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ARMED FORCES TAX FAIRNESS ACT OF 2002

SEPTEMBER 17, 2002.—Ordered to be printed

Mr. BAUCUS, from the Committee on Finance, submitted the following

REPORT

[To accompany H.R. 5063]

[Including cost estimate of the Congressional Budget Office]

The Committee on Finance, to which was referred the bill (H.R. 5063) to amend the Internal Revenue Code of 1986 to provide a special rule for members of the uniformed services in determining the exclusion of gain from the sale of a principal residence, and to restore the tax exempt status of death gratuity payments to members of the uniformed services, having considered the same, reports favorably thereon with an amendment in the nature of a substitute and recommends that the bill, as amended, do pass.

CONTENTS

99–010

I. LEGISLATIVE BACKGROUND

The Senate Committee on Finance marked up H.R. 5063 (the Armed Forces Tax Fairness Act of 2002) on September 12, 2002, and ordered the bill, as amended, favorably reported by unanimous voice vote.

The Committee believes, especially around the first anniversary of the September 11th attacks, that consideration should be paid to the men and women who are leading America's response and serving our country. These men and women include: (1) members of the Armed Forces deployed overseas; (2) members of the National Guard protecting our borders and airports; and (3) Foreign Service officers serving in dangerous diplomatic posts.

The Committee believes, in addition to our thoughts and thanks, that these individuals deserve to be treated appropriately under the tax laws. The modest sensible provisions included in this legislation are the result of a bipartisan effort to correct the tax treatment of those individuals serving their country in the uniformed services, reserves and Foreign Service.

The bill also contains two provisions that raise revenue to offset the cost of the other provisions. In the case of the provision to modify the tax treatment of certain individual expatriates, these provisions seem especially fitting to offset the improved tax treatment of the men and women serving their country.

II. EXPLANATION OF THE BILL

TITLE I. IMPROVING TAX EQUITY FOR MILITARY PERSONNEL

A. Exclusion From Gross Income of Certain Death Gratuity Payments

PRESENT LAW

Present law provides that qualified military benefits are not included in gross income. Generally, a qualified military benefit is any allowance or in-kind benefit (other than personal use of a vehicle) which: (1) is received by any member or former member of the uniformed services of the United States or any dependent of such member by reason of such member's status or service as a member of such uniformed services; and (2) was excludable from gross income on September 9, 1986, under any provision of law, regulation, or administrative practice which was in effect on such date. Generally, other than certain cost of living adjustments no modification or adjustment of any qualified military benefit after September 9, 1986, is taken into account for purposes of this exclusion from gross income. Qualified military benefits include certain death gratuities.

REASONS FOR CHANGE

The Committee believes that the amount of the exclusion for these death gratuities should be conformed to the present-law levels of such death gratuities. Further, the Committee believes that the amount of the exclusion should be automatically adjusted for future changes in these death gratuities.

EXPLANATION OF PROVISION

The bill extends the exclusion from gross income to any adjustment to the amount of the death gratuity payable under Chapter 75 of Title 10 of the United States Code.

EFFECTIVE DATE

The provision is effective with respect to deaths occurring after September 10, 2001.

B. Exclusion of Gain on Sale of a Principal Residence by a Member of the Uniformed Services or the Foreign Service

PRESENT LAW

Under present law, an individual taxpayer may exclude up to $250,000 ($500,000 if married filing a joint return) of gain realized on the sale or exchange of a principal residence. To be eligible for the exclusion, the taxpayer must have owned and used the residence as a principal residence for at least 2 of the 5 years prior to the sale or exchange. A taxpayer who fails to meet these requirements by reason of a change of place of employment, health, or, to the extent provided under regulations, unforeseen circumstances is able to exclude an amount equal to the fraction of the $250,000 ($500,000 if married filing a joint return) that is equal to the fraction of the 2 years that the ownership and use requirements are met. There are no special rules relating to members of the uniformed services, or the Foreign Service of the United States.

REASONS FOR CHANGE

The Committee believes that members of the uniformed services and the Foreign Service of the United States who would otherwise qualify for the exclusion of the gain on the sale of a principal residence should not be deprived the exclusion because of service to their country.

