described in item B., above, are provided for bonds presently allowed to be issued outside State volume limitations that are subject to such limitations under the amendment

E. Arbitrage Restrictions **1. Profit limitations and determination of bond yield**	Present law includes three sets of arbitrage restrictions applicable to tax-exempt bonds	The present-law arbitrage rules would be modified as follows.	The present-law arbitrage rules are modified, as follows:	The present law arbitrage rules are modified as follows
	General restrictions applicable to all tax-exempt bonds *Profit limitations.*—If bond proceeds are reasonably expected to be invested in securities (other than tax-exempt bonds) having a yield that is materially higher than the yield on the bonds, bond interest is taxable. The amount of permitted arbitrage earnings depends on whether the bond proceeds are invested in obligations related to the purpose of the borrowing or in other, nonpurpose obligations, and whether the issuer elects to earn unlimited arbitrage profits for certain temporary periods	*General restrictions applicable to all tax-exempt bonds* *Profit limitations.*—(a) Clarification would be provided that the reasonable expectations test does not protect intentional acts to create arbitrage occurring after the bonds are issued	*General restrictions applicable to all tax exempt bonds* *Profit limitations.*—(a) Same as President's proposal except the restriction on investment in higher yielding obligations also is expanded to include investments in annuity contracts and other property held for investment (This rule ensures that purchase of 3rd party contracts to fund deferred payment arrangements are subject to yield restrictions in the same manner as direct funding of these arrangements.)	*General restrictions applicable to all tax exempt bonds* *Profit limitations* —Same as House bill
		(b) The right to elect to earn higher arbitrage profits over the entire term of the bonds by foregoing a temporary period when unlimited arbitrage is permitted would be repealed	(b) Same as President's proposal.	(b) Same as President's proposal and House bill
	Exceptions.—(a) Investments during a temporary period prior to use for the purpose of the borrowing. (Generally, this temporary period may not exceed 3 years.)	*Exceptions.*—(a) Temporary periods during which unlimited arbitrage is permitted would be restricted as follows: (1) No temporary period would be permitted for bond issues to finance acquisitions; and (2) For construction projects, the temporary period would end on the earlier of the date— (A) The project was substantially completed; (B) An amount equal to bond proceeds had been spent on the project, or (C) Three years after the earlier of the date the bonds were issued or the date construction on the project began	*Exceptions.*—(a) Same as President's proposal except the temporary period for bonds used to finance acquisitions is 30 days	*Exceptions.*—(a) No provision
	(b) Investments not exceeding a minor portion (15%) of bond proceeds in materially higher yielding obligations. (A reasonably required debt service reserve fund is the most important example of the use of this exception.)		(b) The minor portion exception is repealed.	(b) The minor portion exception is retained but limited to the lesser of 5% of bond proceeds or $100,000 (determined without regard to any reasonably required debt service reserve fund, defined as under present law).

1 Profit limitations and determination of bond yield (cont.)	*Determination of bond yield.*—Bond yield is interpreted to mean the discount rate at which all anticipated payments of principal and interest on the bonds equals the net proceeds of the issue after deducting the costs of issuance. (This deduction of issuance costs permits bond issuers to earn a higher yield on the investment of bond proceeds, and thereby to pay issuance costs out of arbitrage profits.)	*Determination of bond yield.*—Bond yield is determined using the original issue discount rules of the Code. (Thus, costs of issuance may not be recovered out of arbitrage profits.)	*Determination of bond yield.*—Same as President's proposal	*Determination of bond yield.*—Same as President's proposal and House bill
	Additional restrictions for most IDBs	*Extension of present-law additional IDB restrictions*	*Extension of present-law additional IDB restrictions*	*Extension of present-law additional IDB restrictions*
	Profit limitations.—IDBs (other than IDBs for multifamily rental housing) are subject to the following additional arbitrage restrictions: (a) The amount of bond proceeds that may be invested at unrestricted yield in obligations unrelated to the purpose of the borrowing is limited to 150 percent of scheduled annual debt service. (b) The gross earnings on each issue of bonds must be rebated to the Federal Government at specified intervals. *Exceptions.*—The restriction on investment in nonpurpose obligations (item a, above) does not apply to investments for an initial temporary period or to investments for temporary periods related to current debt service (as opposed to reserve funds for future debt service). The rebate requirement does not apply if all bond proceeds are spent for the governmental purpose of the issue within 6 months of issuance of the bonds or to certain debt service funds on which less than $100,000 is earned in a bond year.	The present restriction on investment of bond proceeds in obligations unrelated to the purpose of the borrowing and the rebate requirements applicable to most IDBs would be extended to all tax-exempt bonds.	Same as President's proposal for bonds other than qualified mortgage bonds and qualified veterans' mortgage bonds.	Same as President's proposal and House bill, except— (1) Exempts current debt service funds of governmental units with general taxing powers from rebate requirement; (2) Provides an exception from the rebate requirement for bonds to finance operations of or facilities for governmental units with general taxing powers if all bonds issued by or on behalf of the unit in the year of issue are not reasonably expected to exceed $5 million; (3) Imposes a penalty in lieu of loss of tax-exemption for certain rebate errors in the case of governmental bonds and qualified 501(c)(3) bonds and directs Treasury to monitor the rebate requirement through use of information reports (*see* F., below); and (4) Exempts from rebate certain arbitrage earned on Federally guaranteed student loan bonds during an initial temporary period.
	Additional restrictions for qualified mortgage bonds *Profit limitations.*—The effective rate of interest on mortgage loans provided with qualified mortgage bonds may not exceed the yield on the issue by more than 1.125 percentage points. Investment of qualified mortgage bond proceeds in obligations unrelated to the purpose of the borrowing is restricted in a manner similar to that for most IDBs. Additionally, arbitrage profits must be rebated to the Federal Government or paid or credited to the mortgagors.		*Additional restrictions for qualified mortgage bonds* Same as present law.	*Additional restrictions for qualified mortgage bonds* Same as House bill.
			Additional restrictions for qualified veterans' mortgage bonds The present-law qualified mortgage bond additional arbitrage restrictions and rebate requirement are extended to qualified veterans' mortgage bonds in lieu of the expanded IDB-type restrictions.	*Additional restrictions for qualified veterans' mortgage bonds* Same as House bill.

1. Profit limitations and determination of bond yield (cont.)	*Additional restrictions for student loan bonds* In 1981, Treasury was directed to prescribe regulations applying additional arbitrage restrictions similar to those now applying to most IDBs to student loan bonds. *SLGS Program* The Treasury Department issues a special State and Local Government Series (SLGS) of Treasury bonds to enable issuers of State and local government bonds to avoid earning impermissible arbitrage profits. Interest rates on SLGS are set by reference to the permitted yield on each issue of tax-exempt bonds. Purchasers of SLGS must give Treasury 20 days notice of their intent to purchase. The minimum maturity of SLGS is 45 days.		*Additional restrictions for student loan bonds*.—Repeals present-law direction for special Treasury regulations to the extent inconsistent with new arbitrage restrictions imposed by the bill. *Effective dates.*—Bonds issued after December 31, 1985, except for the restriction on investment of bond proceeds in annuities and similar deferred compensation arrangements purchased from 3rd parties, which would apply to bonds issued after September 25, 1985.	*Additional restrictions for student loan bonds*.—Same as House bill. *Modification of SLGS Program* The Treasury Department would be directed to modify the SLGS program to provide investments similar to those offered by private money market funds (paying yields that would eliminate arbitrage profits and thereby eliminate the need to account for such profits) and to operate the program at no net cost to the Government. These new rules would permit demand deposits under the SLGS program by deleting advance notice requirements related to the purchase of SLGS and deleting minimum maturity requirements. *Effective dates.*—Bonds issued after date of enactment, except for the restriction on investment of bond proceeds in annuities and similar deferred compensation arrangements purchased from third parties, which applies to bonds issued after September 25, 1985. The modified SLGS program is required to be in effect by January 1, 1987.
2. Restrictions on advance refundings	Bonds other than IDBs and mortgage subsidy bonds may be advance refunded. IDBs and mortgage subsidy bonds may not be refunded more than 180 days before the refunded bonds are redeemed. An exception waives this 180-day rule in the case of refunded bonds having a maturity of less than three years.	Advance refundings would be defined to include all refundings where the refunded bonds were not redeemed immediately upon issuance of the refunding bonds. Interest on advance refunding bonds would be taxable.	Advance refundings are defined as refundings where the refunded bonds are not redeemed within 30 days of issuance of the refunding bonds. Up to two advance refundings are permitted for bonds other than nonessential function bonds, subject to the following restrictions— (a) Unless the present value of interest savings resulting from the advance refunding exceeds the costs of issuance of the advance refunding bonds, the aggregate amount of advance refunding bonds issued with respect to an original issue may not exceed 250 percent of the amount of the refunded (i.e., original) bonds; (b) Refunded bonds must be redeemed no later than the earlier of the date the refunded bonds may be redeemed at par or at a premium of 3 percent or less;	Advance refundings are defined as refundings where the refunded bonds are not redeemed within 90 days of issuance of the refunding bonds. Up to three advance refundings are permitted for governmental bonds and qualified 501(c)(3) bonds subject to the following restrictions— (a) No more than three sets of bonds (including the original bonds) may be outstanding at any one time; (b) In the case of advance refundings producing a debt service savings (determined without regard to issuance costs), refunded bonds must be retired no later than their first call date;

Item	Present Law	President's Proposal	House Bill	Senate Amendment
2. Restrictions on advance refundings (cont.)			(c) The temporary period during which unlimited arbitrage profits may be earned on the refunding bonds expires 30 days after the date of issuance, and for the refunded bonds, no later than the date of issuance of the advance refunding bonds, and	(c) Same as House bill,
			(d) Advance refunding bonds are subject to the unified State volume limitation provided by the bill to the extent of amounts attributable to any nongovernmental use of the refunded bonds that exceeded $1 million	(d) No provision;
			(e) No provision	(e) The 150% of annual debt service limitation on nonpurpose investments (*see* E 1, above) does not apply to advance refunding proceeds invested in an escrow for redemption of the refunded bonds, and
			(f) No provision.	(f) Rules are included to preclude flip-flops and other abusive transactions
			Effective date.—Advance refunding bonds issued after December 31, 1985 Advance refundings before December 31, 1985, are counted for the limit to 2 advance refundings, but the bill will not cause any such advance refunding bonds to become taxable Transitional exception is provided permitting advance refunding of certain pre-1986 section 501(c)(3) organization bonds and pre-1986 bonds that were governmental bonds when issued, but no longer qualify as such, subject to the new restrictions.	*Effective date* —Bonds issued after date of enactment Subject to a special exception permitting one additional advance refunding for bonds advance refunded three or more times before enactment, advance refundings before the date of enactment are counted for the limit to three such refundings, but the amendment will not cause any such pre-enactment advance refunding bonds to become taxable Transitional exception is provided permitting pre-enactment bonds that were governmental when issued, but no longer qualify as such, to be advance refunded subject to the new restrictions
3. Restriction on early issuance of bonds	No separate rules require that bond proceeds be spent within a specified period following issuance, however, issuers are required to proceed with "due diligence" to realize the governmental purpose of the borrowing to qualify for a temporary period when unlimited arbitrage may be earned	Five percent or more of bond proceeds would be required to be spent for the purpose of the borrowing within 30 days after bond issuance All bond proceeds (other than costs of issuance and amounts in a reasonably required reserve fund) would have to be spent no later than 3 years after bond issuance.	Same as the President's proposal, except the Treasury is authorized to extend the 30-day or 3-year period during which bond proceeds are required to be spent in cases where undue hardship otherwise would result (e g where delay results from events such as Acts of God). *Effective date* —Bonds issued after December 31, 1985.	No provision

