[JOINT COMMITTEE PRINT]

DESCRIPTION OF MISCELLANEOUS TAX BILLS

SCHEDULED FOR A HEARING

BEFORE THE

SUBCOMMITTEE ON SELECT REVENUE MEASURES

OF THE

COMMITTEE ON WAYS AND MEANS

ON JUNE 26, 1980

PREPARED FOR THE USE OF THE

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BY THE STAFF OF THE

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INTRODUCTION

This pamphlet provides a description of miscellaneous tax bills scheduled for a public hearing on June 26, 1980, by the Ways and Means Subcommittee on Select Revenue Measures.

The first part of the pamphlet is a summary of the bills. This is followed by a more detailed description of the bills (in numerical order), including a description of present law, issues involved, an explanation of the provisions of the bills, effective dates, and estimated revenue effects.

I. SUMMARY

1. H.R. 4498—Mr. Weaver, and H.R. 5798—Messrs. Gudger, Bafalis, Barnard, Bevill, Chappel, Preyer, Jones (N.C.), and Andrews (N.C.)

Tax Treatment of Certain Timber Income and Reforestation Expenses

H.R. 4498

In general, the bill would (1) permit the Secretary of Agriculture to require a purchaser to perform work on national forest land cut over in lieu of making cash deposits for reforestation and forest improvement work, (2) impose the regular corporate rates on the taxable income of a corporation to the extent attributable to the export of softwood logs (i.e., deny capital gains treatment and DISC deferral benefits), (3) earmark for a Forest Services Nurseries Fund any increase in taxes attributable to the special taxation of taxable income from exports of softwood logs, and (4) provide a special income tax credit for specified percentages of a taxpayer's qualified forestry expenditures.

Under the bill, the amount of the special credit against income tax would be equal to the greater of (1) 25 percent of the qualified forestry expenditures paid or incurred by an eligible taxpayer during the taxable year as does not exceed $50,000 [1] (a maximum credit of $12,500) or (2) 10 percent of the total such expenditures for the taxable year.

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[1] The bill provides a $5,000 limit upon qualified forestry expenditures which are taken into account for purposes of the 25-percent credit. However, it is understood that the sponsor of the bill intended the amount to be $50,000 and that the $5,000 amount resulted from a typographical error. In addition, it is understood that on July 19, 1979, the Subcommittee on Forests of the House Committee on Agriculture approved the credit provisions in principle with the understanding that the 25-percent credit limitation would be based on $50,000 in qualified expenditures.

H.R. 5798

This bill would provide a special income tax credit for specified percentages of an eligible taxpayer's qualified forestry expenditures. The amount of the credit would be determined under the following table:

Qualified forestry expenditures	Rate (percent)	Maximum amount for each bracket
$1 to $5,000	75	$3, 750
$5,001 to $15,000	50	5, 000
$15,001 to $25,000	25	2, 500
$25,001 to $50,000	10	2, 500
Over $50,000	0	0
Total maximum amount per taxpayer		13, 750

2. H.R. 5719—Mr. Lederer

Tax Exemption for Proceeds of Certain Bingo Games

Under present law, amounts received by certain tax-exempt or political organizations from bingo games are not subject to income tax as unrelated business income if the games do not violate any State or local law.

The bill would provide that proceeds derived from bingo games are exempt from income tax in the case of charitable, etc., or political organizations if the State or local statute or ordinance making such games illegal is not "generally enforced."

3. H.R. 6985—Messrs. Minish, Guarini, Mrs. Fenwick, Messrs. Thompson, Courter, Hughes, Patten, Rinaldo, Forsythe, Howard, Roe, Maguire, Florio, Hollenbeck, and Rodino, H.R. 6953—Messrs. Hughes and Roe, and H.R. 7149—Mr. Roe.

Refund of Taxes on Certain State Police Officer Subsistence Allowances

Under present law, cash meal allowances received by State police officers are includible in gross income. However, Public Law 95–427 provided that certain cash meal allowances received by State police officers during the period after 1969 and before 1977 are not includible in income to the extent the allowances *were not reported* by the officers.

The bills would allow a refund or credit of taxes paid by a State police officer with respect to cash meal allowances which *were reported* in gross income in returns filed by the officer for the period after 1969 and before 1977.

4. H.R. 7263—Messrs. Conable, Gibbons, Duncan (Tenn.), Archer, Corman, Frenzel, Pickle, Jones (Okla.), Moore, Gradison, and Fowler

Nonqualified Deferred Compensation Plans for Nonresident Aliens

The bill would provide special rules for nonqualified plans of deferred compensation primarily for the benefit of persons substantially all of whom are nonresident aliens. These provisions would govern the allowability of deductions with respect to the plans and the effect of the plans on earnings and profits. Also, trusts under the plans would be exempted from certain rules relating to foreign trusts with U.S. beneficiaries.

5. H.R. 7276—Mr. Lederer

Investment Tax Credit for Rehabilitated Buildings Leased to Tax-exempt Organizations or Governmental Units

The Revenue Act of 1978 made the investment tax credit generally available to expenditures incurred after October 31, 1978, for rehabilitating older business and commercial buildings (except those used for residential purposes). However, under the investment tax credit rules, generally no credit is allowed for property used by a tax-exempt organization or governmental unit.

The bill would allow the investment tax credit for rehabilitated buildings which are leased to a tax-exempt organization or governmental unit.

6. H.R. 7318—Messrs. Dingell and Jacobs

Charitable Deduction for Certain Contributions of Real Property for Conservation Purposes

Under present law, a deduction for a charitable contribution generally is not allowable for income, estate, and gift tax purposes for a transfer of an interest in property which is less than the taxpayer's entire interest in the property. An exception to this general rule is provided for transfers of certain leases, options, easements, and remainder interests relating to real property if transferred exclusively for conservation purposes. This exception applies to transfers made before June 14, 1981.

The bill would allow a deduction for income, estate, and gift tax purposes for the contribution, exclusively for conservation purposes, of (1) the donor's entire interest in the real property if the taxpayer retains only mineral interests and the right of access to those minerals and the retained minerals may not be removed by any method of surface mining; (2) a remainder interest in real property; or (3) a restriction granted in perpetuity on the use which may be made of real property. Eligible recipients of qualified conservation contributions would be limited to certain publicly supported charitable organizations and governmental units.

The bill also would eliminate the June 14, 1981, termination date for contributions of partial interests in real property made exclusively for conservation purposes.

7. H.R. 7392—Mr. Gephardt

Clarification of Limitation on Deductibility of Certain Entertainment Facility Expenses Includible in Income of Recipient

The bill would provide that disallowance of expenses for entertainment, amusement, or recreation expenses (Code sec. 274(a)) does not apply to expenses which are includible in the gross income of the recipient of the entertainment, amusement, or recreation as compensation for services or as a prize or award under Code section 74. This exception would not apply to a payor unless he furnishes the Internal Revenue Service with an information return (Form 1099) indicating the amount to be included in the gross income of the payee, regardless of the amount involved.

8. H.R. 7487—Messrs. Guarini, Rostenkowski, Florio, and Madigan

Excise Tax on Lighter Gauge Steel Drums

Under the bill, a 20-percent manufacturers excise tax would be imposed on the sale of lighter gauge steel drums.

9. H.R. 7520—Messrs. Ullman, Gore, Pickle, Jones (Okla.), Jenkins, Lederer, Fowler, Duncan (Tenn.), Frenzel, Martin and Moore

Tax Treatment of Mutual or Cooperative Telephone and Electric Companies

The bill would provide that, in determining whether a mutual or cooperative telephone or electric company meets the 85-percent member-income requirement for tax exemption (under Code sec. 501 (c)(12)), any income from rental of poles (used in the cooperative's exempt activities) or from display listings in a directory is to be disregarded. The bill also would provide that income from the rental of such poles by mutual or cooperative telephone and electric companies is not subject to the tax on unrelated business taxable income.

10. H.R. 7606—Mr. Ullman

Employee Stock Ownership Improvements Act of 1980

Sec. 2. Cash distribution option and put option for stock bonus plans

Tax qualified stock bonus plans must generally distribute employer stock to participants entitled to a distribution. A tax credit employee stock ownership plan or an employee stock ownership plan which is a stock bonus plan, however, may distribute cash, subject to a participant's right to demand that benefits be distributed in the form of employer securities.

The bill would provide that a qualified stock bonus plan may distribute cash to a participant entitled to a distribution, subject to the participant's right to demand that benefits be distributed in the form of stock. If a stock bonus plan provides for cash distributions and if stock which is distributed is not readily tradable on an established market, the participant would have the right to require the employer to repurchase the stock. This provision would be effective for plan years beginning after December 31, 1979.

Sec. 3. Special limitaton for employee stock ownershp plans

Under present law, the dollar limitation on annual additions with respect to a participant in a tax credit employee stock ownership plan or in an employee stock ownership plan may be increased, provided certain requirements with respect to allocations of employer contributions are met. The amount of such increase is the lesser of (1) the usual limitation on annual additions to a participant's account, or (2) the amount of employer securities contributed to the plan.