EXPLANATION OF PROVISION

Under the bill, an individual may elect to suspend for a maximum of 10 years the 5-year test period for ownership and use during certain absences due to service in the uniformed services, or Foreign Service of the United States. The uniformed services include: (1) the armed forces (the Army, Navy, Air Force, Marine Corps, and Coast Guard); (2) the commissioned corps of the National Oceanic and Atmospheric Administration; and (3) the commissioned corps of the Public Health Service. If the election is made, the 5-year period ending on the date of the sale or exchange of a principal residence does not include any period up to 5 years during which the taxpayer or the taxpayer's spouse is on qualified official extended duty as a member of the uniformed services, or in Foreign Service of the United States. For these purposes, qualified official extended duty is any period of extended duty by a member of the uniformed services, or the Foreign Service of the United States while serving at a place of duty at least 50 miles away from the taxpayer's principal residence or under orders compelling residence in Government furnished quarters. Extended duty is defined as any period of duty pursuant to a call or order to such duty for a period in excess of 90 days or for an indefinite period. The election may be made with respect to only one property for a suspension period.

EFFECTIVE DATE

The provision is effective for elections made with respect to sales after the date of enactment.

C. Exclusion for Amounts Received Under Department of Defense Homeowners Assistance Program

PRESENT LAW

HAP payment

The Department of Defense Homeowners Assistance Program (HAP) provides payments to certain employees and members of the Armed Forces to offset the adverse effects on housing values that result from military base realignment or closure. The payments are authorized under the provisions of Title 42, U.S.C., section 3374.

HAP provides payments to eligible individuals who may, in general, either (1) receive a cash payment as compensation for losses that may be or have been sustained in a private sale, in an amount not to exceed the difference between (a) 95 percent of the fair market value of their property prior to public announcement of intention to close all or part of the military base or installation and (b) the fair market value of such property at the time of the sale, or (2) receive, as the purchase price for their property, an amount not to exceed 90 percent of the prior fair market value as such value is determined by the Secretary of Defense, or the amount of the outstanding mortgages.

Tax treatment

Unless specifically excluded, gross income for Federal income tax purposes includes all income from whatever source derived. Amounts received under HAP are received in connection with the performance of services, and thus are includable in gross income as compensation for services. Additionally, such payments are "wages" for Federal Insurance Contributions Act tax purposes (including Medicare).

REASONS FOR CHANGE

The Committee believes that the exemption from gross income and FICA taxes is necessary to provide full compensation for the losses in home values incurred as a result of military base realignment or closure. The Committee further believes that this will help to facilitate necessary military base realignment or closure.

EXPLANATION OF PROVISION

The bill exempts from gross income amounts received under the Homeowners Assistance Program. Amounts received under the program are also not considered wages for Federal Insurance Contributions Act tax purposes (including Medicare).

EFFECTIVE DATE

The provision is effective for payments made after the date of enactment.

D. Expansion of Combat Zone Filing Rules to Contingency Operations

PRESENT LAW

General time limits for filing tax returns

Individuals generally must file their Federal income tax returns by April 15 of the year following the close of a taxable year (sec. 6072). The Secretary may grant reasonable extensions of time for filing such returns (sec. 6081). Treasury regulations provide an additional automatic 2-month extension (until June 15 for calendar-year individuals) for United States citizens and residents in military or naval service on duty on April 15 of the following year (the otherwise applicable due date of the return) outside the United States (Treas. Reg. sec. 1.6081–5(a)(6)). No action is necessary to apply for this extension, but taxpayers must indicate on their returns (when filed) that they are claiming this extension. Unlike most extensions of time to file, this extension applies to both filing returns and paying the tax due.

Treasury regulations also provide, upon application on the proper form, an automatic 4-month extension (until August 15 for calendar-year individuals) for any individual timely filing that form and paying the amount of tax estimated to be due (Treas. Reg. sec. 1.6081–4).

In general, individuals must make quarterly estimated tax payments by April 15, June 15, September 15, and January 15 of the following taxable year. Wage withholding is considered to be a payment of estimated taxes.