Item	Present Law	President's Proposal	House Bill	Senate Amendment
*. Information Reporting Requirement for All Tax-Exempt Bonds	Issuers of private activity bonds (defined as IDBs, student loan bonds, and bonds for section 501(c)(3) organizations) and mortgage subsidy bonds are required to report certain information about volume and users of bond-financed facilities to the Treasury.	The present-law information reporting requirements for bonds other than mortgage subsidy bonds would be extended to all tax-exempt bonds.	Same as the President's proposal *Effective date*.—Bonds issued after December 31, 1985.	Same as President's proposal and House bill *Effective date*.—Bonds issued after date of enactment
. Special Transitional Exceptions		No provisions	Various project-specific transitional exceptions.	Various project-specific transitional exceptions.
. General Stock Ownership Corporation Provisions (secs. 702 and 703 of the House bill and secs. 1517 and 1518 of the Senate amendment)	A State may establish a General Stock Ownership Corporation (GSOC) that serves as an investment fund for its citizens. GSOCs may elect to be exempt from tax with the shareholders reporting as income their prorata share of the GSOCs taxable income. (No State has used this provision.)	The GSOC provisions would be repealed as "deadwood." *Effective date*.—January 1, 1984.	Same as President's proposal *Effective date*.—January 1, 1984	Same as President's proposal and House bill. *Effective date*.—January 1, 1984

Item	Present Law	President's Proposal	House Bill	Senate Amendment
A. Income Taxation of Trusts and Estates (sec. 1211 of the House bill and secs. 101, 1611–1614 of the Senate amendment)				
1. In general	The income taxation of a trust depends on whether the trust is a grantor or nongrantor trust. In the case of a grantor trust (i.e., one where the grantor (or other person with the power to revoke the trust) has certain powers with respect to the trust), income is taxed directly to the grantor. In the case of a nongrantor trust, each trust is treated as a separate taxable entity.	As under present law, income of a grantor trust is taxed directly to the grantor. However, the President's proposal revises the definition of a grantor trust. During the lifetime of the grantor, all income of any nongrantor trust generally would be taxed to the trust at the top marginal rate of the grantor.	The bill limits the scope of the grantor trust rules and continues to tax the income of a grantor trust directly to the grantor. Nongrantor trusts generally are taxed at the top marginal rate of the grantor. In addition, special rules may permit the use of lower rates where the trust's beneficiaries are minor children of the grantor. In addition, in the case of a qualifying beneficiary trust, income generally is taxed to the trust at the top marginal rate of the beneficiary. Foreign trusts are taxed under the present law rules.	Nongrantor trusts and estates are taxed as under present law, except that the tax brackets applicable to such trusts and estates are narrowed. As under present law, income of a grantor trust is taxed directly to the grantor. However, the definition of a grantor trust is revised, as described below.
2. Trusts other than grantor trusts	Any trust that is not a grantor trust is treated as a separate taxable entity.	Any trust that is not a grantor trust would continue to be treated as a separate taxable entity.	Any trust that is not a grantor trust continues to be treated as a separate taxable entity.	Same as House bill.
	Taxable year.—The trust may elect a taxable year other than that of the grantor. Beneficiaries of trusts are taxable on distributions from trusts to the extent of the trust's taxable income for taxable years ending with, or within, the taxable year of the beneficiary. If the trust is on a different taxable year than its beneficiaries, the beneficiaries defer taxable income from one taxable year to the next. A trust can elect to use any year as its taxable year.	*Taxable year.*—Each nongrantor trust would be required to adopt the same taxable year as the grantor.	*Taxable year.*—The trust may elect a taxable year other than that of the grantor.	*Taxable year.*—Trusts (both existing and newly created) are required to adopt a taxable year ending in October, November, or December.
	Applicable rate.—Each nongrantor trust separately calculates tax liability at the rate applicable to married taxpayers filing separately.	*Applicable rate.*—Each nongrantor trust generally is taxed at the top marginal rate of the grantor.	*Applicable rate.*—The income of a nongrantor trust that is not a qualified beneficiary trust generally is taxed at the top marginal rate of the grantor. The rate is determined by applying any unused rate bracket amount allocated to the trust by the grantor. For example, if the grantor has $20,000 of unused rate bracket amount in the 35% bracket in a particular year, the grantor could allocate that amount to any trust he had created. The trust would be taxed at 35% on the first $20,000 of income and 38% on any income in excess of $20,000.	*Applicable rate.*—Undistributed income of both existing and newly created nongrantor trusts is taxed at the following rates: $0–$5,000 ..... 15% $5,000 or more ..... 27% The benefit of the 15-percent bracket is phased-out for trust taxable income between $13,000 to $25,000.

2. Trusts other than grantor trusts (cont.)			Where a trust has more than one grantor, each portion of the trust attributable to a particular grantor generally is treated as a separate trust for Federal tax purposes However, married individuals may elect to be treated as a single grantor. In addition, where the trust beneficiaries are children of the grantor who are between the ages of 14 and 21, the unused rate bracket amounts of the children may be allocated to the trust If no unused rate bracket amount is allocated to a trust for a particular year, the income of the trust is taxed at the top marginal rate (38%) *Qualified beneficiary trust* --In the case of a qualified beneficiary trust, the income of the trust is taxed at rates determined by using the unused rate bracket amount of the beneficiary A qualified beneficiary trust is one where all of the trust income and corpus may be used only for distributions to, or for the benefit of, the beneficiary or his estate. A qualified beneficiary trust also includes any QTIP trust.	
	Calculation of tax liability.—In calculating tax liability— (1) the personal exemption is limited to $100 or $300; (2) no zero bracket amount is permitted; (3) an unlimited charitable deduction is available; and (4) a distribution deduction generally is allowed for distributions to beneficiaries.	*Calculation of tax liability* —In calculating tax liability, the President's proposal generally follows present law except that— (1) no personal exemption is allowed, and (2) a distribution deduction is allowed during the lifetime of the grantor only for certain mandatory distributions and only if the grantor has not retained a disqualifying interest.	*Calculation of tax liability* —In calculating tax liability, generally follows the President's proposal except that— (1) a personal exemption of $100 is allowed, and (2) a distribution deduction is not allowed at any time	*Calculation of tax liability* —Same as present law
		Mandatory distributions.—Mandatory distributions generally would include— (1) A fixed or ascertainable amount of trust income or property required by the terms of the trust to be distributed to a specific beneficiary or beneficiaries (whether or not actually distributed); and (2) Amounts irrevocably set aside for a beneficiary, provided the amount set aside is required to be distributed ultimately to the beneficiary or the beneficiary's estate, and the beneficiary agrees to include currently in income the amount set aside.		

2. Trusts other than grantor trusts (cont.)		*Disqualifying interest*.—If the grantor retains a disqualifying interest, then no distribution deduction will be permitted, even for mandatory distributions. A grantor has a disqualifying interest— (1) if any person other than the grantor or the grantor's spouse possesses the discretionary power to make payments of trust property to the grantor or the grantor's spouse; (2) if any portion of the trust may revert to the grantor or the grantor's spouse, unless the reversion cannot occur prior to the death of the income beneficiary of such portion and such beneficiary is younger than the grantor, or prior to the expiration of a term of years that is greater than the life expectancy of the grantor at the creation of the funding of the trust; (3) if any person has the power exercisable in a nonfiduciary capacity to control trust investments, to deal with the trust for less than full and adequate consideration, or to exercise any general administrative powers in a nonfiduciary capacity without the consent of a fiduciary; (4) if, and to the extent that, an otherwise deductible mandatory distribution satisfies a legal obligation of the grantor or grantor's spouse, including a legal obligation of support or maintenance; or (5) if trust income or corpus can be used to carry premiums on life insurance policies on the life of the grantor or the grantor's spouse with respect to which the grantor or the grantor's spouse possesses any incident of ownership.		
	Aggregation of trusts.—Pursuant to Treasury regulations, two or more trusts will be treated as a single trust if (1) the trusts have substantially the same grantor or grantors and substantially the same primary beneficiary or beneficiaries, and (2) a principal purpose of the use of separate trusts is the avoidance of Federal income tax.	*Aggregation of trusts*.—Under the proposal, during the lifetime of the grantor, income of all trusts created by the grantor (in the case of a joint return, the grantor and the grantor's spouse) generally will be aggregated with the grantor's income (in the case of a joint return, the sum of the grantor's and the spouse's income) to determine the marginal tax rate applicable to the trust. The total tax then must be allocated to each trust proportionately on the basis of taxable income.	*Aggregation of trusts*.—Same as the President's proposal, except that it simplifies the aggregation by permitting the grantor (or designated beneficiary) to allocate unused rate bracket amounts. In addition, where trust beneficiaries are minor children of the grantor (who are between the ages of 14 and 21), it permits the children to allocate their unused rate bracket amounts to the trust, effectively subjecting some or all of the trust income to an effective tax rate lower than that of the grantor.	*Aggregation of trusts*.—Same as present law.

3. Taxation of trusts after the death of the grantor	Under present law, there is no distinction between the taxation of a trust during the grantor's lifetime or after his death	For all taxable years beginning after the grantor's death, each trust established by the grantor must separately compute taxable income Tax liability is computed using the rate schedule applicable to married individuals filing separately; with no zero bracket amount, no personal exemption and a dedoction for all distributions actually made.	After the death of the grantor, the trust determines its tax by taking into account any rate bracket amount allocated to the trust under the grantor's will If the grantor's will does not provide for an allocation of his rate bracket amounts, his rate bracket amounts are allocated among all the trusts created by the grantor in proportion to the agreement of the trustees or if no agreement can be reached on an equal basis.	Same as present law, except for rates set forth above (in item 2)
4 Taxation of distributions to beneficiaries	*In general.*—Distributions to beneficiaries are taxed to beneficiaries and deductible by the trust to the extent of the distributable net income (DNI) of the trust. *Tier system.*—DNI is allocated first to distributions that are required to be made out of income for the year, secondly to distributions made to charity out of trust income, and lastly to other distributions	As under current law, distributions to beneficiaries that are deductible to the trust would be taxable to beneficiaries. However, the tier rules would be repealed and each receipient would take into account a proportionate share of DNI.	Repeals the DNI rules, exempts all distributions from the recipient beneficiary's income.	Same as present law
5. Taxation of previously accumulated income	Distributions to beneficiaries out of previously accumulated income are taxed to beneficiaries under a throwback rule designed to tax the income upon distribution at the beneficiaries' average marginal rate in the previous five years	The throwback rules continue to apply and would be expanded to apply to income accumulated while a beneficiary was under 21 years of age. In addition, the President's proposal suggests that it may be appropriate to impose an interest charge on the tax payable with respect to an accumulation distribution	Repeals the throwback rules	Same as present law