The bill would provide that the increase in the limitation on annual additions to a participant's account under a tax credit employee stock ownership plan or employee stock ownership plan would be the lesser of (1) the usual limitation on annual additions to a participant's account, or (2) the amount of employer securities (or cash used to acquire such securities) contributed to the plan. This provision would be effective for years beginning after December 31, 1979.

Sec. 4. Valuation of employer securities in tax credit employee stock ownership plans

Present law provides that the value of employer securities listed on a national exchange which are contributed to a tax credit employee stock ownership plan is the average of closing prices for such securities for the 20 consecutive trading days immediately preceding the due date for filing the employer's tax return for the year (including extensions).

The bill would provide that the value of employer securities listed on a national exchange contributed to a tax credit employee stock ownership plan would be the average of the closing prices of such securities for the 20 consecutive trading days immediately preceding the date of contribution to the plan. This provision would be effective for taxable years beginning after December 31, 1979.

Sec. 5. Participation of subsidiary corporation in a tax credit employee stock ownership plan

Present law rules regarding tax credit employee stock ownership plans permit a 50-percent owned first-tier subsidiary of a parent corporation, and 80-percent owned second and lower-tier subsidiaries, to use the parent corporation's stock for their tax credit employee stock ownership contributions.

The bill would provide that a corporation which is a second-tier subsidiary of a parent corporation and which is at least 50-percent owned by a first-tier subsidiary of a parent corporation may, if the parent corporation owns 100 percent of the first-tier subsidiary, use stock of the parent corporation in its tax credit employee stock ownership plan. This provision would be effective as if it had been included in section 141 of the Revenue Act of 1978.

Sec. 6. Retirement savings by tax credit employee stock ownership plan participants

Present law provides that an employee who is an active participant in a tax-qualified plan during a year is not eligible to make deductible contributions to an IRA (an individual retirement account, individual retirement annuity, or a retirement bond). An employer may allow an employee to elect not to participate in a tax credit employee stock ownership plan in order for the individual to establish an IRA, however, the plan is subject to certain minimum coverage requirements.

The bill would provide that the minimum coverage requirements for tax credit employee stock ownership plans would be changed in the event that such a plan is the only tax-qualified plan maintained by an employer. If employees are permitted to elect out of such a tax credit employee stock ownership plan for the purpose of establishing IRAs, the tax credit employee stock ownership plan would not fail to meet the minimum coverage requirements of the Code if the plan benefits at least 50 percent of all employees, and if the total allocations under the plan are equal to no more than two percent of the compensation of participating employees. This provision would be effective for plan years beginning after December 31, 1979.

Sec. 7. Certain distributions from money purchase pension plans

An employee (or spouse of an employee) who receives a lump sum distribution from a tax-qualified pension, profit-sharing, or stock bonus plan may defer tax on the distribution by rolling over the proceeds (net of any employee contributions) within 60 days of receipt (1) to an IRA (an individual retirement account, annuity, or bond), or (2) to another qualified pension, etc., plan. A lump sum distribution from a qualified plan is eligible for favorable income tax treatment (e.g., 10-year income-averaging) if no portion of the distribution is rolled over.

If an employer maintains more than one qualified plan of the same type, the plans are aggregated for the purpose of determining whether the entire balance due an employee has been distributed. Under the aggregation rules, all pension plans (defined benefit and money purchase) maintained by the employer are treated as a single plan, all profit-sharing plans maintained by the employer are treated as a single plan, and all stock bonus plans maintained by the employer are treated as a single plan.

The bill would allow an employee (or spouse of an employee) who receives a total distribution from a money purchase pension plan to roll over the distribution to an IRA or to another qualified plan even though the employer also maintains a defined benefit pension plan covering the employee and a total distribution is not made from the defined benefit plan in the same taxable year. If the recipient rolls over a total distribution from a money purchase pension plan and, in a subsequent taxable year, receives a total distribution from a defined benefit pension plan maintained by the employer, the later plan distribution could be rolled over tax-free but would not otherwise be eligible for the favorable income tax treatment accorded lump sum distributions.

Generally, this provision would apply to taxable years beginning after December 31, 1978. A transitional rule for distributions received during 1979 and 1980 would also be provided.

Sec. 8. Voting rights pass through requirement for defined contribution plans

A tax-qualified defined contribution plan is required to pass through voting rights on employer securities to plan participants with respect to major corporate issues in certain circumstances. The vote pass-through applies if (1) the employer which established the plan does not have a class of publicly traded stock, (2) the plan acquired employer securities after December 31, 1979, and (3) after the acquisition of such securities, more than 10 percent of the plan's assets are invested in employer securities.

The bill would repeal the provision of present law which, after December 31, 1979, would require certain defined contribution plans which hold more than 10 percent of their assets in employer securities to pass through voting rights to participants on major corporate issues. This provision would be effective for securities acquired after December 31, 1979.

Sec. 9. Cafeteria plans and deferred compensation

A cafeteria plan is an employee benefit plan under which a participant may choose between taxable benefits and one or more nontaxable

A cafeteria plan is an employee benefit plan under which a participant may choose between taxable benefits and one or more nontaxable fringe benefits. A cafeteria plan may not include deferred compensation.

The bill would permit a cafeteria plan to include deferred compensation under the rules applicable to cash or deferred profit-sharing and stock bonus plans. This provision would be effective for taxable years beginning after December 31, 1979.

II. DESCRIPTION OF BILLS

1. H.R. 4498—Mr. Weaver and H.R. 5798—Messrs. Gudger, Bafalis, Barnard, Beville, Chappell, Preyer, Jones (N.C.), and Andrews (N.C.)

Tax Treatment of Certain Timber Income and Reforestation Expenses

Present law

Corporate tax rates

Generally, under present law, a graduated tax is imposed on the first $100,000 of taxable income of a corporation. In brackets of $25,000 in taxable income, the rates are 17, 20, 30, and 40 percent. A rate of 46 percent is imposed on taxable income in excess of $100,000. An alternative tax of 28 percent applies to corporate net capital gains (the excess of long-term capital gain over net short-term capital loss) if lower than the corporation's regular tax rate.

With respect to timber held by a taxpayer for sale or use in the taxpayer's trade or business, the taxpayer may elect to treat the cutting of timber as a sale or exchange if the timber or the contract right to cut the timber has been held for more than 12 months (Code sec. 631 (a)). If that election is made, the gain recognized from treating the cutting as a sale or exchange is eligible for capital gains treatment (Code sec. 1231(b)(2)).[1] Similar rules are also prescribed for the disposal of timber with a retained economic interest (Code sec. 631(b)).

Domestic International Sales Corporations

Under present law, the profits of Domestic International Sales Corporations, or "DISCS", are not taxed to the DISCs but are taxed to the shareholders when actually distributed or deemed to be distributed. Under one of the qualification requirements, at least 95 percent of the corporation's gross receipts must consist of qualified export receipts. For this purpose, gross receipts from the sale of timber qualify as receipts from the sale of qualified export property. The President may by Executive order designate property as in short supply and thereby exclude it from qualification if he determines that the supply is insufficient to meet requirements of the domestic economy.

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[1] The preference portion of a corporate capital gain may be subject to the 15-percent add-on minimum tax. However, in the case of timber, the amount which would otherwise be treated as a tax preference is reduced by the sum of one-third of the corporation's timber preference income plus $20,000 (Code secs. 57(a)(9)(C) and 57(e)). Reductions are required for computing the regular tax deduction allowable for purposes of the corporate minimum tax (Code sec. 56(d)) and a special tax carryover rule for timber is provided (Code sec. 56(e)).

Reforestation expenditures

Under present law, direct costs incurred in connection with reforestation of timberlands are treated as capital expenditures. (Treas. Regs. § 1.611–3(a)). Reforestation costs for this purpose are those for site preparation (including girdling, herbicide applications, baiting of rodents, and bush removal), seed or seedlings, plus labor and tool expenses incident to planting or seeding. Depreciation on tractors, trucks and other equipment used in these activities must also be capitalized as a reforestation cost.[2]

These capitalized reforestation costs may not be depreciated but are recovered through a depletion deduction when the timber is harvested fifteen or more years later.

If a private owner of timberland receives funds from the Federal Government or State government under certain reforestation cost sharing programs, these funds are not included in income. In addition, the private owner of timberlands does not receive any depletion, depreciation or other deduction for his reforestation costs paid with these cost-sharing funds, and the owner's basis in the property does not reflect the amount of these payments.[3] These rules apply for grants made after September 30, 1979.

Where additional costs are incurred for clearing brush and unwanted trees after the planting or seeding of timberlands, these costs are currently deductible because they are in the nature of maintenance charges.[4]

Investment tax credit

Under present law, a credit against income tax liability is provided for a taxpayer's investment in certain types of depreciable business assets. Generally, the credit allowable is 10 percent of qualified investment.

The credit is generally not allowable with respect to timber since it is not depreciable property.[5]

Issues

The issues raised by the bills are:

(1) Whether the Secretary of Agriculture may require the purchaser of timber from national forest land to perform work on land cut over by the purchaser instead of requiring deposits of money to cover reforestation and forest improvement work.

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[2] Rev. Rul. 75–467, 1975–2 C. B. 93.

[3] These rules, found in sections 126 and 1255 of the Code, were enacted under section 543 of the Revenue Act of 1978 (P.L. 95–600).