Suspension of time periods

In general, the period of time for performing various acts under the Internal Revenue Code, such as filing tax returns, paying taxes, or filing a claim for credit or refund of tax, is suspended for any individual serving in the Armed Forces of the United States in an area designated as a "combat zone" during the period of combatant activities (sec. 7508). An individual who becomes a prisoner of war is considered to continue in active service and is therefore also eligible for these suspension of time provisions. The suspension of time also applies to an individual serving in support of such Armed Forces in the combat zone, such as Red Cross personnel, accredited correspondents, and civilian personnel acting under the direction of the Armed Forces in support of those Forces. The designation of a combat zone must be made by the President in an Executive order. The President must also designate the period of combatant activities in the combat zone (the starting date and the termination date of combat).

The suspension of time encompasses the period of service in the combat zone during the period of combatant activities in the zone, as well as (1) any time of continuous qualified hospitalization resulting from injury received in the combat zone[1] or (2) time in missing in action status, plus the next 180 days.

The suspension of time applies to the following acts:

(1) Filing any return of income, estate, or gift tax (except employment and withholding taxes);

(2) Payment of any income, estate, or gift tax (except employment and withholding taxes);

(3) Filing a petition with the Tax Court for redetermination of a deficiency, or for review of a decision rendered by the Tax Court;

(4) Allowance of a credit or refund of any tax;

(5) Filing a claim for credit or refund of any tax;

(6) Bringing suit upon any such claim for credit or refund;

(7) Assessment of any tax;

(8) Giving or making any notice or demand for the payment of any tax, or with respect to any liability to the United States in respect of any tax;

(9) Collection of the amount of any liability in respect of any tax;

(10) Bringing suit by the United States in respect of any liability in respect of any tax; and

(11) Any other act required or permitted under the internal revenue laws specified by the Secretary of the Treasury.

Individuals may, if they choose, perform any of these acts during the period of suspension.

Spouses of qualifying individuals are entitled to the same suspension of time, except that the spouse is ineligible for this suspension for any taxable year beginning more than 2 years after the date of termination of combatant activities in the combat zone.

REASONS FOR CHANGE

The Committee believes that military personnel deployed outside the United States away from their permanent duty station while participating in a contingency operation should be entitled to utilize the same suspension of time provisions as those deployed in a combat zone.

EXPLANATION OF PROVISION

The bill applies the special suspension of time period rules to persons deployed outside the United States away from the individual's permanent duty station while participating in an operation designated by the Secretary of Defense as a contingency operation

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[1] Two special rules apply to continuous hospitalization inside the United States. First, the suspension of time provisions based on continuous hospitalization inside the United States are applicable only to the hospitalized individual; they are not applicable to the spouse of such individual. Second, in no event do the suspension of time provisions based on continuous hospitalization inside the United States extend beyond 5 years from the date the individual returns to the United States. These two special rules do not apply to continuous hospitalization outside the United States.

or that becomes a contingency operation. A contingency operation is defined[2] as a military operation that is designated by the Secretary of Defense as an operation in which members of the Armed Forces are or may become involved in military actions, operations, or hostilities against an enemy of the United States or against an opposing military force, or results in the call or order to (or retention on) active duty of members of the uniformed services during a war or a national emergency declared by the President or Congress.

EFFECTIVE DATE

The provision applies to any period for performing an act that has not expired before the date of enactment.

E. ABOVE-THE-LINE DEDUCTION FOR OVERNIGHT TRAVEL EXPENSES OF NATIONAL GUARD AND RESERVE MEMBERS

PRESENT LAW

National Guard and Reserve members may claim itemized deductions for their nonreimbursable expenses for travel, meals, and lodging when they must travel away from home (and stay overnight) to attend National Guard and Reserve meetings. These overnight travel expenses are combined with other miscellaneous itemized deductions on Schedule A of the individual's income tax return and are deductible only to the extent that the aggregate of these deductions exceeds two percent of the taxpayer's adjusted gross income. No deduction is generally permitted for commuting expenses to and from drill meetings.

REASONS FOR CHANGE

The Committee believes that all National Guard and Reserve members incurring unreimbursed overnight expenses to attend National Guard and Reserve meetings should be able to deduct these expenses from their income, not just those who itemize their deductions. Accordingly, the Committee provides an above-the-line deduction for these expenses.