Item	Present Law	President's Proposal	House Bill	Senate Amendment
6. Grantor trusts	Under certain circumstances, the grantor (or other person having the power to revoke the trust) is taxed directly on trust income. *The grantor.*—The grantor generally is treated as the owner of all or a portion of the trust if (1) the grantor has a reversionary interest expected to return to him within ten years; (2) the grantor has the power to control beneficial enjoyment of the income or corpus; (3) the grantor retains certain administrative powers; (4) the grantor retains the right to revoke the trust at any time during the first ten years of the trust's existence; or (5) the income of the trust may be distributed to the grantor or the grantor's spouse during the first ten years of the trust's existence. *Persons other than the grantor.*—A person other than the grantor is treated as the owner of all or a portion of the trust if (1) that person has the power to revoke the trust, or (2) that person surrendered the power to revoke and that person retained one of the powers listed above.	The President's proposal limits the circumstances under which a grantor would be treated as the owner of the trust. A grantor would be taxed directly on trust income only if (a) payments of trust property are required to be made to, or for the benefit of, the grantor or the grantor's spouse; (b) payments may be made to or for the benefit of the grantor or the grantor's spouse— (i) under a discretionary power to make payments, or (ii) by exercise of a power to revoke or amend the trust, which power is in the grantor or the grantor's spouse; (c) the grantor or the grantor's spouse has any power to cause the trustee to lend trust income or corpus to either of them without adequate security and interest; or (d) the grantor or the grantor's spouse has borrowed trust income or corpus and has not completely repaid the loan or any interest thereon before the beginning of the taxable year.	The House bill expressly provides that the grantor of a grantor trust will be treated as owning the assets of the trust for all purposes. The grantor trust rules are modified so that they apply only where there are (1) certain administrative powers which permit indirect control over the trust assets, (2) a power to revoke, or (3) a power to control income.	The grantor trust rules are modified to delete the 10-year exception of present law (e.g., "Clifford" trusts) and to treat powers and interests of the grantor's spouse as powers and interests of the grantor (e.g., spousal remainder trusts).
7. Estates	A decedent's estate is treated as a separate taxable entity, beginning as of the date of death. The estate may elect a taxable year different than the decedent's taxable year. Under present law, an estate is allowed a $600 personal exemption and otherwise computes its tax liability generally in the same manner as a nongrantor trust, except that the throwback rules do not apply.	The President's proposal would— (a) provide that an estate would be treated as a separate taxable entity; (b) require the estate to adopt the same taxable year as the decedent; (c) subject an estate to tax at a separate rate schedule, with no personal exemption and no zero bracket amount, but with a deduction for distributions to beneficiaries, (d) exempt any estate with less than $600 of gross income from Federal tax liability; and (e) continue the taxable year of the decedent after his death as if the decedent died on the last day of his taxable year.	Under the House bill— (a) an estate is treated as a separate taxable entity that is required to adopt the same taxable year as the decedent; (b) an estate is taxable at the same rates as a single individual, calculated without a zero bracket amount but with a personal exemption of $600; (c) no distribution deductions is allowed; and (d) the executor, with the consent of the surviving spouse, is permitted to elect to continue the taxable year of the decedent after his death as if the decedent died on the last day of his taxable year.	The undistributed income of both existing and newly created estates for taxable years beginning more than 2 years after the decedent's death is taxed according to the rates applicable to nongrantor trusts (See item 2, above). The rate for the first two taxable years is the rate of a married person filing separately.

Item	Present Law	President's Proposal	House Bill	Senate Amendment
8. Payment of estimated income taxes by trusts and estates (sec. 1614 of Senate amendment)	Neither trusts nor estates are required to make estimated payments of their income taxes. Trusts are required to pay their income tax at the time of filing of the income tax return Income tax of an estate is payable in four quarterly payments after the year in which the income is earned	No provision.	No provision	Trusts and estates are required to make estimated payments of income taxes. In addition, the amendment repeals the rule that permits estates to pay their taxes over 4 equal installments Thus, any income taxes of an estate that are not paid as estimated taxes are payable at the normal due date of the income tax return of the estate (i e., 3½ months after the close of the taxable year).
9. Effective date		*Effective date* —The President's proposal generally would apply to irrevocable trusts created after December 31, 1985, and to trusts that are revocable on January 1, 1986, for taxable years beginning on or after that date. If additional amounts are contributed after December 31, 1985, to a trust that is irrevocable on that date, the trust would be treated as created after that date. For other trusts that are irrevocable on January 1, 1986, certain of these rules would apply with modifications.	*Effective date.*—Applies to irrevocable trusts created after September 25, 1985, and to trusts that are revocable on September 25, 1985, for taxable years beginning on or after that date. If additional amounts are contributed after September 25, 1985, to a trust that is irrevocable on that date, such contribution is treated as a separate trust created after that date. Other trusts that are irrevocable on September 25, 1985, continue to be subject to tax under present law.	*Effective date.*—The rate changes are effective on July 1, 1987. For 1987 returns, tax rate schedules will blend the schedules of rates that would have been applied under present law (i e., 1986 rates as adjusted for inflation) with the new rate schedules. The changes in the grantor trust rules are effective for transfers in trust made after March 1, 1986, with an exception under which the 10-year rule of present law would continue to apply to certain trusts created pursuant to certain binding property settlements entered into before March 1, 1986. The change in the taxable year rules is effective with respect to taxable years beginning after December 31, 1986 Thus, in the case of a trust that presently has a taxable year ending before October, the trust's first taxable year beginning after December 31, 1986, will be a short taxable year Distributable net income taxable to beneficiaries for that short taxable year are to be included in income of the beneficiary evenly over a 4-year period. The change in the rule requiring trusts and estates to pay estimated tax is effective for taxable years beginning after December 31, 1986.

Item	Present Law	President's Proposal	House Bill	Senate Amendment
B. Unearned Income of a Minor Child (sec. 1201 of the House bill, and sec. 1601 of the Senate amendment)	If income-producing assets are transferred to a minor child, income earned on those assets generally is taxed to the child at the child's marginal rate.	The proposal would tax unearned income of a child under 14 years of age to the child at the top marginal rate of the parents to the extent the income was attributable to property received from the parents. Earned income and unearned income derived from assets received from sources other than a parent that are placed in a qualified segregated account would be taxed at the child's marginal rate.	The unearned income of a child under 14 years of age is taxed to the child at the top marginal rate of the parents to the extent the income is attributable to property received from the parents. Such rate is deemed to be the top marginal rate (38 percent), unless the parent assigns an unused rate bracket amount at a lower rate to the child. Earned income and unearned income derived from assets received from sources other than a parent that are placed in a qualified segregated account are taxed at the child's marginal rate.	Same as House bill, except that the tax payable by the child on the parental source unearned income is equal to the additional amount of tax that the parent would be required to pay if the child's parental source unearned income were included in the parent's taxable income.
		Property eligible to be placed in a qualified segregated account would include earned income, money or property received from someone other than the parents and property received by reason of a parent's death.	Property eligible to be placed in a qualified segregated account includes earned income, money or property received from someone other than the parent or step parent, and property received by reason of a parent's or step parent's death.	
		The proposal would apply with respect to a child under 14 years of age who is eligible to be claimed as a dependent on the parents' return.	The provision applies with respect to a child under 14 years of age who has at least one living parent as of the close of the taxable year.	
		Effective date.—The proposal would apply for taxable years beginning after December 31, 1985.	*Effective date.*—Taxable years beginning after December 31, 1985.	*Effective date.*—Taxable years beginning after December 31, 1986.

C. Gift and Estate Taxes 1. Current use valuation recapture period for pre-1982 estates (sec. 1616 of the Senate amendment)	Real property used in certain farming and other closely held business activities may be valued at its current use, rather than fair market, value for estate tax purposes. A special recapture tax is imposed if the property is disposed of or ceases to be used in its qualified use within a 10-year recapture period. (In 1981, this recapture period was reduced from 15 years, effective for estates of individuals dying after December 31, 1981.)	No provision	No provision	The reduction in the recapture period to 10 years enacted in 1981 is extended to estates of individuals who died after 1976 and before 1982.
2. Filing estate tax current use valuation elections (sec. 1615 of the Senate amendment)	Real property used in certain farming and other closely held business activities may be valued at its current use, rather than fair market, value for estate tax purposes. This provision is available only if elected on the first estate tax return filed and only if the election, as filed, substantially complies with Treasury Department regulations.	No provision.	No provision	Estates of individuals dying before January 1, 1986, that substantially complied with the requirements enumerated on the Federal Estate Tax Return (as opposed to Treasury regulations) are allowed to perfect defective elections within 90 days after being notified by IRS.
3. Gift tax treatment of certain disclaimers (sec. 1617 of the Senate amendment)	A disclaimer is an irrevocable refusal to accept property. If a disclaimer complies with Federal rules, the disclaimed property is not treated as having been transferred by the party making the disclaimer for Federal gift tax purposes. Disclaimers made after 1976 are governed by statutory rules; disclaimers made before 1977 are governed by Treasury regulations, adopted on November 15, 1958. (The U.S. Supreme Court upheld these regulations in *Jewett* v. *Commissioner*, 455 U.S. 305 (1982).)	No provision.	No provision.	Disclaimers of property transferred before November 15, 1958, that were made before December 9, 1980, are valid for Federal gift tax purposes if the requirements of the 1958 Treasury regulations (other than timing) were satisfied and the disclaimer was made within a reasonable time after the property vested (rather than was transferred, as required by the regulations). (As modified by floor amendment by Senators Metzenbaum and Chafee, adopted by voice vote.)
4. Gift and estate tax deductions for certain conservation easements (sec. 717 of the Senate amendment)	A special exception to the general restrictions on tax deductions for charitable contributions of partial interests in property applies in the case of qualified conservation contributions (e.g., easements). To qualify for a gift or estate tax deduction, these contributions must satiafy the same requirements, including a conservation purpose requirement, that apply for income tax deductions.	No provision	No provision.	Gift or estate tax deductions are permitted for qualified conservation contributions without regard to the income tax conservation purpose requirement. *Effective date.*—Transfers after December 31, 1986.

5. Special rule for Estate of James H.W. Thompson (sec. 1618 of the Senate amendment)	Gift and estate tax deductions are permitted for charitable contributions only if property is transferred directly to a qualified organization and certain other requirements are satisfied.	No provision.	No provision	Certain property transferred by James H W Thompson to his nephew who then transferred the property to a charitable foundation pursuant to his uncle's wishes qualifies for an estate tax charitable deduction as if it passed directly from Thompson to the charity
6. Gift and estate tax marital deduction elections (sec. 1620 of the Senate amendment)	A deduction is allowed for gift and estate tax purposes for property transferred to a spouse. This "marital deduction" is not allowed for terminable interests (i.e., property interests that will not be subject to gift or estate tax if the property is transferred by the donee-spouse) unless the property is qualified terminable interest property ("QTIP property") and a special election is made. This special election must be made on the first estate tax return filed, or on a gift tax return filed by April 15 of the year after the year in which the gift is made. If a QTIP election is made, the property is subject to gift or estate tax if the donee-spouse subsequently transfers it.	No provision	No provision	Estates that in good faith claim a marital deduction on property that is found to be terminable interest property on audit are permitted to make QTIP elections within 90 days after that finding if the property otherwise qualifies for that election (Floor amendment by Senator Wilson, adopted by voice vote) *Effective date* —Estates of individuals dying after 1981, but only if the period of limitations for assessment of tax does not expire before the date of enactment in the case of estates of individuals dying before date of enactment.