[4] Rev. Rul. 66–18, 1966–1 C. B. 59, indicates that such expenses are currently deductible. This ruling was modified by Rev. Rul. 71–228, 1971–1 C. B. 53, to indicate that costs of annual shearing of Christmas trees are also currently deductible. This latter ruling also follows the decision in *Daniel D. Kinley*, 51 T.C. 1002 (1969), *aff'd per curiam*, 70–2 USTC ¶ 9462 (2d Cir. 1970), acq. 1971–2 Cum. Bull. 3.) See also, *Ransburg* v. *United States*, 281 F. Supp 324 (S.D. Ind. 1967) (current deduction for weed, brush and insect control expenses conceded by United States; the court also allowed a current deduction of expenses for annual shearing of Christmas trees).

[5] However, trees comprising a timber producer's seed orchard to produce seedlings qualify for the investment tax credit (Rev. Rul. 78–264, 1978–2 C.B. 9).

(2) Whether alternative capital gains treatment and DISC deferral benefits should be denied with respect to taxable income attributable to sales or exchanges of softwood logs which are exported.

(3) Whether any additional taxes raised by special treatment of taxable income from exported softwood logs should be earmarked for a Forest Services Nurseries Fund.

(4) Whether an income tax credit should be allowed with respect to certain forestry expenditures.

Explanation of the bills

H.R. 4498

In general, the bill would (1) permit the Secretary of Agriculture to require a purchaser to perform work on national forest land cut over in lieu of making cash deposits for reforestation and forest improvement work, (2) impose the regular corporate rates on the taxable income of a corporation to the extent attributable to the export of softwood logs, (3) earmark for a Forest Services Nurseries Fund any increase in taxes attributable to the special taxation of taxable income from exports of softwood logs, and (4) provide a special income tax credit for specified percentages of a taxpayer's qualified forestry expenditures.

Consideration of the Bill by the Subcommittee on Forests of the Committee on Agriculture

The bill, H.R. 4498, was jointly referred to the Committee on Ways and Means and the Committee on Agriculture. On July 19, 1979, the Subcommittee on Forests of the Committee on Agriculture approved the income tax credit provisions (sec. 203) of the bill in concept although it did not actually report the bill. Because this provision is not within the jurisdiction of the Committee on Agriculture, the subcommittee recommended that the Committee on Ways and Means hold hearings on that provision of the bill. The Subcommittee on Forests did not approve the provisions under which tax benefits would be denied for taxable income attributable to exports of softwood logs.

Taxable income from softwood log exports

Under the bill, corporate taxable income attributable to sales or exchanges of softwood logs which are exported would be subject to the regular corporate tax rates and not eligible for capital gains treatment. This provision would apply with respect to softwood logs exported by the taxpayer or another person. However, the provision would not apply with respect to sales or exchanges of logs if the taxpayer in good faith accepts a certification from the purchaser that the logs will not be exported. For purposes of this provision, a softwood log means a softwood log or cant which has a diameter inside the bark at the small end of 6 inches or more, and any softwood square each side of which is 6 inches or more.

The bill also would provide that, in the case of a DISC, the taxable income attributable to softwood logs shall be deemed to be distributed as a taxable dividend to shareholders. Thus, the DISC deferral benefits would be denied for the taxable income attributable to export sales of softwood logs.

The increase in corporate taxes attributable to the preceding provisions would be earmarked for a special fund to be known as the Forest Service Nurseries Fund. Transfers of these amounts would be based on estimates by the Secretary of the Treasury with proper adjustments in the amount of subsequent transfers to reflect differences between estimated and actual receipts attributable to those provisions. Amounts in the fund would be available, as provided by appropriation Acts, to the Secretary of Agriculture (acting through the Forest Service) to establish and operate nurseries to provide stock for the reforestation of public and private forest lands.

Tax credit for forestry expenditures

Under the bill, a credit against the income tax liability of an eligible taxpayer would be allowed. The amount of the credit would be equal to the greater of (1) 25 percent of the qualified forestry expenditures paid or incurred by the taxpayer during the taxable year that does not exceed $50,000 [6] (a maximum credit of $12,500) or (2) 10 percent of the total such expenditures for the taxable year.

For purposes of the provision, an eligible taxpayer is any person who owns at the end of the taxable year not less than 25 acres of land suitable for producing timber usable for the manufacture of wood products and who during the taxable year did not receive or expend cost-sharing funds received under section 4 of the Cooperative Forestry Assistance Act of 1978 (16 U.S.C. 2103). Qualified forestry expenditures eligible for the credit would mean amounts which are capitalized and paid or incurred for the planting of tree seeds or seedlings (other than for fruit and nut tree seeds and seedlings) in such species and numbers as are suitable for producing timber and the planting of any shelterbelt. Eligible expenditures would include the expenses of site preparation for the planting of tree seeds or seedlings or shelterbelt. Site preparation would include the treatment of soil and litter. For purposes of the bill, shelterbelt means any strip of living trees or shrubs established and maintained for the purpose of providing for wind erosion control, snow accumulation, or wildlife habitation. No expenditures are to be taken into account by a taxpayer for a taxable year unless expenditures are paid or incurred with respect to one acre or more. Further, no expenditures are to be taken into account if they are currently deductible by the taxpayer.

The amount of credit allowable for a taxable year would be subject to a tax liability limitation. For this purpose, the taxpayer's tax liability would be the amount of income taxed otherwise owed after reduction for all other nonrefundable credits having a lower section number than the proposed credit (i.e., the regular investment tax credit, energy credits, etc.). For the first $25,000 in tax liability ($12,500 in the case of a married individual filing a separate return),

[6] The bill provides a $5,000 limit upon qualified forestry expenditures which are taken into account for purposes of the 25-percent credit. However, it is understood that the sponsor of the bill intended the amount to be $50,000 and that the $5,000 amount resulted from a typographical error. In addition, it is understood that on July 19, 1979, the Subcommittee on Forests of the House Committee on Agriculture approved the credit provisions in principle with the understanding that the 25-percent credit limitation would be based on $50,000 in qualified expenditures.

the credit would be allowable dollar for dollar against tax liability. For amounts in excess of $25,000 (or $12,500), the amount of the credit would be limited to 90 percent of the tax liability in excess of $25,000 (or $12,500). Any unused credits could be carried back 3 years and carried foward for 7 years.

The provisions would be applied to a controlled group of corporations as if the group were a single taxpayer. The credit would be allowable to each member of the group in proportion to the qualifying expenditures made by each member. For purposes of this provision, a 50-percent control test would apply. Under Treasury regulations, other businesses under common control are to be treated as a single taxpayer.

H.R. 5978

This bill also would provide an income tax credit for forestry expenditures. It does not contain any provisions relating to exports of softwood logs.

Under the bill, the amount of the credit would be determined under the following table:

Qualified forestry expenditures	Rate (percent)	Maximum amount for each bracket
$1 to $5,000	75	$3, 750
$5,001 to $15,000	50	5, 000
$15,001 to $25,000	25	2, 500
$25,001 to $50,000	10	2, 500
Over $50,000	0	0
Total maximum amount per taxpayer		13, 750

For purposes of this provision, an eligible taxpayer means any person who owns at the end of the taxable year not less than 10 acres of land which is capable of producing crops of industrial wood or providing other forest resources. Under the bill, qualified forestry expenditures means amounts paid or incurred which are capitalized for creating and enhancing vegetation on forest lands for purposes of forest growth and quality, fish and wildlife habitat, soil stabilization, or outdoor recreation. For this purpose, no expenditures are taken into account for any taxable year unless the expenditures apply to areas of 10 acres or larger. Further, no expenditure is to be taken into account if it is currently deductible for the taxable year. Finally, a taxpayer will not be treated as having paid or incurred any qualified expenditures if they are made from funds received as cost-sharing payments through the Forestry Incentives Programs authorized by section 4 of the Cooperative Forestry Assistance Act of 1978 (16 U.S.C. 2103) or through State cost-sharing programs for improving forests.

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The credit allowed would be limited to the tax liability for the taxable year. For this purpose, the tax liability limitation would be the tax otherwise owed reduced by other nonrefundable credits provided under code sections having a lower number or letter designation than this provision. Unused credits for a taxable year could be carried forward 5 years.

Special rules for controlled corporate groups or other business entities under common control are provided under the bill. These provisions are similar to those provided under H.R. 4498.

Effective dates

H.R. 4498

In general, the tax amendments would apply to taxable years beginning after the date of enactment of the bill. For purposes of the special rules relating to exports of softwood logs, a sale or exchange would be excepted if made pursuant to a binding contract executed on or before the date of enactment.

H.R. 5978

The provisions of this bill would apply to taxable years beginning after the date of enactment of the bill.