EXPLANATION OF PROVISION

The bill provides an above-the-line deduction for the unreimbursed overnight travel, meals, and lodging expenses of National Guard and Reserve members who must travel away from home (and stay overnight) as part of their official duties. Accordingly, these individuals incurring these expenses may deduct them from gross income regardless of whether they itemize their deductions. Expenses eligible for this provision include unreimbursed expenses to attend National Guard and Reserve meetings as well as unreimbursed expenses incurred as part of a mobilization ordered by either the President or the Governor. The amount of the expenses that may be deducted may not exceed the general Government per diem rate applicable to that locale.

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[2] The definition is done by cross-reference to 10 U.S.C. 101.

EFFECTIVE DATE

The provision is effective for amounts paid or incurred in taxable years beginning after December 31, 2001.

F. Modification of Membership Requirement for Exemption From Tax for Certain Veterans' Organizations

PRESENT LAW

Under present law, a veterans' organization as described in section 501(c)(19) of the Code generally is exempt from taxation. The Code defines such an organization as a post or organization of past or present members of the Armed Forces of the United States (1) that is organized in the United States or any of its possessions; (2) no part of the net earnings of which inures to the benefit of any private shareholder or individual; and (3) that meets certain membership requirements. The membership requirements are that (1) at least 75 percent of the organization's members are past or present members of the Armed Forces of the United States, and (2) substantially all of the remaining members are cadets or are spouses, widows, or widowers of past or present members of the Armed Forces of the United States or of cadets. No more than 2.5 percent of an organization's total members may consist of individuals who are not veterans, cadets, or spouses, widows, or widowers of such individuals.[3]

Contributions to an organization described in section 501(c)(19) may be deductible for Federal income or gift tax purposes if the organization is a post or organization of war veterans.[4]

REASONS FOR CHANGE

As the membership of veterans' organizations changes due to aging and the deaths of members, veterans' organizations that currently qualify for tax exemption under section 501(c)(19) may cease to qualify for exempt status under that section, even though the membership, apart from changes due to deaths, remains the same. The Committee believes that a limited expansion of the membership of veterans' organizations will enable certain of such organizations to retain exempt status, which might otherwise be in jeopardy, and will not unduly expand the membership base beyond persons with a close connection to members of the Armed Forces or cadets.

EXPLANATION OF PROVISION

The bill permits ancestors or lineal descendants of past or present members of the Armed Forces of the United States or of cadets to qualify as members for purposes of the "substantially all" test. The bill does not change the requirement that 75 percent of the organization's members must be past or present members of the Armed Forces of the United States.

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[3] Treas. Reg. sec. 1.501(c)(19)–1(b)(2). The Treasury has not amended this regulation to reflect changes made by P.L. 97–248.

[4] Sec. 170(c)(3); sec. 2522(a)(4).

EFFECTIVE DATE

The provision is effective for taxable years beginning after the date of enactment.

G. Clarification of Treatment of Certain Dependent Care Assistance Programs Provided to Members of the Uniformed Services of the United States

PRESENT LAW

Present law provides that qualified military benefits are not included in gross income. Generally, a qualified military benefit is any allowance or in-kind benefit (other than personal use of a vehicle) which: (1) is received by any member or former member of the uniformed services of the United States or any dependent of such member by reason of such member's status or service as a member of such uniformed services; and (2) was excludable from gross income on September 9, 1986, under any provision of law, regulation, or administrative practice which was in effect on such date. Generally, other than certain cost of living adjustments, no modification or adjustment of any qualified military benefit after September 9, 1986, is taken into account for purposes of this exclusion from gross income.

REASONS FOR CHANGE

The Committee believes that it is important to remove any uncertainty regarding the tax treatment of dependent care assistance provided to members of the uniformed services.

EXPLANATION OF PROVISION

The bill clarifies that dependent care assistance provided under a dependent care assistance program for a member of the uniformed services by reason of such member's status or service as a member of the uniformed services is excludable from gross income as a qualified military benefit. The uniformed services include: (1) the armed forces (the Army, Navy, Air Force, Marine Corps, and Coast Guard); (2) the commissioned corps of the National Oceanic and Atmospheric Administration; and (3) the commissioned corps of the Public Health Service. Amounts received under the program are also not considered wages for Federal Insurance Contributions Act tax purposes (including Medicare).

EFFECTIVE DATE

The provision is effective for taxable years beginning after December 31, 2001. No inference is intended as to the tax treatment of such amounts for prior taxable years.