D. Generation-Skipping Transfer Tax (secs. 1221-1223 of the House bill)	A generation-skipping transfer tax (GST tax) is imposed on transfers under a trust or similar arrangement having beneficiaries in more than one generation below that of the grantor of the trust. Subject to certain transition rules, the GST tax applies to transfers occurring after June 11, 1976	No provision in 1985 President's proposal; however, a separate Treasury Department proposal, introduced in the 98th Congress, would modify the GST tax as follows:	The House bill includes the previously introduced Treasury proposal with the following modifications:	No provision (retains present law)
1. Taxable transfers	The GST tax is imposed on taxable terminations under and taxable distributions (other than income) from a trust or a similar arrangement in which beneficiaries in more than one generation younger than that of the grantor have an interest (or certain powers over the property) (i.e., generation-sharing arrangements). Direct transfers to persons more than one generation below that of the grantor are not subject to GST tax (i.e., direct skips).	The modified GST tax would be imposed on taxable terminations and taxable distributions (including distributions of income) under generation-sharing arrangements, as under present law. Taxable beneficiaries would include only persons having interests in (as opposed to powers over) property Direct skips would be subject to tax.	Same as Treasury proposal, except a provision is added under which direct skips to grandchildren would not be treated as generation-skipping transfers if the grandchild's parent who was a lineal descedant of the transferor was deceased when the transfer occurred	No provision.
	In the case of trusts having beneficiaries assigned to three or more younger generations GST tax is imposed on the termination of the interests (or powers) of each of the intermediate younger generations (when the trust property is not subject to gift or estate tax)	In the case of trusts having beneficiaries assigned to three or more younger generations, GST tax would be imposed only on the termination of the oldest such generation.	Same as present law.	
2. Exemption from tax	There is no specific exemption or credit that a grantor may apply against GST tax; however, if a generation-skipping transfer occurs at or after the deemed transferor's death, any unused portion of the deemed transferor's gift and estate tax unified credit may be applied against GST tax. Additionally, a special $250,000 per deemed transferor exemption is permitted for transfers to grandchildren.	A specific exemption of $1 million per transferor would be provided in lieu of the present credit and grandchild exclusion. The specific exemption would be transferable between spouses. Rules would be provided for allocation of unused exemption amounts remaining after the death of a transferor. Under special rule, certain trust beneficiaries could receive up to $10,000 per year in generation-skipping transfers free of GST tax	Same as the Treasury proposal except generation-skipping transfers by married individuals are treated as made one-half by each spouse pursuant to rules similar to the present gift tax rules on such gifts to third persons; the additional $10,000 exemption for distributions to certain generation-skipping beneficiaries is deleted; and a special $2 million per grandchild exemption is provided for direct skips.	No provision.
3. Tax rate	The GST tax is imposed at the gift or estate tax rate that would be imposed if the property were transferred to the beneficiary by a deemed transferor (generally, the parent of the beneficiary). GST tax on taxable terminations is determined on a tax-inclusive basis (like the estate tax) and taxable distributions are taxed on a tax-exclusive basis (like the gift tax).	All generation-skipping transfers would be subject to tax at a flat rate, equal to 80 percent of the maximum gift and estate tax rate. GST tax on transfers under generation-skipping arrangements would be determined on a tax-inclusive basis; tax would be determined on a tax-exclusive basis on direct skips	All generation-skipping transfers would be subject to tax at a flat rate, equal to the maximum gift and estate tax rate (currently, 55%; scheduled to decline to 50% in 1988). GST tax is determined as provided in the Treasury proposal	No provision

Item	Present Law	President's Proposal	House Bill	Senate Amendment
1. Credit for State taxes	A limited credit against GST tax is permitted for State death taxes imposed on generation-skipping transfers (based on the deemed transferor concept)	A credit against GST tax would be permitted equal to 5 percent of State taxes on generation-skipping transfers.	A credit against GST tax is permitted equal to 5 percent of State taxes on generation-skipping transfers. *Effective date*.—The amended GST tax applies to transfers after the date of enactment, subject to the following exceptions: (1) Inter vivos transfers occurring after September 25, 1985, would be subject to the amended tax; (2) Transfers from trusts that were irrevocable before September 26, 1985, would be exempt to the extent that the transfers were not attributable to additions to the trust corpus occurring after that date, and (3) Transfers pursuant to wills in existence before September 26, 1985, would not be subject to tax if the decedent was incompetent on that date and at all times thereafter until death. The present GST tax would be repealed, retroactive to June 11, 1976.	No provision

Item	Present Law	President's Proposal	House Bill	Senate Amendment
A. Penalties 1. Penalties relating to information returns (sec. 1301 of the House bill and sec. 501 of the Senate amendment)	The Code provides a $50 penalty for each failure to file an information return with the IRS and each failure to supply a copy of the information return to the taxpayer. The maximum penalty is generally $50,000, except in cases of intentional disregard. The Code also provides a $5 penalty ($50 under certain circumstances) for failure to furnish a correct taxpayer identification number. There is no specific penalty for including other incorrect information on an information return.	(a) Eliminate the $50,000 maximum; and (b) Impose a new $5 penalty for supplying incorrect information (with a reasonable cause exception). *Effective date.*—Returns due on or after January 1, 1986 (without regard to extensions).	Same as the President's proposal, except provides a $100,000 maximum penalty ($20,000 for supplying incorrect information). *Effective date.*—Returns due on or after January 1, 1986 (without regard to extensions).	Same as House bill. Additionally, provides that the $20,000 maximum does not apply in cases of intentional disregard. *Effective date.*—Returns due on or after January 1, 1987 (without regard to extensions).
2. Penalty for failure to pay taxes (sec. 1302 of the House bill and sec. 502 of the Senate amendment) *a. Penalty*	(a) A taxpayer who fails to pay taxes when due must pay a penalty of one-half of one percent of the tax for the first month not paid. The penalty increases by one-half of one percent for each month the failure to pay continues, up to a maximum of 25 percent.	(a) Repeal present-law penalty.	(a) Increases the penalty for failure to pay from one-half of one percent to one percent per month (up to the 25 percent limit) after the taxpayer has been notified that the IRS will levy upon the taxpayer's assets to collect the past-due taxes. This is the point at which the IRS uses more expensive collection methods. Improves the coordination of the penalty for failure to pay taxes with the penalty for failure to file a tax return. *Effective date.*—Amounts assessed after December 31, 1985.	(a) Same as House bill. *Effective date.*—Amounts assessed after December 31, 1986.
b. Cost of collection charge	(b) No provision.	(b) Replace the penalty for failure to pay taxes with a cost of collection charge. The goal of the proposal is to recover IRS' costs of collecting delinquent payments. *Effective date.*—Returns due on or after January 1, 1986 (without regard to extensions).	(b) No provision.	(b) Requires the Treasury to report to the Senate Finance and House Ways and Means Committees by March 1, 1987, with specific recommendations as to how the cost of collection charge described in the President's proposal is proposed to be implemented.

Item	Present Law	President's Proposal	House Bill	Senate Amendment
3. Negligence and fraud penalties (sec. 1303 of the House bill and sec. 503 of the Senate amendment)	(a) The penalty for negligence has two components. The first is a time-sensitive component, which is half of the interest due from the date the return was required to be filed until the date the tax is assessed on the portion of the underpayment attributable to negligence. The second component is 5 percent of the entire underpayment of tax. If a fraud penalty is imposed, no negligence penalty is imposed.	(a) No provision	(a) Applies the negligence penalty only to the portion of the underpayment not subject to the fraud penalty. The time-sensitive component is not changed.	(a) Applies the negligence penalty only to the portion of the underpayment attributable to negligence and increases the 5-percent component of the negligence penalty to 10 percent. The time-sensitive component is not changed.
	(b) A per se negligence penalty applies to failures to include on a tax return interest or dividends that were reported to the taxpayer on an information report, in the absence of clear and convincing evidence that there was no negligence. This penalty applies only to the portion of the underpayment attributable to the failure to report.	(b) No provision.	(b) Applies the per se negligence penalty to all failures to include on a tax return items subjects to information reporting.	(b) Same as House bill
	(c) The general negligence penalty does not apply to all taxes imposed by the Code.	(c) No provision.	(c) Applies the general negligence penalty to all taxes imposed by the Code.	(c) Same as House bill.
	(d) The penalty for fraud has two components. The first is a time-sensitive component, which is half of the interest due from the date the return was required to be filed until the date the tax is assessed on the portion of the underpayment attributable to fraud. The second component is 50 percent of the entire underpayment of tax.	(d) No provision.	(d) Applies the fraud penalty only to the portion of the underpayment of tax attributable to fraud; increases the 50 percent component of the fraud penalty to 75 percent. The time-sensitive component is not changed.	(d) Same as House bill.
			Effective date.—Returns required to be filed on or after January 1, 1986.	*Effective date.*—Returns required to be filed on or after January 1, 1987.
4. Penalty for substantial understatement of tax liability (sec. 501 of the Senate amendment)	If a taxpayer substantially understates income tax for any taxable year, the taxpayer must pay a penalty equal to 10 percent of the underpayment of tax attributable to the understatement. An understatement is substantial if it exceeds the greater of 10 percent of the tax required to be shown on the tax return or $5,000 ($10,000 for most corporations). This penalty does not apply to items for which there was substantial authority for the position taken by the taxpayer or to items with respect to which the taxpayer made adequate disclosure on his tax return (with special rules for tax shelters).	No provision.	No provision.	Increases this penalty from 10 to 20 percent of the amount of the underpayment of tax attributable to the understatement. *Effective date.*—Returns due after December 31, 1986 (without regard to extensions).

Item	Present Law	President's Proposal	House Bill	Senate Amendment
B. Interest Provisions 1. Interest rate (sec. 1331 of the House bill and sec. 511 of the Senate amendment)	Taxpayers must pay interest to the Treasury on underpayments of tax, and the Treasury must pay interest to taxpayers on overpayments of tax Both the rate taxpayers pay to the Treasury and the rate the Treasury pays to taxpayers are the same rate. That rate is determined semiannually The rate utilized is the prime rate	No provision.	The interest rate that Treasury pays to taxpayers is the 3-month Treasury bill rate plus 2 percentage points The interest rate that taxpayers pay to the Treasury is the 3-month Treasury bill rates plus 3 percentage points. The rate is adjusted quarterly *Effective date.*—Determinations of interest for periods after December 31, 1985.	Same as House bill, except that the underlying rate is the Federal short-term rate *Effective date*—Determinations of interest for periods after December 31, 1986.
2. Interest on underpayments of accumulated earnings tax (sec. 1332 of the House bill and sec. 512 of the Senate amendment)	The Code imposes the accumulated earnings tax to prevent corporations from accumulating (rather than distributing) dividends with the intent of reducing or avoiding taxes Interest is charged only from the date IRS demands payment of the tax, rather than the date the return was originally due to be filed	No provision.	Charges interest on underpayments of the accumulated earnings tax from the date the return was originally due to be filed *Effective date.*—Returns due in or after 1986.	Same as House bill. *Effective date.*—Returns due in or after 1987.