Revenue effects

The estimated revenue effects for the provisions of the bills are set forth in the following table:

[In millions of dollars]

	Fiscal years				
	1981	1982	1983	1984	1985
H.R. 4498:					
All taxable income from softwood log exports taxed at regular rates	4	14	26	42	52
Denial of DISC benefits	3	7	11	15	18
Credit for forestry expenditures	−8	−19	−22	−24	−26
H.R. 5798	−9	−23	−26	−27	−28

2. H.R. 5719—Mr. Lederer

Tax Exemption for Proceeds of Certain Bingo Games

Present law

Most organizations which are generally exempt from Federal income tax, such as charitable or educational organizations described in Code section 501(c)(3), remain subject to tax on any "unrelated business taxable income," defined as gross income derived from any "unrelated trade or business" (Code secs. 511–512). In Public Law 95–502, the Congress provided that the term "unrelated trade or business" does not include any trade or business which consists of conducting certain bingo games (Code sec. 513(f)). This provision was effective for taxable years beginning after December 31, 1969 (the effective date for extension to most exempt organizations of the tax on unrelated business taxable income).

Also in Public Law 95–502, the Congress provided that political organizations are not subject to tax on income from bingo games proceeds from which would not be taxable if received by exempt organizations (Code sec. 527(c)(3)(D)). This provision was generally effective for taxable years beginning after December 31, 1974 (the effective date of Code sec. 527, which provides rules for the taxation of political organizations).

In the case of both tax-exempt and political organizations, the rules added by Public Law 95–502 apply only if (among other requirements) the conducting of the bingo game "does not violate any State or local law" (Code sec. 513(f)(2)(C)). In House Report 95–1608 on these bingo game provisions, the Ways and Means Committee stated that "this limitation is designed to ensure that no Federal tax benefit is provided for activities which are conducted illegally."

The Treasury Department has issued final regulations under the bingo game rules added by Public Law 95–502, which incorporate the statutory limitation that favored tax treatment is not available in the case of bingo games conducted in violation of State or local law (Treas, Reg. §1.513–5(c)(1)). The statement of "supplemental information" published with the final regulations states that the Internal Revenue Service had received comments, in response to issuance of such regulations in proposed form, suggesting that a bingo game should not be considered to violate State or local law if a statute or ordinance prohibiting such games nonetheless is not generally enforced against tax-exempt organizations (45 Fed. Reg. 33969, May 21, 1980). The Treasury statement declares that "it would not be appropriate for the Internal Revenue Service to independently determine that a statute proscribing gambling is, nevertheless, not the law of the State." The statement also refers to the legislative history cited above.

Issue

The issue is whether proceeds derived from bingo games should be exempted from income tax in the case of charitable, etc. or political organizations if the State or local statute or ordinance making such games illegal is not "generally enforced."

Explanation of the bill

The bill would provide that proceeds derived from bingo games are exempt from income tax in the case of charitable, etc. or political organizations if the State or local statute or ordinance making such games illegal is not "generally enforced."

Effective date

The bill would be effective for taxable years beginning after December 31, 1969.

Revenue effect

It is estimated that this bill will reduce budget receipts by less than $5 million annually.

3. H.R. 6935—Messrs. Minish and Guarini, and H.R. 6953—Mr. Hughes

Refund of Taxes on Certain State Police Officer Subsistence Allowances

Present law

Code section 119, which was enacted in 1954, excludes from an employee's gross income the value of employer-furnished meals if they are provided for the employer's convenience, on its business premises, and for substantially noncompensatory reasons. The legislative history of section 119 indicates that the exlcusion applies only to the value of meals furnished in kind.[1]

Although in 1954 Congress provided for an exclusion of up to $5.00 per day of statutory subsistence allowances paid to police officers, this provision was repealed in 1958 "to bring the tax treatment of subsistence allowances for police officials into line with the treatment of such allowances in the case of other taxpayers. . . ."[2]

On November 29, 1977, the Supreme Court decided *Commissioner* v. *Kowalski*, 434 U.S. 77, which held that cash meal allowances paid to a state trooper were includible in income since the section 119 exclusion applied only to meals furnished in kind. This decision resolved a conflict between the various appellate courts as to the taxability of cash meal allowances.

In response to the *Kowalski* decision, Congress enacted section 3 of Public Law 95–427. Under that section, the Supreme Court's decision generally applies only prospectively. The Act allowed an exclusion from gross income for certain subsistence allowances received by an officer during the years 1970 through 1976 to the extent that the allowances were not included in income on the officer's income tax return. It also applied to all of these subsistence allowances received in 1977 without regard to an officer's treatment of those allowances on his or her return.

Public Law 95–427 did not authorize the refund of taxes paid prior to 1977 on such cash allowances if those payments had been included in income on the officer's income tax return. Thus, the Act was restricted to cases where officers might experience hardships in paying income tax deficiencies assessed with respect to cash meal allowances.

Issue

The issue is whether taxes paid with respect to cash meal allowances received by State police officers during 1970 through 1976 should be refunded where the allowances were reported as income.

[1] S. Rep. No. 1622, 83d Cong., 2d Sess. 190–191 (1954).

[2] H.R. Rep. No. 775, 85th Cong., 1st Sess. 7 (1957), 1958–3 C.B. 817.

Explanation of the bill

The bills would allow a refund or credit of tax paid by a State police officer with respect to a cash meal allowance (within the meaning of section 3 of Public Law 95–427) received between 1969 and 1977 regardless of whether those cash payments were reported in gross income.

Effective date

The bills would be effective upon enactment. The period of limitations for making refunds would not operate to bar any claim for refund filed within one year of the date of enactment of the bill.

Revenue effect

It is estimated that either bill will result in a one-time decrease in budget receipts of $5 million in fiscal year 1981. This represents refunds or credits for tax paid by State police officers with respect to cash meal allowances during 1970 through 1976 where the allowances were reported in income.

Prior Congressional consideration

During the 95th Congress, the Subcommittee on Taxation and Debt Management Generally of the Senate Committee on Finance conducted hearings on S. 2872. That bill included amendments which were substantially similar to the provisions of H.R. 6953. The Finance Committee did not report those amendments.

4. H.R. 7263—Messrs. Conable, Gibbons, Duncan (Tenn.), Archer, Corman, Frenzel, Pickle, Jones (Okla.), Moore, Gradison, and Fowler

Nonqualified Deferred Compensation Plans for Nonresident Aliens

Present law

United States businesses operating abroad often provide deferred compensation for their foreign employees. In many cases, plans are established which cover almost exclusively nonresident alien employees, rather than U.S. citizens working abroad. The foreign operations of the U.S. business may be conducted through a branch of a U.S. corporation or through a foreign subsidiary of a U.S. parent corporation.

General rules relating to deductibility of deferred compensation

In general, the year in which a taxpayer is allowed to deduct expenses, such as compensation, is determined by its method of accounting. Generally, cash basis taxpayers deduct expenses in the year they are paid, while accrual basis taxpayers deduct the expenses in the year in which all events have occurred which determine the fact of the liability and the amount of the liability can be estimated with reasonable accuracy.

However, the Code provides special rules (sec. 404) for deductions of amounts under pension and other deferred compensation plans, which must be met in addition to the usual requirements for deduction of the amounts as business expenses (secs. 162 and 212). Separate rules apply with respect to qualified and nonqualified deferred compensation plans.

Qualified plans.—In order for a deferred compensation plan to be "qualified" under the Code, contributions under it must be paid into a trust to protect them from the employer's creditors. A number of other requirements must also be met. In particular, the plan must be administered for the sole benefit of employees and their beneficiaries, eligibility to participate must be nondiscriminatory, contributions or benefits must be nondiscriminatory, and benefits must be paid no later than specified dates. Additional requirements must be met if the plan covers self-employed individuals, such as partners. The Employee Retirement Income Security Act of 1974 (ERISA) added a number of additional requirements, including, for example, new eligibility rules, minimum standards for vesting and accrual of benefits, minimum funding standards, maximum limitations on contributions and benefits, a requirement that benefits be paid in certain cases in the form of joint and survivor annuities, and prohibitions on certain dealings between the plan and related parties.

If a plan is qualified, a deduction is allowed at the time a contribution is paid into the plan's trust. The amount of the contribution allowable as a deduction is no less than the amount necessary to satisfy the minimum funding standard prescribed by ERISA. A maximum limitation is also placed on the amount of the contribution which may be deducted. Generally, this may not exceed the "normal cost" of the plan for the year plus an amount which would amortize plan benefit liabilities attributable to past service of employees (if not already included in normal cost under the funding method used by the taxpayer) over a period of no less than 10 years. (The "normal cost" is a measure intended to reflect the ratable share of the increase in plan liabilities to participants resulting from service performed that year. Under some allowable funding methods, a ratable portion of liability for past service of the employees is also included in the year's normal cost.) No deduction is allowed for contributions in excess of the "full funding limitation," the amount by which the accrued liability for benefits of the plan exceeds the value of its assets. Other limitations on deductions also apply if the employer maintains qualified profit sharing or stock bonus plans for his employees. An unlimited carryforward is allowed for contributions in excess of the limitations.

Nonqualified plans.—If a plan of deferred compensation does not meet the requirements for qualification under the Code, a separate rule applies to the deductibility of contributions. The deduction is taken in the taxable year in which an amount attributable to the contribution is includible in the income of the employee. A similar rule applies to deferred compensation arrangements with independent contractors. However, if the plan covers more than one employee, the deduction may be taken only if separate accounts are maintained for each employee. Otherwise, the IRS takes the position that the contribution is never deductible, except in the case of unfunded plans where payment is made directly to the former employees.