C. Information Reporting Provisions 1. Information reporting on real estate transactions (sec. 1341 of the House bill and sec. 521 of the Senate amendment)	Brokers must, when required by Treasury regulations, file information reports on the business they transact for customers (sec. 6045). To date, the IRS has issued regulations requiring reporting only of gross proceeds of sales of securities, commodities, regulated futures contracts, and precious metals. Reporting on real estate transactions is not currently required under these regulations. Failure to file a required information report is generally subject to a $50 penalty per failure, up to a maximum of $50,000.	No provision.	Real estate transactions must be reported. The reporting is to be done by the settlement attorney or other stakeholder. This generally would be the person responsible for closing the transaction. *Effective date.*—Real estate transactions occurring on or after January 1, 1986.	Real estate transactions must be reported by the first person on the following list (or, if no such person is involved in the transaction, the next person on the list involved in the transaction): (a) the title company, (b) the mortgage lender, (c) the settlement attorney or other person responsible for closing the transaction, (d) the seller's broker, (e) the buyer's broker, or (f) any other person designated in Treasury regulations. (Floor amendment by Senator Humphrey reordering the list of persons required to report, adopted by voice vote.) *Effective date.*—Real estate transactions occurring on or after January 1, 1987.
2. Information reporting on persons receiving contracts from certain Federal agencies (sec. 1342 of the House bill and sec. 522 of the Senate amendment)	There is no provision that requires information reporting on persons receiving Federal contracts.	No provision.	Requires Federal executive agencies to file an information return on each person with which the agency enters into a contract, listing the person's name, address, taxpayer identification number, and any other information required by Treasury. *Effective date.*—Contracts signed on or after or in effect on or after January 1,1986.	Same as House bill. *Effective date.*—Contracts signed on or after or in effect on or after January 1, 1987.
3. Information reporting on State and local taxes (sec. 145 of the House bill)	No provision requires State and local governments to provide information reports to the IRS and the taxpayer on payments of State and local income, real property, and personal property taxes.	No provision.	Any State or local government that imposes an income tax, a real property tax, or a personal property tax, must report to the individual who paid those taxes and to the IRS the amount of those taxes paid by that individual. *Effective date.*—January 1, 1987.	No provision.
4. Information reporting on royalties (sec. 523 of the Senate amendment)	Information reporting on royalty payments exceeding $600 per payee is required by Treasury regulations, issued under general statutory authority. Information reporting on interest begins at $10 per payee, under specific statutory authority.	No provision.	No provision.	Requires information reporting statutorily for royalty payments exceeding $10 per payee, parallel to information reporting on interest. *Effective date.*—Payments made after December 31, 1986.

5. Taxpayer identification numbers of dependents required to be shown on tax returns (sec. 566 of the Senate amendment)	There is no requirement that a taxpayer claiming a dependent on a tax return report the taxpayer identification number (generally, the social security number) of that dependent on that tax return	No provision	No provision.	A taxpayer claiming a dependent who is at least 5 years old must report the taxpayer identification number of that dependent on that tax return. (Floor amendment by Senator Evans, adopted by voice vote.) *Effective date.*—Returns due on or after January 1, 1987 (without regard to extensions)
6. Tax-exempt interest required to be shown on tax returns (sec. 1343 of the House bill)	There is no requirement that all taxpayers report the amount of tax-exempt interest they receive on their tax returns The individual income tax return (Form 1040) for 1985 does, however, require that taxpayers with taxable social security benefits report the tax-exempt interest they receive	No provision	Any person required to file a tax return must report on that return the amount of tax-exempt interest received or accrued during the taxable year *Effective date.*—Taxable years beginning after December 31, 1985	No provision.
7. Modification of separate mailing requirement (secs. 501(c)(2), (3), and (5), and 523 of the Senate amendment)	Information reports on interest, dividends, and patronage dividends must be supplied to the taxpayer either in person or in a separate, first-class mailing Generally, nothing else may be enclosed in the envelope.	No provision	No provision	Permits the following enclosures: (a) a check, (b) a letter explaining why no check is enclosed, or (c) a statement of the taxpayer's account The envelope and each enclosure must state "Important Tax Return Document Enclosed " *Effective date* —Information returns required to be filed after December 31, 1986

Item	Present Law	President's Proposal	House Bill	Senate Amendment
D. Tax Shelter Administration 1. Tax shelter user fee (sec. 531 of the Senate amendment)	The cost of administering the tax law with respect to tax shelters is paid as part of the overall IRS budget, which is funded from general revenues. This cost is approximately $165 million annually, and includes audits, examination, appeals, litigation, and criminal investigation. No specific fee is imposed on tax shelters to offset this cost.	No provision	No provision	Requires taxpayers who claim on tax returns cumulative net losses (plus three times the value of cumulative tax credits) that exceed cumulative actual cash invested in a tax shelter to pay a user's fee of 1 percent of the losses claimed and 3 percent of the credits claimed. (These percentages are set at a level that will raise revenue approximately equal to the IRS cost of administering the law with respect to tax shelters.) "Tax shelter" is defined as: (a) any enterprise required to register with a Federal or State securities agency (other than a C corporation), (b) any syndicate more than 35 percent of the losses of which are allocable to limited partners or limited entrepreneurs, or (c) any plan or entity the principal purpose of which is to avoid or evade Federal income taxes. (These definitions are currently used in the Code to determine when tax shelters may deduct items.) This user fee is non-deductible. Additionally, a penalty equal to the user fee is imposed if the taxpayer does not pay the user fee with the tax return. *Effective date.*—Returns filed on or after January 1, 1987.
2. Tax shelter registration (sec. 532 of the Senate amendment)	Tax shelter organizers are required to register with the IRS tax shelters they organize, develop, or sell. A tax shelter is any investment for which the ratio of the deductions plus 200 percent of the credits to the cash actually invested is projected to be greater than 2 to 1. The investment also must be subject to Federal or State securities requirements or be privately placed with 5 or more investors.	No provision.	No provision.	Multiply the value of the credits by 300 percent, instead of 200 percent (to conform to individual tax rate changes). *Effective date.*—Same as individual tax rate changes.

Item	Present Law	President's Proposal	House Bill	Senate Amendment
3. Penalty for failure to register a tax shelter (sec. 533 of the Senate amendment)	Specified tax shelters are required to register with the IRS and obtain a tax shelter identification number. The penalty for failure to register a tax shelter with the IRS is $10,000 or, if less, one percent of the aggregate amount invested in the tax shelter (but in no event less than $500).	No provision	No provision	Increases the penalty to the greater of one percent of the aggregate amount invested in the tax shelter or $10,000 *Effective date*.—Date of enactment.
4. Penalty for failure to report the tax shelter identification number (sec. 534 of the Senate amendment)	If a taxpayer invests in a tax shelter that has a tax shelter identification number, the taxpayer is required to include that number on the tax return. The penalty for failure to do so is $50, unless the failure is due to reasonable cause.	No provision	No provision	Increases the penalty to $250 *Effective date*.—Returns filed after date of enactment
5. Penalty for failure to maintain lists of investors (sec. 535 of the Senate amendment)	Organizers and sellers of specified tax shelters are required to maintain lists of investors. The penalty for failure to do so is $50 for each name missing from the list, unless the failure is due to reasonable cause, up to a maximum of $50,000 per year	No provision	No provision.	Increases the penalty to $100 per name omitted, up to a maximum of $100,000 per year. *Effective date*.—Date of enactment
6. Tax shelter interest (sec. 536 of the Senate amendment)	If a taxpayer owes interest due to a substantial underpayment of tax (more than $1,000) attributable to a tax-motivated transaction (such as a tax shelter), interest is computed at 120 percent of the generally applicable rate	No provision.	No provision	Increases the rate to 200 percent of the otherwise applicable rate. *Effective date*.—Interest accruing after December 31, 1986.

Item	Present Law	President's Proposal	House Bill	Senate Amendment
E. Estimated Tax Payments **1. Individuals (sec. 1311 of the House bill and sec. 561 of the Senate amendment)**	Individuals owing tax must make estimated tax payments (Income taxes withheld from wages are considered to be estimated tax payments.) These payments must equal at least the lesser of 100 percent of last year's tax liability or 80 percent of the current year's tax liability	No provision.	Requires that individuals must make estimated tax payments that equal at least the lesser of 100 percent (as under present law) of last year's tax liability or 90 percent (rather than 80 percent) of the current year's tax liability *Effective date.*—Payments due for taxable years beginning on or after January 1, 1986.	Same as House bill *Effective date* —Payments due for taxable years beginning on or after January 1, 1987
2. Excise tax on private foundation investment income (sec. 561 of the Senate amendment)	Private foundations must pay an excise tax on their net investment income. The tax is paid when the tax return is filed. Corporations are required to make quarterly estimated tax payments of corporate income taxes; failure to do so is subject to a penalty	No provision	No provision.	Quarterly estimated payments must be made of this excise tax, under the same rules that apply to corporate income taxes. (Floor amendment by Senator Matsunaga, adopted by voice vote.) *Effective date* —Taxable years beginning after December 31, 1986.
3. Unrelated business income tax (sec. 565 of the Senate amendment)	Tax-exempt organizations that operate unrelated businesses are required to pay tax on the income from the unrelated business. The tax is paid when the tax return is filed. Corporations are required to make quarterly estimated tax payments of corporate income taxes; failure to do so is subject to a penalty.	No provision.	No provision.	Quarterly estimated payments must be made of the unrelated business income tax, under the same rules that apply to corporate income taxes (Floor amendment by Senator Kennedy, adopted by voice vote) *Effective date* —Taxable years beginning after December 31, 1986
F. Tax Litigation and Tax Court **1. Awards of attorneys' fees in tax cases (sec. 1315 of the House bill and sec. 541 of the Senate amendment)**	(a) Attorneys' fees may be awarded in tax cases to private parties who prevail on the issues litigated if the taxpayer proves that the Government's position was unreasonable. Awards are limited to $25,000. This provision expired with respect to court proceedings commenced after December 31, 1985.	(a) No provision.	(a) Extends the present-law sunset date until December 31, 1989 *Effective date.*—Actions commencing after December 31, 1985, and before January 1, 1990.	(a) The authorization of attorneys' fees and other court costs in tax cases is made permanent, with the following modifications: (1) If it is determined that the taxpayer prevailed in the tax litigation, the burden rests on the Government to show that its position was substantially justified or that special circumstances exist that make an award of litigation costs unjust. (2) The "substantially justified" standard applies to the administrative action or inaction by the Government on which such proceeding is based. (3) No award is allowed to a prevailing party who unreasonably protracted the proceedings;

Item	Present Law	President's Proposal	House Bill	Senate Amendment
1. Awards of attorneys' fees in tax cases—Cont.				(4) The $25,000 cap is eliminated (as under present law, recoverable costs would not include costs of the administrative process); and (5) In lieu of the cap, limits are imposed on hourly charges by attorneys and expert witness fees recoverable under the provision *Effective date.*—Actions commencing after December 31, 1985 However, no payments may be made as a result of this provision before October 1, 1986
	(b) On the basis of advise from GAO, no amounts have been disbursed to pay Tax Court awards of attorneys' fees	(b) No provision.	(b) Authorizes funding of attorneys' fee awards out of source used in non-tax cases. *Effective date.*—Actions commenced after February 28, 1983.	(b) Same as House bill
	(c) There is no authority for a court to assess all or a portion of an attorneys' fee award against an IRS employee.	(c) No provision	(c) Gives courts the authority to assess all or a portion of an attorneys' fee award against an IRS employee if the proceeding results from an arbitrary or capricious action of the employee. *Effective date.*—Actions commencing after December 31, 1985, and before January 1, 1990	(c) No provision
	(d) There is no requirement that Treasury report to Congress annually on attorneys' fees awards.	(d) No provision	(d) Requires an annual report from Treasury to Congress on attorneys' fees awards *Effective date.*—Reports required for 1985 through 1989.	(d) No provision.
2. Exhaustion of administrative remedies (sec. 1316(a) of the House bill)	A taxpayer may go directly to Tax Court without requesting review by the administrative appeals office within the IRS. After the case is opened in the Tax Court, it is sent to the IRS appeals office for settlement. Many of these cases are then settled without significant involvement by the Court.	No provision	Authorizes the Tax Court to impose a $120 penalty if the taxpayer has not used reasonable efforts to resolve his case administratively before going to court *Effective date.*—Cases filed in the Tax Court after January 1, 1987	No provision.
3. Report to Congress on Tax Court inventory (sec. 1316(d) of the House bill)	No provision requires an annual report from the Tax Court and the IRS on the Tax Court inventory	No provision.	Requires the Tax Court and IRS to report to Congress annually on Tax Court inventory and measures taken to close cases more efficiently. *Effective date.*—Reports required annually beginning after 1985.	No provision

1. Tax Court provisions *a. Tax Court practice fee (sec. 542 of the Senate amendment)*	(a) The Tax Court imposes a $25 application fee prior to admission to practice before the Court No fee is imposed after the application fee has been paid The Tax Court rules authorize the Court to initiate disciplinary proceedings against practitioners who appear before it The Court is authorized to appoint outside counsel to pursue disciplinary matters	(a) No provision	(a) No provision	(a) Authorizes the Tax Court to impose a periodic registration fee on practitioners admitted to practice before it The Tax Court is to establish the level of the fee and the frequency of its collection, but the fee may not exceed $30 per year These funds would be available to the Tax Court to pay outside counsel engaged by the Court to pursue disciplinary matters *Effective date.*—January 1, 1987.
b. Provide Tax Court with jurisdiction over late payment penalties (sec. 543 of the Senate amendment)	(b) Provides a penalty if the taxpayer does not pay the taxes shown on the tax return The Tax Court has held that it does not have jurisdiction over this penalty because it does not relate to a deficiency.	(b) No provision	(b) No provision.	(b) Provides the Tax Court with jurisdiction over this late payment penalty *Effective date.*—Date of enactment
c. Provide Tax Court with assistance of U.S. Marshals (sec. 544 of the Senate amendment)	(c) U.S Marshals provide courtroom security, among other duties. It is not clear that the Tax Court has the authority to request the assistance of U.S. Marshals, because the Tax Court is an Article I (rather than Article III) court	(c) No provision	(c) No provision	(c) Authorizes that U.S. Marshals be available to the Tax Court in the same manner that they are available to other courts *Effective date*—Date of enactment.
d. Salary and travel expenses of Special Trial Judges (sec. 545 of the Senate amendment)	(d)(1) The Chief Judge of the Tax Court is authorized to appoint Special Trial Judges, who assist in the work of the Court. The Code provides that their salary is determined by the procedures relating to the Commission on Executive, Legislative, and Judicial Salaries The Executive Order implementing that provision fails to include Special Trial Judges	(d)(1) No provision.	(d)(1) No provision.	(d)(1) Provides that the salary of Special Trial Judges is 90 percent of the salary of Tax Court judges (This is historically the level of their salary)
	(2) Prior to January 17, 1985, Special Trial Judges were entitled to reimbursement for travel expenses on the same basis as other Federal judges On that date, the Comptroller General determined that they were entitled only to reduced reimbursement pursuant to the Federal Travel Regulations	(2) No provision	(2) No provision.	(2) Provides that Special Trial Judges are to be reimbursed for travel expenses at the same level as other judges *Effective date*—Date of enactment
e. Tax Court Judges' retirement provisions (Sec. 546 of the Senate amendment)	(e) District Court judges meeting age and longevity of tenure requirements may resign, engage in the practice of law, and continue to receive retirement pay Tax Court judges who resign after meeting these age and longevity of tenure requirements, but who engage in the practice of Federal tax or contract law, forfeit retirement pay. Forfeiture also occurs if a retired (rather than resigned) judge accepts a government position, whether compensated or not.	(e) No provision	(e) No provision.	(e) Permits Tax Court judges to resign, practice law, and continue to receive retirement pay in the same manner that District Court judges currently are permitted to do Provides that forfeiture of retired pay by a retired judge who accepts a government position only applies if the position is compensated *Effective date*—Date of enactment

Item	Present Law	President's Proposal	House Bill	Senate Amendment
[illegible]. Tax Administration Trust Fund (sec. 558 of the Senate amendment)	The IRS is responsible for administering almost all of the tax laws. The cost of the entire IRS is funded through annual appropriations of general revenues. For FY 1986, it will cost approximately $3.9 billion to operate the IRS. Approximately $7 billion is received annually in interest and penalties.	No provision	No provision	Establishes a Tax Administration Trust Fund, funded by all interest and penalties received under the Code. The following amounts may be utilized by the IRS without additional appropriations: [In millions] FY 1987 $4,340 FY 1988 $4,647 FY 1989 $4,920 FY 1990 $4,978 FY 1991 $5,033 This is an increase averaging $0.9 billion per year during the five years the Trust Fund is effective, measured against FY 1986 levels. The increase in spending is targeted to examination, collection, and other increased compliance measures. *Effective date.*—October 1, 1986. The Trust Fund expires on September 30, 1991.

Item	Present Law	President's Proposal	House Bill	Senate Amendment
II. Tax Administration Provisions 1. Suspend statute of limitations during prolonged dispute with third parties (sec. 556 of the Senate amendment)	There is generally a three-year statute of limitations on tax assessments and prosecutions, except in cases of fraud, failure to file, or a sizeable understatement of income. The statute continues to run even if the IRS must obtain records held by third parties. If the IRS must litigate to obtain access to the third party records, the statute of limitations can expire prior to final determination as to the availability of the records.	No provision	No provision	If third party records are not produced within six months of an administrative summons, the statute of limitations is suspended until the issue is resolved. *Effective date.*—Date of enactment.
2. Authority to rescind statutory notice of deficiency (sec. 1321 of the House bill and sec. 551 of the Senate amendment)	Once the IRS has issued a statutory notice of deficiency, the IRS does not have the authority to withdraw the notice; only a Tax Court decision can alter its effect.	No provision	Where the IRS and the taxpayer mutually agree, a statutory notice of deficiency may be rescinded. *Effective date.*—Statutory notices of deficiency issued on or after January 1, 1986.	Same as House bill. *Effective date.*—Statutory notices of deficiency issued on or after date of enactment.
3. Authority to abate interest due to errors or delay by the IRS (sec. 1322 of the House bill and sec. 552 of the Senate amendment)	The IRS does not have the authority to abate interest charges where the additional interest has been caused by IRS errors and delays, except in cases of certain IRS math errors.	No provision.	In cases where an IRS official either fails to perform a ministerial act in a timely manner or makes an error in performing a ministerial act, the IRS has the authority to abate the interest attributable to such delay. No aspect of the delay can be attributable to the taxpayer. The interest abatement only applies to the period of time attributable to the failure to perform the ministerial act, and only after the taxpayer has been contacted by the IRS. The IRS is required to exercise this authority to abate interest in instances in which it issues an erroneous refund check, except where the taxpayer has caused the overstated refund to occur, or where an erroneous refund check exceeds $1 million. *Effective date.*—Interest accruing with respect to deficiencies or payments for taxable years beginning in or after 1982.	Same as House bill, except that no significant aspect of the delay can be attributable to the taxpayer.
4. Suspension of compounding where interest on deficiency is suspended (sec. 1323 of the House bill and sec. 553 of the Senate amendment)	The running of interest is suspended where the IRS fails to issue the taxpayer a bill stating how much the taxpayer owes within 30 days of concluding an audit. This rule does not apply to the compounding of interest on previously accrued interest.	No provision	Compounded interest on the previously accrued interest is suspended when the underlying interest is also suspended. *Effective date.*—Interest accruing in taxable periods after December 31, 1985.	Same as House bill. *Effective date.*—Interest accruing after December 31, 1982.

Item	Present Law	President's Proposal	House Bill	Senate Amendment
5. Exemption from levy for service-connected disability payments (sec. 1324 of the House bill and sec. 551 of the Senate amendment)	Various payments, such as unemployment benefits, workmen's compensation, and a minimum amount of ordinary wages, are exempt from IRS levy. Military service-connected disability payments are not, however, exempt from levy.	No provision	Military service-connected disability payments are exempt from levy. *Effective date.*—Payments made after December 31, 1985	Same as House bill. *Effective date.*—Payments made after December 31, 1986.
6. Modification of administrative rules applicable to forfeiture (sec. 1325 of the House bill)	The IRS can seize property that is used in violating the provisions of the Internal Revenue laws. If the amount of personal property seized is valued at $2,500 or less, the IRS may use administrative procedures to forfeit the property and sell it without judicial action, after both appraisal and notice to potential claimants.	No provision	The IRS may administratively sell up to $100,000 of personal property used in violation of the Internal Revenue laws. Such sale would require both an appraisal to determine value and notice to potential claimants. Potential claimants can require a court proceeding by posting a $2,500 bond. *Effective date.*—January 1, 1986	No provision
7. Certain recordkeeping requirements (sec. 1326 of the House bill and sec. 555 of the Senate amendment)	In general, law enforcement officers are not subject to the substantiation rules and the income and wage inclusion rules for specified use of a law enforcement vehicle. IRS special agents are not, however, included within the term "law enforcement officers."	No provision.	Use of an automobile by a special agent of the IRS is treated in the same manner as use of an automobile by an officer of any other law enforcement agency. *Effective date.*—Date of enactment	Same as House bill. *Effective date.*—January 1, 1985
8. Disclosure of returns and return information to certain cities (sec. 557 of the Senate amendment)	Disclosure of returns and return information can be made to States for tax administration purposes provided that safeguards against disclosure are ensured. Disclosure to cities is not permitted.	No provision.	No provision	Any city with a population in excess of 2 million that imposes an income or wage tax may, if the Secretary so provides, receive returns and return information for the same purposes and with the same safeguards as are required of a State under present law. *Effective date.*—Date of enactment
9. Regulatory Flexibility Act applied to IRS (sec. 567 of the Senate amendment)	The Regulatory Flexibility Act requires that an analysis of the impact of rules and regulations (other than interpretative regulations) on small businesses be performed. Treasury's position is that most IRS rules and regulations are interpretative.	No provision	No provision	Applies the Regulatory Flexibility Act to all rules and regulations prescribed by the Treasury. (Floor amendment by Senator Sasser, adopted by voice vote.) *Effective date.*—Date of enactment