Separate accounts are established only for defined contribution plans, which generally require that an amount established pursuant to a formula, which may vary from employee to employee, be contributed to the accounts of the participants. Each employee bears the risk of fluctuations in the value of the investments in his account. Separate accounts are not maintained, however, for defined benefit plans. These plans specify by formula the benefits which participants are to receive on retirement. Contributions to them are based on actuarial calculations of the amounts which will be required to be paid out, generally based in the aggregate on the ages and life expectancies of members of the workforce, likely turnover of participants, and expected investment performance of amounts contributed. The employer bears the risk of investment gain or loss. Because the actuarial assumptions are based on aggregated data, no separate accounts are maintained. Hence, in situations where this rule applies, no deduction is allowed for contributions to a defined nonqualified benefit plan.

Foreign deferred compensation plans

Foreign branch operations.—The Code permits the trust of a qualified plan to be organized under foreign law but does not otherwise expressly waive any of the requirements for qualification. In Letter Ruling 7904042, the Internal Revenue Service held that if a plan for the benefit of nonresident alien employees did not meet all of the requirements for qualification under the Code (including the provisions added by ERISA), no deduction would be allowable under the rules for qualified plans described above. Instead, the Service held that amounts would be deductible, if at all, only under the rules which apply to nonqualified plans. Since the plans in question were defined benefit plans which did not maintain separate accounts for participants, the Service denied deductions for contributions made to the plans.

Foreign subsidiary operations.—Foreign subsidiaries of U.S. corporations generally do not have U.S. operations which would subject them to U.S. tax, and since their income is thus not subject to U.S. tax, the question of whether a deduction is allowed for contributions to a plan for nonresident aliens does not have the same direct effect on their U.S. tax liability as in the case of a foreign branch of a U.S. corporation. However, the treatment of the contribution in computing the foreign subsidiary's accumulated profits has important consequences in determining the indirect foreign tax credit which the U.S. parent corporation is allowed with respect to dividends received from the foreign subsidiary.[1]

Generally, if a U.S. corporation owns at least 10 percent of the voting stock of a foreign corporation from which it receives a dividend, the U.S. corporation is deemed to pay the amount of foreign income taxes paid by the foreign subsidiary on the accumulated earnings from which the dividend was paid. The U.S. corporation may then, within limitations, claim a credit against its U.S. tax liability in the amount of the foreign income taxes deemed paid by it. Under regulations, the determination of foreign taxes paid on accumulated earnings is made on a year-by-year basis, starting with the most recent year. If only part of the accumulated earnings of that year are paid out, only a proportionate part of the foreign income taxes paid with respect to the earnings for that year are deemed paid. Thus, if a dividend of a given size is paid, more of the foreign income taxes paid by the foreign subsidaries will be deemed to have been paid by (and thus would be creditable by) the U.S. parent if the accumulated earnings of the subsidiary are smaller than if they are larger—because a proportionately larger share of the accumulated earnings would be paid out in the dividend, resulting in a greater proportion of the foreign taxes being deemed paid.

The deduction issue discussed in connection with foreign branches can also be relevant in the case of a foreign subsidiary if it conducts a U.S. business, the taxable income from which must be determined, or if it is a controlled foreign corporation (CFC).[2]

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[1] Section 406 of the Code permits, in limited instances, a U.S. parent corporation with a qualified plan to make contributions on behalf of employees of a foreign subsidiary who are U.S. citizens. In such cases, a deduction is allowed to the foreign subsidiary.

[2] Generally, a foreign corporation is a CFC if more than 50 percent of the voting power is held by "United States shareholders," that is, U.S. persons each of whom holds 10 percent or more of the voting power.

In the case of a CFC, supbart F (secs. 951–64 of the Code) provides that, in general, the United States shareholders must currently include in their income certain types of tax haven income of the corporation and certain types of passive investment income. Generally, the amount of this income to be taken into account is reduced by deductions properly allocable to that income, so if foreign pension costs are so allocable, it is necessary to determine whether and when they are deductible. Moreover, an indirect foreign tax credit similar to that described above may be allowed to the U.S. shareholder with respect to the amount which the shareholder must include in income. The credit is equal to the proportionate part of the foreign income taxes paid on the earnings and profits of the CFC from which the distribution is deemed to be made. Thus, questions similar to those described above arise as to the size of the earnings and profits.

In Letter Ruling 7839005, the Internal Revenue Service considered an accrual basis CFC which established an irrevocable balance sheet reserve for pension expenses. The taxpayer contended that the CFC's earnings and profits should be reduced by the amount of its pension liability which had properly been accrud. The Service held, however, that earnings and profits could be reduced only to the extent of pension payments actually made. The Service did not view as controlling the taxpayer's argument that this result would distort (generally by reducing) its allowable indirect foreign tax credit with respect to dividend distributions from the CFC.

Foreign trusts with U.S. beneficiaries.—The Code provides that if a U.S. person transfers property to a foreign trust, and a U.S. person is the beneficiary of any part of the trust, then the transferor is treated as the owner of the transferred trust property and therefore is taxable on the income earned on that part. Moreover, if the trust does not have a U.S. beneficiary at the time of the transfer but later acquires one, the transferor is subject to tax on all the undistributed net income on amounts it previously transferred to the trust. The Code expressly provides that these rules do not apply to foreign trusts established under qualified plans. However, there is no similar exception for foreign trusts under nonqualified plans. Thus, if a U.S. corporation makes a contribution to a foreign trust of a nonqualified plan, it is possible that the corporation would be taxable on the income earned on the contribution, either immediately if the trust has a U.S. person as a beneficiary, or subsequently if one of the plan participants or his beneficiary becomes a U.S. citizen or resident.

Issues

The issues are whether or not, in the case of a nonqualified plan of deferred compensation maintained for the benefit of nonresident aliens:

(1) special rules should be prescribed with respect to the allowability of deductions with respect to the plan;

(2) special rules should be prescribed as to the effect of the plan on earnings and profits; and

(3) it should be specified that the rules relating to foreign trusts with U.S. beneficiaries do not apply to contributions to such a trust under the plan.

Explanation of provisions

Allowance of deductions

The bill would provide that, in the case of a nonqualified deferred compensation plan which is maintained primarily for the benefit of persons substantially all of whom are nonresident aliens, the general rules regarding the timing and allowability of deductions for contributions will not apply (unless the taxpayer elects to have those rules apply to the plan). Instead, if the contributions otherwise qualify for deduction as business expenses, special rules for deductibility are prescribed.

General rules.—Four general requirements apply to any deductions (except deductions for direct payments, described below) to be taken under the special rules. First, the benefits provided by the plan must be either required by foreign law or set forth in a written document communicated to the active participants. Second, in the case of a defined benefit plan, the deduction is limited to amounts paid or accrued in respect of benefits that are reasonably capable of actuarial estimation. Third, to the extent the amount taken into account is dependent upon actuarial determinations, the actuarial cost method and assumptions used must in the aggregate be reasonable. Fourth, the amount to be taken into account for the taxable year must be determined in a manner consistent with generally accepted accounting principles in the United States applicable to the charging of pension costs against income.

In addition to these general requirements, special rules are prescribed which must be met in both of the circumstances which could give rise to a liability for deferred compensation other than a direct payment: the payment of contributions to a trust or fund on the one hand, and other payment or accrual on the other hand.

Trust contributions.—If an amount is transferred to a separate trust or fund and has not been allowed previously as a deduction, then, whether or not benefits to be provided from the trust are subject to a substantial risk of forfeiture, a deduction is allowed for the amount transferred if the conditions described above under "General rules" are met and if certain other requirements are met. In the case of a defined benefit plan, the amount transferred and any income earned thereon must not revert to the employer or to the employer's benefit prior to the satisfaction of all liabilities with respect to participants and beneficiaries under the plan. Also, the transferred amount must not exceed the full funding limitation for the year. In the case of a defined contribution plan, the amount transferred and any income earned thereon must not revert to the employer or to employer's benefit, and the amount taken into account must be allocated to individual accounts of participants that will be adjusted at least annually for the income and expenses of the fund. As is currently the case with qualified plans, a taxpayer will be allowed a deduction with respect to a taxable year if the contribution on which the deduction is based is made by the time the taxpayer files a timely return for that year.

Other payments and accruals.—If the above requirements relating to payment into a trust or fund are not met, but the conditions described above under "General rules" are satisfied, then a deduction is allowed at the time of payment or accrual, if the amount is paid or accrued in respect of benefits that are not subject to a substantial risk of foreiture, and, if the amount is accrued, it represents the actuarial present value of such accrued benefits.

Direct payments.—The bill also provides that, if a deduction has not previously been allowed under the above rules, it will be allowed when a payment, which is not subject to a substantial risk of forfeiture, is made to a participant or beneficiary by an employer.

Nonresident alien participation.—As described earlier, these rules apply only where substantially all of the beneficiaries are nonresident aliens. The bill provides for a reduction of the deduction otherwise allowable where not all the active participants are nonresident aliens. Generally, the amount otherwise allowable is to be multiplied by a fraction, the numerator of which is the payments or accruals made on behalf of active participants who are nonresident aliens, and the denominator of which is the payments or accruals made on behalf of all active participants. However, no reduction is required if during the taxable year at least 95 percent of all active participants are nonresident aliens, and at least 95 percent of the contributions made to or benefits accruing under the plan are in respect of active participants who are nonresident aliens.