Item	Present Law	President's Proposal	House Bill	Senate Amendment
. Modification of Employee Withholding Allowance Forms (sec. 1335 of the House bill and sec. 562 of the Senate amendment)	Employees can claim withholding allowances on Form W-4. That form determines how much in Federal taxes is withheld from the employee's wages. Withholding allowances can be claimed for personal exemptions, tax credits, and estimated deductions (such as itemized deductions). That form remains in effect until the taxpayer changes or revokes it	No provision	Modifies withholding schedules to better approximate the newly effective rate schedules *Effective date.*—January 1, 1986	Same as House bill In addition, if an employee does not file a revised Form W-4 before January 1, 1988, the employer must withhold income taxes from the employee's wages as if the employee claimed either one allowance (if single) or two allowances (if married). *Effective date.*—January 1, 1987
Report on Return-Free Tax System (sec. 1315 of the House bill and sec. 563 of the Senate amendment)	Individuals whose income exceeds specified levels must file income tax returns each year. Generally, these returns must be filed by April 15, unless the taxpayer receives an extension of time to file.	Provide the IRS with the authority to implement a return-free system for individuals. Taxpayers who meet certain criteria (relating to the complexity of their returns) would be offered the option of not filing an income tax return. Instead, the IRS would prepare the return and compute the tax liability of the taxpayer. The IRS would do this using wage reports currently filed with the Social Security Administration and information returns currently filed with the IRS. The IRS would send the taxpayer a report stating the Service's calculation of the taxpayer's tax liability. The taxpayer would be free to challenge the Service's calculation of tax *Effective date.*—Not specified in President's proposal	Requires a report from IRS to the House Ways and Means and Senate Finance Committees. Report is to state (1) Who can participate in proposal and who cannot; (2) How the proposal would be phased in; (3) What resources (computers, staff, etc.) are needed; and (4) The types of changes to the Code that would inhibit or enhance the use of the return-free system The IRS is also to consider whether an in-house test of the proposal (not involving taxpayers) would be beneficial *Effective date.*—Report due six months after the date of enactment	Same as House bill

Item	Present Law	President's Proposal	House Bill	Senate Amendment
\. Exchanges and Rentals of Membership Lists of Certain Tax-Exempt Organizations (sec. 1104 of the House bill and sec. 1702 of the Senate amendment)	Charitable and other tax-exempt organizations are subject to a tax on income from an unrelated trade or business (the UBIT), i.e., where the conduct of the business is not substantially related to the exempt functions of the organization The U.S Court of Claims has held that income received by the Disabled American Veterans from other exempt organizations and commercial businesses for the use of its mailing lists is subject to the UBIT	No provision.	The bill provides an exemption from the UBIT, in the case of certain tax-exempt organizations eligible to receive charitable contributions, for income from exhanges or rentals of membership or donor mailing lists with or to other such organizations *Effective date.*—Exchanges and rentals of lists after the date of enactment	Same as House bill
. Distribution of Low-Cost Articles by Charities (sec. 1404 of the House bill)	Charitable and other tax-exempt organizations are subject to a tax on income from an unrelated trade or business (the UBIT), i e., where the conduct of the business is not substantially related to the exempt functions of the organization. Under Treasury regulations, the UBIT does not apply where an organization "sends out low cost items incidental to the solicitation of charitable contributions." The regulations do not provide a definition of "low cost articles."	No provision.	The bill codifies the regulation providing an exemption from the UBIT, in the case of certain tax-exempt organizations eligible to receive charitable contributions, for income from certain distributions of low-cost articles incidental to soliciting charitable contributions. The bill also defines "low cost articles" as any article with a cost not in excess of $5 (indexed for inflation). *Effective date* —Distributions of low cost articles after the date of enactment.	No provision
:. Expansion of UBIT Exemption for Certain Trade Show Income (sec. 1715 of the Senate amendment)	Charitable and other tax-exempt organizations are subject to a tax on income from an unrelated trade or business (the UBIT), i e., where the conduct of the business is not substantially related to the exempt functions of the organization An exemption from the UBIT is provided for income derived by trade associations (sec. 501(c)(6)) or labor unions (sec. 501(c)(5)) from qualified trade show and convention activities at which members of the sponsoring organization sell products or services (sec. 513(d)).	No provision.	No provision.	The section 513(d) UBIT exemption is expanded to cover (1) qualified trade shows or conventions at which suppliers to the sponsoring organization's members sell products or services, and (2) qualified trade show and convention activities of charitable organizations (sec. 501(c)(3)) and social welfare organizations (sec. 501(c)(4)) (Floor amendment by Sen Matsunaga, adopted by voice vote) *Effective date.*—Qualified trade show or convention activities conducted in taxable years beginning after the date of enactment

Item	Present Law	President's Proposal	House Bill	Senate Amendment
D. Tax Exemption for Certain Title-Holding Companies (sec. 1706 of the Senate amendment)	A corporation organized to hold title to property, and to distribute the income therefrom to one or more related tax-exempt organizations, may itself be tax exempt. The IRS has taken the position that such a title-holding company is not tax exempt if two or more of its parent organizations are unrelated. An exempt organization's income from debt financed property (other than real estate) generally is treated as unrelated business income, which is subject to tax. An exception is provided for certain pension plans and educational organizations	No provision	No provision.	Tax-exempt status is provided for a corporation or trust that (a) has no more than 35 shareholders, (b) has only one class of stock or beneficial interest, and (c) is operated for the exclusive purpose of holding title to property and distributing income to eligible shareholders. The term eligible shareholders includes a qualified pension plan; a governmental pension plan; any State or political subdivision, or any tax-exempt charitable organizatinn (sec. 501(c)(3)). The exception from the unrelated business income tax imposed on debt-financed property is extended to title-holding companies. In addition, income derived by eligible shareholders from title holding companies generally is not treated as income from debt-financed property *Effective date.*—Taxable years beginning after 1986.
E. Divestiture Exemption for Certain Grandfathered Business Holdings of Private Foundations (sec. 1705 of the Senate amendment)	If on May 26, 1969, a private foundation (together with disqualified persons) had business holdings exceeding permitted limitations (generally, 20 percent), the amount of foundation/disqualified person holdings must be reduced in two phases (Code sec. 4943). In general, a disqualified person is a substantial contributor to the foundation, a family member of a substantial contributor, or a substantial owner of an entity that is a substantial contributor If the 1969 holdings exceeded 95 percent, the foundation has a 20-year period (i.e., until May 26, 1989) to reduce the combined holdings to 50 percent. Within 15 years after the first-phase deadline, the holdings must be reduced, in certain cases, to 35 percent; in addition, the foundation itself may not hold more than 25 percent of the voting stock, dependent on whether disqualified persons own more than two percent	No provision.	No provision	The 20-year grandfather exception for certain excess business holdings acquired prior to May 27, 1969, is made permanent if— (1) the management of the foundation and the management of the business enterprise are sufficiently unrelated, (2) no disqualified person who was not a foundation manager on May 6, 1986, can become a foundation manager after that date, (3) no disqualified person receives compensation (other than reasonable directors' fees) from both the foundation and the business enterprise, (4) the foundation continues to meet the charitable payout rules of present law, and (5) the foundation and any disqualified persons comply with the section 4943 rules applicable to any holdings in the enterprise acquired after May 26, 1969 *Effective date.*—Date of enactment

Item	Present Law	President's Proposal	House Bill	Senate Amendment
F. Reduction of Private Foundation Payout Requirement by Certain Costs of Hazardous Waste Removal (sec. 1712 of the Senate amendment)	To avoid penalty excise taxes, a private nonoperating foundation annually must make expenditures or grants for charitable purposes in an amount (the "distributable amount") equal to five percent of the fair market value of its investment assets (sec. 4942).	No provision.	No provision	The otherwise applicable distributable amount for the James Graham Brown Foundation is reduced by certain costs paid or incurred by the Foundation for removal or remedial action with respect to a hazardous substance released at a facility owned or operated by the Foundation. (Floor amendment by Sens McConnell and Ford, adopted by voice vote.) *Effective date*.—Taxable years beginning after December 31, 1982.
G. Exception to Membership Organization Deduction Rules (sec. 1710 of the Senate amendment)	A membership organization generally may deduct expenses relating to the furnishing of goods or services to members only from income derived from members or from transactions with members (sec. 277). This rule does not apply to certain financial institutions, insurance companies, securities or commodities exchanges, or certain other organizations.	No provision	No provision.	Membership organizations engaged primarily in the gathering and distribution of news to their members for publication are permitted to deduct expenses relating to the furnishing of goods and services to members from income whether or not derived from members (Floor amendment by Sen. Moynihan, adopted by voice vote.) *Effective date*.—Date of enactment.
H. Tax-Exempt Status for Technology Transfer Organization (Sec. of the Senate amendment)	In November, 1985, the U.S. Tax Court denied tax-exempt status under section 501(c)(3) to the Washington Research Foundation, a nonprofit organization formed to assist the transfer of technology from universities and tax-exempt research institutions to the private sector. The Tax Court held that the organization was not exclusively operated for charitable purposes because its major activity of providing patenting and licensing services was commercial in nature.	No provision	No provision.	An organization that transfers technology from universities and scientific research organizations to the private sector is treated as a tax-exempt charitable organization if it meets certain requirements, including that it was incorporated on July 20, 1981. The intended beneficiary of this provision is the Washington Research Foundation. (Floor amendment by Sen. Gorton, adopted by voice vote.) *Effective date*.—Date of enactment

Item	Present Law	President's Proposal	House Bill	Senate Amendment
A. Targeted Jobs Tax Credit (sec. 282 of the House bill and sec. 1708 of the Senate amendment)	A tax credit is available on an elective basis to employers of individuals from nine targeted groups, i.e., individuals who are recipients of payments under means-tested transfer programs, economically disadvantaged (as measured by family income), or disabled. The credit generally equals 50 percent of the first $6,000 of qualified first year wages and 25 percent of the first $6,000 of qualified second year wages. A credit equal to 85 percent of up to $3,000 of wages of any disadvantaged summer youth employee also is allowed. The employer's deduction for wages must be reduced by the amount of the credit. Under present law, the credit does not apply with respect to targeted-group individuals who begin work for the employer after December 31, 1985.	No provision.	The targeted jobs credit is extended for two additional years with several modifications: the credit for second-year wages is eliminated, the first-year credit is reduced to 40 percent of the first $6,000 of qualified first-year wages (except in the case of disadvantaged youth employees), the credit for wages paid to an individual who works for the employer for fewer than 14 days is eliminated, and the authorization for appropriations for administrative and publicity expenses is extended through fiscal year 1987. *Effective date.*—Applies for individuals beginning work for the employer after 1985 and before 1988.	Same as House bill, except that (1) the credit is extended for three years (together with authorization for administrative and publicity expenses), (2) a 50 percent credit is retained for first-year wages, and (3) the credit is not available for individuals who work for less than 90 days (14 days in the case of qualified summer youth employees) or 120 hours (20 hours in the case of qualified summer youth employees). *Effective date.*—Applies for individuals beginning work for the employer after 1985 and before 1989.
B. Olympic Trust Fund and Excise Tax (sec. 1103 of the House bill)	No provision. (Various earmarked excise taxes are dedicated to specific trust funds.)	No provision.	*(1) Excise tax.*—A 10-percent excise tax is imposed on amounts paid for U.S. television and radio broadcast rights for Olympic games. *Effective date.*—Amounts paid after November 22, 1985, other than pursuant to binding contracts in effect on that date. Any inconsistent U.S. treaty provision is overriden. *(2) Olympic Trust Fund.*—An Olympic Trust Fund is established in the Treasury to receive amounts from the new excise tax. Trust fund monies, less related Treasury administrative expenses are available to be paid to the U.S. Olympic Committee for Olympic-related expenses. *Effective date.*—Date of enactment.	No provision.
C. Collection of Diesel Fuel Excise Tax (sec. 1351 of the House bill and sec. 571 of the Senate amendment)	An excise tax of 15 cents per gallon is imposed on the sale of diesel fuel for use in a diesel-powered highway vehicle. This tax is collected at the retail level. The excise tax on gasoline (9 cents per gallon) is imposed and collected at the manufacturer's level. Collection of this tax may be deferred to the last sale before retail, however, if all parties are registered with the IRS.	No provision.	The diesel fuel excise tax for highway vehicles may be imposed on the sale from the wholesaler to the retailer of the fuel (or by the manufacturer where the sale is direct to the retailer), at the election of a "qualified retailer." *Effective date.*—Sales of diesel fuel (for use in highway vehicles) after the first calendar quarter beginning more than 60 days after date of enactment.	Same as House bill. (Floor amendment by Sen. Stevens, adopted by voice vote.)

Item	Present Law	President's Proposal	House Bill	Senate Amendment
D. Social Security and FUTA Provisions				
1. Allow ministers to reelect social security coverage (sec. 1882A of the Senate amendment)	The Federal Insurance Contributions Act (FICA) imposes separate payroll taxes on employers and employees equal to a percentage of wages paid as remuneration for employment, subject to certain exceptions. For self-employed individuals, a similar tax is imposed on self-employment income under the Self-Employment Contributions Act (SECA). These taxes are used to fund the social security programs of Old-Age and Survivors' Insurance, Disability Insurance, and Hospital Insurance. Generally, employees who are ministers of a church in the exercise of their ministry or members of religious orders (other than members subject to a vow of poverty) in the exercise of duties required by the order are treated as self-employed individuals for purposes of social security taxes. However, such individuals who are conscientiously, or because of religious principles, opposed to participation in a public insurance system may elect to be exempt from self-employment taxes and credit under social security (on earnings for services as ministers or members of religious orders) by filing an irrevocable one-time application to that effect within two years of beginning their ministry.	No provision.	No provision.	A one-time irrevocable election into social security coverage is allowed for ministers who previously elected out of social security. The amendment allows a period of two years in which to elect back into social security. A minister making the election back would become subject to SECA tax and his or her earnings would be credited for benefit purposes. In addition, administrative provisions are adopted to advise ministers proposing to elect out of social security in the future that the election is limited to individuals with conscientious or religious opposition to participation. (Floor amendment by Senator Armstrong, adopted by voice vote.) *Effective date.*—Taxable years beginning on or after the date of enactment.
2. Common paymaster rule for FICA and FUTA taxes (sec. 1721 of the Senate amendment)	Pursuant to the Federal Insurance Contributions Act (FICA), a payroll tax is imposed on every employer with respect to each individual in his employ. The tax imposed is a percentage (currently 7.15 percent) of the base amount of wages paid to the employee (currently $42,000). Similarly, the Federal Unemployment Tax Act (FUTA) imposes a tax on every employer with respect to each individual he employs. The tax imposed is 0.8 percent on the first $7,000 of wages. In general, when the same individual is employed by two or more employers, each is subject to the FICA and FUTA tax on the base income of the individual. An exception applies where two or more related corporations concurrently employ the same individual and compensate him through a common paymaster which is one of the corporations. In such case, the tax is determined as though the individual has only one employer, the common paymaster. As a result, the tax is applied against only a single base amount of wages.	No provision.	No provision.	The common-paymaster rule is applied in the case where the same employee works for a corporation and its related partnership for purposes of collection of FICA and FUTA taxes. The same test for determining related corporations is employed to determine whether a partnership is related. (Floor amendment by Sen. Moynihan, adopted by voice vote.) *Effective date.*—Wages paid or incurred after December 31, 1986.

Item	Present Law	President's Proposal	House Bill	Senate Amendment
3. Agricultural wages subject to FUTA (sec. 707 of the Senate amendment)	FUTA tax applies to wages of workers in agricultural operations with a payroll of at least $20,000 in any calendar quarter, or with 10 or more employees in 20 weeks of the year	No provision	No provision	The quarterly payroll threshold at which agricultural wages are covered under FUTA is increased from $20,000 to $40,000 (See, also IV.A 9) *Effective date* Wages paid after September 30, 1986
4. FUTA for certain Indian tribes (sec. 1881A of the Senate amendment)	Generally, Indian tribes are treated as any other employer and are subject to Federal unemployment tax (FUTA). No exception is provided if unemployment compensation coverage is denied by the State in which the Indian tribes have been denied unemployment compensation coverage by the State of Colorado and are not required to pay State unemployment compensation taxes	No provision	No provision	FUTA taxes assessed against certain Indian tribes for the period of time they are refused unemployment compensation coverage by the State are excused (Floor amendment by Sen Armstrong, adopted by voice vote.) *Effective date.*—Services performed before, on, or after the date of enactment, and before January 1, 1988.
5. Treatment of certain technical personnel (sec. 1717 of the Senate amendment)	Section 530 of the Revenue Act of 1978, as amended, provides that taxpayers who had in the past a reasonable basis (such as past industry practice) for not treating workers as employees could continue such treatment, under certain circumstances, without incurring employment tax liabilities	No provision	No provision	Section 530 of the Revenue Act of 1978 does not apply to services provided pursuant to an arrangement between the taxpayer and another organization whereby the individual provided services as an engineer, designer, drafter, computer programmer, systems analyst, or other similarly skilled worker engaged in a similar line of work for such other organization (Floor amendment by Sen Packwood on behalf of Sen Moynihan, adopted by voice vote.) *Efffective date* —Services rendered after the date of enactment
6. Payroll tax deposits (sec. 636 of the Senate amendment)	Unless the Code specifies the mode or time for collecting a tax, it is to be collected as provided in Treasury regulations. The Code does not specify the mode or time for collecting (a) income taxes withheld from employees or (b) the employee or employer FICA taxes Consequently, the mode and time for collecting these taxes is specified in Treasury regulations. Under these regulations, if the aggregate amount of undeposited taxes reaches $3,000 or more at the end of any one-eighth-monthly period, the employer must deposit the taxes within three banking days of the close of the one-eighth-monthly period	No provision	No provision	Increases from $3,000 to $5,000 the amount of undeposited payroll taxes an employer may aggregate before the one-eighth monthly deposit rule becomes effective *Effective date* —Months beginning after December 31, 1986

Item	Present Law	President's Proposal	House Bill	Senate Amendment
C. Budget-Related Provisions				
1. Revenues for budget purposes (sec. 1718 of the Senate amendment)	No provision	No provision	No provision.	Revenue windfalls in fiscal years 1986 and 1987 that are attributable to provisions of the Tax Reform Act of 1986 shall not be taken into account for determining total budget revenues for the fiscal years 1986-1989. A revenue windfall is any increase in revenues over present law. For fiscal years 1988 and 1989, any revenue shortfall attributable to the Tax Reform Act of 1986 shall not be taken into account to the extent that it exceeds the fiscal year 1986 and 1987 windfalls. This provision applies for determining Budget Act points of order and for purposes of sequestrations under the "Gramm-Rudman-Hollings" budget legislation. (Floor amendment by Sens. Domenici, Gramm, Rudman, and Hollings, adopted by voice vote.)
2. Budget revenue fluctuations (sec. 1720 of the Senate amendment)	No provision.	No provision.	No provision.	The conference committee on H.R. 3838 should report Federal tax reform legislation that produces a revenue path with minimal revenue fluctuations. (Sense of the Senate floor amendment by Sen. Chiles, adopted by voice vote.)
D. Tax Code Revisions				
1. Reference to Internal Revenue Code (sec. 2 of the House bill)	The current tax code (26 U.S.C.) is referred to as the "Internal Revenue Code of 1954" (as amended). The 1954 Code (sec. 7852(d)) states that no provision of the Code is to apply where it would be contrary to any treaty obligation of the United States in effect on the date of enactment of the 1954 Code (August 16, 1954).	No change in Code reference.	Recodifies the Code as the "Internal Revenue Code of 1985" (i.e., reenacts the provisions of the 1954 Code—as in effect on the date of enactment of the bill—together with amendments as made by the bill). Restates that the 1985 Code does not override existing U.S. treaty provisions in effect on the date of enactment of the 1954 Code or in effect on the date of enactment of the bill.	No change in Code reference.
2. Tax reform moratorium (sec. 1719 of the Senate amendment)	There have been three major tax revisions in the past five years, affecting many provisions of the Internal Revenue Code.	No provision.	No provision.	Expresses a Sense of the Congress that the provisions of the Internal Revenue Code that are added or amended in the current legislation remain unchanged for a period of at least five years from the date of enactment. (Floor amendment by Senator Mattingly, adopted by a vote of 50-47.)

Item	Present Law	President's Proposal	House Bill	Senate Amendment
Miscellaneous Provisions				
1. Foster care payments (sec. 1401 of the House bill)	A foster parent may exclude from gross income certain reimbursements for expenses of caring for a foster child placed in the home by a government agency or a State-licensed, tax-exempt child placement agency. To obtain the exclusion, the foster parents must account for all expenses incurred for each foster child in their care.	No provision	The present-law exclusion is modified to eliminate the requirement of detailed recordkeeping. *Effective date.*—Taxable years beginning after 1985.	No provision
2. Rules for spouses of Vietnam MIAs (sec. 1402 of the House bill and sec. 1701 of the Senate amendment)	Certain tax relief provisions applicable with respect to Vietnam MIAs and their spouses expired after 1982 (secs. 2(a)(3)(B), 692(b), 6013(f)(1), and 7508(b)).	No provision.	The bill reinstates and makes permanent the expired provisions relating to Vietnam MIAs, effective for taxable years beginning after 1982.	Same as House bill
3. Exempt certain reindeer income from tax (sec. 1716 of the Senate amendment)	Under the Reindeer Industry Act of 1937, the United States Government purchased all reindeer herds and improvements held by non-Alaskan natives. Since then, this property has been held in trust by the government for Alaskan natives who manage the reindeer herds. The Court of Appeals for the Ninth Circuit ruled in 1985 that reindeer-related income derived by Alaskan natives from herds is not exempt from Federal taxation absent a clear expression of such intent in the 1937 Act.	No provision	No provision	During the period of the trust, income derived directly from the sale of reindeer or reindeer products as provided in the 1937 Act is exempt from Federal income taxation. (Floor amendment by Sen. Stevens, adopted by voice vote.) *Effective date.*—Applies as if originally included in the related provision of the 1937 Act.
4. Information on special or unique treatment under tax bill (sec. 1711 of the Senate amendment)	There is no requirement that conference reports on tax legislation are to contain the name of taxpayers receiving special or unique treatment.	No provision	No provision	It is the sense of the Senate that the conference report on H.R. 3838 contain the name of any business concern or group receiving special or unique treatment, and the reason for and cost of such treatment. (Floor amendment by Sen. Metzenbaum, adopted by voice vote.)

Item	Present Law	President's Proposal	House Bill	Senate Amendment
5. Certain quality control studies for AFDC and Medicaid (sec. 1711 of the Senate amendment)	Under section 12301 of the Consolidated Omnibus Budget Reconciliation Act of 1985 (COBRA), the Department of Health and Human Services (HHS) and the National Academy of Sciences (NAS) are required to undertake a study of quality control measures in connection with the administration of the Aid to Families with Dependent Children and Medicaid programs HHS and NAS are required to report the results of their study to the Congress within one year of the date of enactment of COBRA (April 7, 1986). In addition, HHS is required to publish certain regulations relating to auch quality control measures within 18 months of the date of enactment of COBRA.	No provision.	No provision	HHS and NAS are required to report the results of their quality control study within one year after contracting to undertake the study The date by which HHS is required to publish the specified regulations is six months after the deadline for reporting the results of the quality control study to the Congress. (Floor amendment by Sen Evans, adopted by voice vote)

XVIII. TECHNICAL CORRECTIONS

(A separate document provides a comparative description of the differing technical corrections provisions of the House bill and the Senate amendment.)