Other rules.—The bill allows an unlimited carryforward of amounts not currently deductible (except amounts disallowed because of the participation of individuals other than nonresident aliens). The bill also requires that whatever accounting method is used to determine the deductible amount must be used consistently. Changes in the accounting method (but not actuarial assumptions) would require the permission of the Service.

Effect on earnings and profits

The bill would provide that, if an amount would be deductible under the special rules provided by the bill, the earnings and profits of the corporation are to be reduced to the same extent.

Foreign trusts

The bill would make it clear that in the case of a contribution to a foreign trust subject to the special deduction rules, the corporation making the contributions is not treated as the owner of part of the trust merely because the trust has or acquires U.S. beneficiaries.

Effective date

The bill would be effective upon enactment.

Revenue effect

The revenue estimate for this bill is not yet available.

5. H.R. 7276—Mr. Lederer

Investment Tax Credit for Rehabilitated Buildings Leased to Tax-exempt Organizations or Governmental Units

Present law

The Revenue Act of 1978 extended the investment tax credit to rehabilitation expenditures incurred in connection with existing buildings used in all types of business or productive activities except those, such as apartments, which are used for residential purposes. Eligible buildings include factories, warehouses, office buildings, hotels, and retail and wholesale stores.

To qualify as a rehabilitation expenditure, the expenditure must be incurred after October 31, 1978, in connection with the rehabilitation or reconstruction of a building which has been in use for a period of at least 20 years before the commencement of the rehabilitation.

Under present law (Code secs. 48(a) (4) and (5)), property owned by or leased to a tax-exempt organization (other than use in an unrelated trade or business) or by a governmental unit is not qualified for the investment tax credit.

The Technical Corrections Act of 1979 (P.L. 96–222) provided an exception to the rules designed to deal with certain equipment leasing tax shelters (under these rules property subject to a net lease is ineligible for the credit if the lessor is a noncorporate lessor). This exception was provided to accommodate the traditional and customary use of net lease arrangements for buildings.

Issue

The issue is whether the investment tax credit should be allowed in the case of rehabilitated buildings leased to tax-exempt organizations and governmental units.

Explanation of the bill

The bill would make the present exception denying the credit for property used by a tax-exempt organization or governmental unit inapplicable in the case of qualified rehabilitation expenditures to rehabilitate existing buildings.

Effective date

The bill would be effective for taxable years ending after October 31, 1978.

Revenue effect

The revenue estimate for this bill is not yet available.

6. H.R. 7318—Messrs. Dingell and Jacobs

Charitable Deduction for Certain Contributions of Real Property for Conservation Purposes

Present law

As a general rule, a deduction is not allowed for income, estate, and gift tax purposes for contributions to charity of less than the taxpayer's entire interest in the contributed property. This restriction was enacted by Congress in the Tax Reform Act of 1969 to prevent certain tax-avoidance transactions in which the taxpayer could obtain a deduction for a gift to a charity of the use of part of his property. Exceptions allowing deductions for charitable contributions of partial interests in property are provided for the contribution of (1) a remainder interest in a personal residence or farm; (2) an undivided portion of the taxpayer's entire interest in the property; (3) certain interests in trust; and (4) interests not transferred in trust that would be deductible if made in trust (Code secs. 170(f), 2055(e)(2), and 2522(c)(2)). The Conference Report on the Tax Reform Act of 1969 states that a gift of an open space easement in gross is to be considered a gift of an undivided interest in property where the gift is in perpetuity. On the basis of that Conference Report language, the Internal Revenue Service has allowed deductions for contributions of certain kinds of easements under the undivided interest exception including open space, historical, and recreational easements. Rev. Rul. 74–583, 1974–2 C.B. 80; Rev. Rul. 75–358, 1975–2 C.B. 76; Rev. Rul. 75–373, 1975–2 C.B. 77.

However, explicit statutory exceptions for charitable contributions made "exclusively for conservation purposes" were provided in Tax Reform Act of 1976 (and modified by the Tax Reduction and Simplification Act of 1977). Under these exceptions, a deduction is permitted for the contribution to a charitable organization for conservation purposes of (a) a lease on, option to purchase, or easement with respect to real property granted in perpetuity or (b) a remainder interest in real property. (Code secs. 170(f)(3)(B) (iii) and (iv).) The exceptions for these partial interests contributed for conservation purposes only apply to contributions made before June 14, 1981.

Issues

Issues raised by the bill include the following:

(1) Should a deduction be allowed after June 13, 1981, for contributions of partial interests in real property made exclusively for conservation purposes?

(2) Should the eligible recipients of conservation contributions be limited to certain publicly supported charitable organizations and governmental units?

(3) Since the value to the public of a conservation easement lies in the restrictions it places on the donor's use of the retained property (because, unlike most types of property contributed to charity, an easement cannot, as such, be used by the charity), should a deduction be allowed for the contribution of an easement only where the restrictions imposed by the easement serve some public benefit and are likely to be enforced?

(4) Should the owner of property that may have subsurface oil and gas or other minerals, or property that is actively used for the extraction of oil and gas or other minerals, be permitted a deduction for contributing the fee interest while retaining all rights to extract the oil and gas or other minerals through non-surface extraction methods?

(5) Should the definition of conservation purposes be broadened to include the preservation of "open space" or farmland where such preservation is consistent with a defined governmental policy (an important issue in light of the uncertainty as to whether a gift of an open space easement qualifies for a deduction under present law as a gift of an undivided interest)?

(6) Should the definition of historically important land areas or structures in section 170(f)(3)(C)(ii) be more closely coordinated with the National Register and with the related provisions of the Code allowing rapid amortization of expenditures incurred in rehabilitating certified historic structures (sec. 191(d))?

(7) Should rules be provided for situations where a transferred partial interest in real property, for which a deduction was allowed because it served a conservation purpose, ceases to be used in furtherance of the conservation purpose?

Explanation of the bill

The bill would revise present Code provisions allowing deductions for charitable contributions of easements and other partial interests in real estate contributed for conservation purposes. In addition, these provisions, which are to expire on June 14, 1981, would be extended for future years without any later sunset date.

The bill would allow a deduction for the contribution of a qualified real property interest to a qualified organization exclusively for conservation purposes. Under the bill, a qualified real property interest would be (1) the entire interest of the donor in the real property, other than a qualified mineral interest; (2) a remainder interest; or (3) a restriction granted in perpetuity on the use which may be made of the real property. A qualified mineral interest would be subsurface oil, gas, or other minerals and the right to access to such minerals. If, however, the minerals retained may be removed or extracted by surface mining methods, then the gift would not be a qualified conservation contribution. In general, a qualified organization would be a governmental unit or a publicly supported charitable organization.

Effective date

The provisions of the bill (other than section 2 relating to the repeal of the June 14, 1981, sunset date for Code secs. 170(f)(3)(B) and (C)) would apply to transfers made after the date of enactment in taxable years ending after such date.

Revenue effect

It is estimated that this bill would reduce fiscal year receipts by $5 million annually.

7. H.R. 7392—Mr. Gephardt

Clarification of Limitation on Deductibility of Certain Entertainment Facility Expenses Includible in Income of Recipient

Present law

Prior to the enactment of the Revenue Act of 1978, expenses incurred with respect to entertainment facilities[1] were deductible if they were ordinary and necessary, the facility was used primarily for the furtherance of the taxpayer's business (i.e., more than 50 percent of the time that it was used), and the expense in question was related directly to the active conduct of the taxpayer's business. For this purpose, entertainment facility expenses included dues or fees paid to any social, athletic, or sporting club or organization. Dues or fees paid to professional associations, civic organizations, or to clubs operated solely to provide meals under circumstances normally considered to be conducive to business discussions generally were not considered to be entertainment facility expenses.

In determining whether an entertainment facility was used primarily for business purposes, all the taxpayer's ordinary and necessary business use of the facility was taken into account. Once it was determined that the facility was used primarily for business, the portion of the expenses which were related directly to the active conduct of the taxpayer's business could be deducted.

The Revenue Act of 1978 provided generally that no deduction was allowable for any entertainment facility expense. However, the Act retained a number of exceptions to the general rule that existed under prior law. One of these relates to expenses treated as employee compensation (sec. 274(e)(3)). Under this exception, expenses for goods, services, and facilities are not subject to the disallowance rules to the extent that the expenses are treated by the taxpayer, with respect to the recipient of the entertainment, as compensation to an employee on the taxpayer's return and as wages to the employee for purposes of income tax withholding. Thus, in the case of facility expenses which satisfy this exception, the Act retained the rules of prior law which formerly had applied to expenses treated as employee compensation.

The Technical Corrections Act of 1979 provided that the provision disallowing expenses for entertainment facilities did not apply to expenses paid or incurred in 1979 or 1980 where the entertainment facilities are provided to a nonemployee of the payor, the amount of the expense is includible in the gross income of the recipient of the entertainment facilities as compensation for services or as a prize or award, and the payor complies with any required reporting of information

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[1] An entertainment facility generally is any item of personal or real property owned, rented, or used by a taxpayer during the taxable year for, or in connection with, an activity normally considered to be of an entertainment nature.

return (i.e., an information return (Form 1099) is furnished to the Internal Revenue Service (but not the recipient) for amounts in excess of $600).

Issue

The issue is whether the limitations of the Revenue Act of 1978 on entertainment facilities ought to apply to expenses of the taxpayer for facilities provided to nonemployees where the amount of the expense is includible in the gross income of the recipient as compensation or as a prize or award and the taxpayer provides the Internal Revenue Service with any required information return indicating the amount to be included in the gross income of the recipient, regardless of the amount involved.

Explanation of the bill

The bill would provide that disallowance of expenses for entertainment, amusement, or recreation expenses (Code sec. 274(a)) does not apply to expenses which are includible in the gross income of the recipient of the entertainment, amusement, or recreation as compensation for services or as a prize or award under Code section 74. This exception would not apply to a payor unless he furnishes the Internal Revenue Service with any required information return (Form 1099) indicating the amount to be included in the gross income of the payee, regardless of the amount involved.

Effective date

The bill would be effective to expenses paid or incurred after December 31, 1980.

Revenue effect

It is estimated that this bill will have no direct effect on budget receipts.

8. H.R. 7487—Messrs. Guarini, Rostenkowski, Florio and Madigan

Excise Tax On Lighter Gauge Steel Drums

Present law

Under present law, there is no excise tax imposed on lighter gauge or other steel drums.

Issue

The issues raised by this bill include the following:

(1) Whether an excise tax should be imposed upon lighter gauge steel drums in order to encourage the use of heavier gauge steel drums which can be reconditioned and re-used more times.

(2) Whether increased use of heavier gauge steel drums will reduce the volume of drums disposed of without reconditioning and thereby minimize the risk of contamination of the environment from residues in the drums disposed of.

(3) Whether any increased use of drums which can be reconditioned more times will result in significant energy savings.

Explanation of the bill

The bill would impose an excise tax on the sale by the manufacturer, producer, or importer of lighter gauge steel drums. The tax would be 20 percent of the sale price. Under the provisions of the bill, a lighter gauge steel drum means any drum the body of which is of steel sheet lighter than 18 gauge and which has a liquid capacity of at least 35, but no more than 65, United States gallons. In general, the tax would apply to drums which cannot be reconditioned or can be reconditioned only two or three times.

Effective date

The bill would apply with respect to sales after the 180th day after the date of enactment.

Revenue effect

It is estimated that this bill will increase budget receipts by less than $10 million in fiscal year 1981, by less than $5 million annually in 1982 and 1983, and by negligible amounts in later years.

9. H.R. 7520—Messrs. Ullman, Gore, Pickle, Jones (Okla.), Jenkins, Lederer, Fowler, Duncan (Tenn.), Frenzel, Martin, and Moore

Tax Treatment of Mutual or Cooperative Telephone and Electric Companies

Present law

Rural cooperatives

Under present law (Code sec. 501(c)(12)), a mutual or cooperative telephone company qualifies for exemption from Federal income taxation only if at least 85 percent of its income consists of "amounts collected from members for the sole purpose of meeting losses and expenses." In determining whether this member-income test has been satisfied, amounts of credits accrued or received by a mutual or cooperative telephone company from other company for communications services on calls involving members of the telephone cooperative are not taken into account.

Similarly, a rural electric cooperative may qualify for exemption from Federal income taxation under Code section 501(c)(12) if it satisfies the 85-percent member-income test.[1]

Tax on unrelated business income

Under present law, most organizations which are generally tax exempt under the Internal Revenue Code are nonetheless subject to tax on unrelated business taxable income (Code sec. 511). Thus, unless a specific exception applies, an organization which is tax-exempt (under Code sec. 501(a))[2] is subject to tax with respect to income derived from any trade or business the conduct of which is not substantially related (aside from the need of the organization for income or funds) to the exercise or performance of its exempt function.

Issues

Recently, the Internal Revenue Service has indicated that income from the rental of poles (*e.g.*, payments by a rural electric cooperative for use of a rural telephone cooperative's poles) and display listings

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[1] See Rev. Rul. 65-99, 1965-1 C.B. 242; Rev. Rul. 65-174, 1965-2, C.B. 169. In addition, certain rural electric cooperatives in the Tennessee Valley Authority ("TVA") area are exempt from taxation under Code section 501(c)(4) even though, generally because of TVA requirements, they do not meet the 85-percent member-income test. See *U.S.* v. *Pickwick Electric Membership Corp.*, 158 F.2d 272 (6th Cir. 1946).

[2] In this pamphlet, references to "tax-exempt organizations" do not include social clubs (Code sec. 501(c)(7)) and employees' beneficiary associations (Code sec 501(c)(9)), which are taxable on investment income of all types as well as unrelated business income. The term "tax-exempt organizations," as used in this pamphlet also does not include political organizations (described in Code sec. 527) and homeowners' associations (described in Code sec. 528).

in "Yellow Page" directories may be included in nonmember income of rural cooperatives.

The issues are whether income from pole rentals and display listings should be treated as nonmember income for purposes of the 85-percent member-income test and whether income from pole rentals should be subject to the tax on unrelated business taxable income.

Explanation of the bill

The bill would provide that, in applying the 85-percent member-income test to a mutual or cooperative telephone company, any income from qualified pole rentals or from display listings in a telephone directory is to be disregarded. Also, in applying the 85-percent nonmember-income test to mutual or cooperative electric companies, any income from qualified pole rentals is to be disregarded. Income from qualified pole rentals generally means any income from the sale of the right to use any pole (or other structure) (1) which is used by the cooperative in providing telephone or electric services to its members, and (2) the use for which the pole is rented involves the transmission by wire of electricity or of telephone or other communications.

The bill also would provide that the engaging in activities which result in the receipt of qualified pole rentals is not an unrelated trade or business for a mutual or cooperative telephone or electric company. Thus, such rentals would not be subject to the tax on unrelated business taxable income.

Effective date

The amendments relating to the 85-percent member-income test would apply to all taxable years to which the Internal Revenue Code of 1954 applies.

The amendments to the unrelated business income provisions would apply to all taxable years beginning after December 31, 1969 (the general effective date of the Tax Reform Act of 1969, which applied the tax on unrelated business taxable income to organizations exempt under Code sec. 501(c)(12)).

Revenue effect

It is estimated that this bill will reduce budget receipts by less than $5 million annually.

10. H.R. 7606[1]—Mr. Ullman

Employee Stock Ownership Improvements Act of 1980

1. Cash distribution option and put option for stock bonus plans (sec. 2 of the bill and new sec. 401(a)(22) of the Code)

Present law

Under present law, tax-qualified stock bonus plans must generally distribute stock to participants entitled to a distribution. However, a stock bonus plan which is either a tax credit employee stock ownership plan or an employee stock ownership plan may distribute cash, subject to a participant's right to demand that benefits be distributed in the form of employer securities.

Issue

The issue is whether a tax-qualified stock bonus plan generally should be eligible for the same rules with respect to cash and stock distributions to participants which govern tax credit employee stock ownership plans and employee stock ownership plans.

Explanation of provision

The provision would permit a tax-qualified stock bonus plan to distribute cash to a participant entitled to a distribution, subject to the participant's right to demand that benefits be distributed in the form of employer stock. If a stock bonus plan provides for cash distributions and if stock which is distributed is not readily tradable on an established market, the participant would have to have the right to require the employer to repurchase the stock.

Effective date

The provision would be effective for plan years beginning after December 31, 1979.

Revenue effect

It is estimated that this provision will not have any revenue effect.

2. Special limitation for tax credit employee stock ownership plans and employee stock ownership plans (sec. 3 of the bill and sec. 415(c)(6)(A) of the Code)

Present law

Under present law, the dollar limitation on annual additions with respect to a participant in a tax credit employee stock ownership plan or an employee stock ownership plan may be increased, provided certain requirements with respect to allocations of employer contributions

[1] The provisions of this bill have been reported by the Senate Finance Committee as amendments to H.R. 2492 (secs. 301, 303–306, 405, 408 and 409; S. Rept. 96–684).

are met. The amount of such increase is the lesser of (1) the usual dollar limitation on annual additions to a participant's account or (2) the amount of employer securities contributed to the plan.

Issue

The issue is whether a clarifying change to the rule of present law which allows an increase in the limitation on contributions with respect to a participant in a tax credit employee stock ownship plan or an employee stock ownership plan is needed to make it clear that cash used to purchase employer securities is included for purposes of determining the limitation on annual additions to a participant's account.

Explanation of provision

Under the provision, the increase in the dollar limitation on annual additions with respect to a participant in a tax credit employee stock ownership plan or an employee stock ownership plan (provided certain requirements are met with respect to allocations under the plan) would be the lesser of (1) the usual dollar limitation on annual additions to a participant's account, or (2) the amount of employer securities (or cash used to acquire such securities) contributed to the plan.

Effective date

The provision would be effective for years beginning after December 31, 1979.

Revenue effect

It is estimated that this provision will not have any revenue effect.

3. Valuation of employer securities in tax credit employee stock ownership plans (sec. 4 of the bill and sec. 48(n)(B)(i) of the Code)

Present law

Under present law, the value of employer securities listed on a national exchange which are contributed to a tax credit employee stock ownership plan is the average of closing prices for such securities for the 20 consecutive trading days immediately preceding the due date for filing the employer's tax return for the year (including extensions).

Issue

The issue is whether the average closing price of employer securities during the 20 trading days preceding the date of contribution to a plan should be used to determine the value of those securities. It is said that the provision of present law for valuing readily tradable employer securities contributed to a tax credit employee stock ownership plan causes employers to postpone contributions of employer securities to a tax credit employee stock ownership plan until the due date for filing the employer's tax return.

Explanation of provision

Under the bill, the value of employer securities listed on a national exchange contributed to a tax credit employee stock ownership plan would be the average of the closing prices of such securities for the

20 consecutive trading days immediately preceding the date of contribution to the plan.

Effective date

The provision would be effective for taxable years beginning after December 31, 1979.

Revenue effect

It is estimated that this provision will not have any revenue effect.

4. Participation of subsidiary corporation in a tax credit employee stock ownership plan (sec. 5 of the bill and sec. 409A (*1*)(4) of the Code

Present law

The present-law rules governing tax credit employee stock ownership plans permit a 50-percent owned first-tier subsidiary of a parent corporation, and 80-percent owned second and lower-tier subsidiaries, to conribute employer securities of the parent corporation to a tax credit employee stock ownership plan.

Issue

The issue is whether in the case where a first-tier subsidiary corporation owns 50 percent of a second-tier subsidiary and the first-tier subsidiary is 100-percent owned by a parent corporation, sufficient control of the second-tier subsidiary by the parent corporation exists to permit the second-tier subsidiary to contribute employer securities of the parent to a tax credit employee stock ownership plan.

Explanation of provision

Under the provision, if a parent corporation owns 100 percent of a first-tier subsidiary and the first-tier subsidiary owns 50 percent of a second-tier subsidiary, the second-tier subsidiary is allowed to contribute employer securities of the parent corporation to its tax credit employee stock ownership plan. In addition, parent stock could be contributed by 80-percent owned lower-tier subsidiaries in this chain.

Effective date

The provision would be effective as if it had been included in section 141 of the Revenue Act of 1978.

Revenue effect

It is estimated that this provision will not have any revenue effect.

5. Retirement savings by tax credit employee stock ownership plan participants (sec. 6 of the bill and sec. 410(b)(1) of the Code)

Present law

Under present law, an employee who is an active participant in a tax-qualified plan during a year is not eligible to make deductible contributions to an IRA (individual retirement account, individual retirement annuity, or retirement bond). Therefore, if an employee is an active participant in a tax-qualified tax credit employee stock ownership plan during a year such employee is ineligible for an IRA. A plan can allow an employee to elect not to participate in a tax credit employee stock ownership plan in order to allow the employee to establish an IRA. However, the plan may be unable to satisfy certain minimum requirements of the Code relating to employee eligibility for plan participation (sec. 410(b)(1)).

Issue

The issue is whether in the case where the only tax-qualified plan maintained by an employer is a tax credit employee stock ownership plan and if the value of employer securities allocated to employees' accounts under the tax credit employee stock ownership plan is relatively low, the minimum coverage requirements for tax-qualification of the tax credit employee stock ownership plan should be modified to permit employees to elect out of the plan, if the plan so provides, to establish IRAs.

Explanation of provision

Under the provision, the minimum coverage requirement for a tax credit employee stock ownership plan would be changed, if a tax credit employee stock ownership plan is the only tax-qualified plan maintained by an employer. If employees are permitted to elect out of the tax credit employee stock ownership plan for the purpose of establishing IRAs, the tax credit employee stock ownership plan would not fail to meet the minimum coverage requirements of the Code if the plan benefits at least 50 percent of all employees (excluding employees who have not satisfied the minimum age and service requirements or who are otherwise permitted to be excluded), and if the total allocations under the tax credit employee stock ownership plan are equal to no more than two percent of the compensation of participating employees.

Effective date

The provision would be effective for plan years beginning after December 31, 1979.

Revenue effect

It is estimated that this provision will decrease budget receipts by less than $5 million annually.

6. Certain distributions from money purchase pension plans (sec. 7 of the bill and sec. 402(a)(6) of the Code)

Present law

An employee who receives a lump sum distribution from a tax-qualified pension, profit-sharing, or stock bonus plan may defer tax on the distribution by rolling over the proceeds (net of any employee contributions) within 60 days of receipt (1) to an IRA (an individual retirement account, annuity, or bond), (2) to another qualified pension, etc., plan. The rollover rule also applies to the spouse of an employee who receives a lump sum distribution on account of the employee's death. A lump sum distribution from a qualified plan is eligible for favorable income tax treatment (e.g., 10-year income-averaging) if no portion of the distribution is rolled over.

A distribution may be rolled over if it is a distribution of the balance to the credit of an employee under a qualified pension, etc., plan, made within one taxable year of the recipient. Generally, the distribution must have been made on account of death, separation for service, or the attainment of age 59½. If an employer maintains more than one qualified plan of the same type, the plans are aggregated for the purpose of determining whether the balance to the credit of an employee has been distributed. Under the aggregation rules, all pension plans (defined benefit and money purchase) maintained by the employer are treated as a single plan, all profit-sharing plans maintained by the employer are treated as a single plan, and all stock bonus plans maintained by the employer are treated as a single plan.

Issue

The issue is whether the lump sum distribution rollover rules are too restrictive in the case where an employer maintains both a pension plan and a money purchase pension plan for its employees.

Explanation of provision

The bill would allow an employee who receives a total distribution (which otherwise meets the requirements for a tax-free rollover) from a qualified money purchase pension plan to roll over the distribution to an IRA or to another qualified plan where the employer also maintains a defined benefit pension plan covering the employee and a total distribution is not made from the defined benefit plan in the same taxable year. The provision would also apply to the spouse of an employee if the spouse receives such a total distribution on account of the employee's death.

If the recipient rolls over a total distribution from a money purchase pension plan and, in a subsequent taxable year, receives a total distribution from a qualified defined benefit pension plan maintained by the employer, the later plan distribution could be rolled over tax-free (if it otherwise qualifies for tax-free rollover treatment) but would not otherwise be eligible for the favorable income tax treatment accorded lump sum distributions.

Effective date

Generally, this provision would apply to payments made in taxable years beginning after December 31, 1978. In the case of such payments made after December 31, 1978, and before January 1, 1981, the period for making a rollover would not expire before December 31, 1980.

Revenue effect

It is estimated that this provision will decrease budget receipts by less than $5 million annually.

7. Voting rights passthrough requirements for defined contribution plans (sec. 8 of the bill and sec. 410(a)(22) of the Code)

Present law

Under present law, a tax-qualified defined contribution plan is required to pass through voting rights on employer securities to plan participants with respect to major corporate issues under certain circumstances. The vote pass-through applies if (1) the employer which established the plan does not have a class of publicly traded stock, (2) the plan acquired employer securities after December 31, 1979, and (3) after the acquisition more than 10 percent of the plan's total assets are invested in employer securities.

Issue

The issue is whether this requirement will inhibit the contribution of closely held employer securities to defined contribution plans, such as stock bonus plans and profit-sharing plans.

Explanation of provision

The provision would repeal the present law rule under which a tax-qualified defined contribution plan, established by an employer whose stock is not publicly traded, which acquires employer securities after December 31, 1979, and thereafter holds more than 10 percent of its assets in employer securities, is required to pass through to plan participants voting rights on major corporate issues with respect to employer securities held by the plan. The provision does not change the special vote pass-through rules for tax credit employee stock ownership plans.

Effective date

The provision would be effective for securities acquired after December 31, 1979.

Revenue effect

It is estimated that this provision will not have any revenue effect.

8. Cafeteria plans permitted to provide deferred compensation under rules applicable to cash or deferred profit-sharing and stock bonus plans (sec. 9 of the bill and secs. 125 and 410(k) of the Code)

Present law

A cafeteria plan is an employee benefit plan under which a participant may choose between taxable benefits and one or more nontaxable fringe benefits. Under present law, cafeteria plans are not permitted to provide deferred compensation.

Issue

Both cafeteria plans and cash or deferred profit-sharing plans allow employees to choose between current compensation and other benefits. The issue is whether present law is too restrictive because it does not permit employees to choose among currently taxable compensation, deferred compensation, and fringe benefits under a single plan.

Explanation of provision

Under the bill, benefits under a cafeteria plan could include amounts which an employee covered by a profit-sharing or stock bonus plan with a qualified cash or deferred arrangement can elect to have the employer pay as a contribution to a trust under a profit-sharing or stock bonus plan. Amounts contributed by the employer, pursuant to the employee's election, will be treated as nontaxable benefits for purposes of the "cafeteria" plan rules.

Effective date

The provision would be effective for taxable years beginning after December 31, 1979.

Revenue effect

It is estimated that this provision will decrease budget receipts by less than $5 million annually.

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