TITLE II. OTHER PROVISIONS

A. Impose Mark-to-Market Tax on Individuals Who Expatriate

PRESENT LAW

In general

U.S. citizens and residents generally are subject to U.S. income taxation on their worldwide income. The U.S. tax may be reduced or offset by a credit allowed for foreign income taxes paid with respect to foreign-source income. Nonresidents who are not U.S. citizens are taxed at a flat rate of 30 percent (or a lower treaty rate) on certain types of passive income derived from U.S. sources, and at regular graduated rates on net profits derived from a U.S. business.

Income tax rules with respect to expatriates

An individual who relinquishes his or her U.S. citizenship or terminates his or her U.S. residency with a principal purpose of avoiding U.S. taxes is subject to an alternative method of income taxation for the 10 taxable years ending after the expatriation or residency termination under section 877. The alternative method of taxation for expatriates modifies the rules generally applicable to the taxation of nonresident noncitizens in several ways. First, the individual is subject to tax on his or her U.S.-source income at the rates applicable to U.S. citizens rather than the rates applicable to other nonresident noncitizens. Unlike U.S. citizens, however, individuals subject to section 877 are not taxed on foreign-source income. Second, the scope of items treated as U.S.-source income for section 877 purposes is broader than those items generally considered to be U.S.-source income under the Code.[5] Third, individuals subject to section 877 are taxed on exchanges of certain types of property that give rise to U.S.-source income for property that gives rise to foreign-source income.[6] Fourth, an individual subject to section 877 who contributes property to a controlled foreign corporation is treated as receiving income or gain from such property directly and is taxable on such income or gain. The alternative method of taxation for expatriates applies only if it results in a higher U.S. tax liability than would otherwise be determined if the individual were taxed as a nonresident noncitizen.

The expatriation tax provisions apply to long-term residents of the United States whose U.S. residency is terminated. For this purpose, a long-term resident is any individual who was a lawful permanent resident of the United States for at least 8 out of the 15 taxable years ending with the year in which such termination occurs. In applying the 8-year test, an individual is not considered to be a lawful permanent resident for any year in which the individual is treated as a resident of another country under a treaty tie-breaker rule (and the individual does not elect to waive the benefits of such treaty).

Subject to the exceptions described below, an individual is treated as having expatriated or terminated residency with a principal purpose of avoiding U.S. taxes if either: (1) the individual's average annual U.S. Federal income tax liability for the 5 taxable years ending before the date of the individual's loss of U.S. citizenship or

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[5] For example, gains on the sale or exchange of personal property located in the United States, and gains on the sale or exchange of stocks and securities issued by U.S. persons, generally are not considered to be U.S.-source income under the Code. Thus, such gains would not be taxable to a nonresident noncitizen. However, if an individual is subject to the alternative regime under sec. 877, such gains are treated as U.S.-source income with respect to that individual.

[6] For example, a former citizen who is subject to the alternative tax regime and who removes appreciated artwork that he or she owns from the United States could be subject to immediate U.S. tax on the appreciation. In this regard, the removal from the United States of appreciated tangible personal property having an aggregate fair market value in excess of $250,000 within the 15-year beginning 5 years prior to the expatriation will be treated as an "exchange" subject to these rules.

termination of U.S. residency is greater than $100,000 (the "tax liability test"), or (2) the individual's net worth as of the date of such loss or termination is $500,000 or more (the "net worth test"). The dollar amount thresholds contained in the tax liability test and the net worth test are indexed for inflation in the case of a loss of citizenship or termination of residency occurring in any calendar year after 1996. For calendar year 2002, the dollar thresholds for the tax liability test and the net worth test are $120,000 and $599,000, respectively. An individual who falls below these thresholds is not automatically treated as having a principal purpose of tax avoidance, but nevertheless is subject to the expatriation tax provisions if the individual's loss of citizenship or termination of residency in fact did have as one of its principal purposes the avoidance of tax.

Certain exceptions from the treatment that an individual relinquished his or her U.S. citizenship or terminated his or her U.S. residency for tax avoidance purposes may also apply. For example, a U.S. citizen who loses his or her citizenship and who satisfies either the tax liability test or the net worth test (described above) can avoid being deemed to have a principal purpose of tax avoidance if the individual falls within certain categories (such as being a dual citizen) and the individual, within 1 year from the date of loss of citizenship, submits a ruling request for a determination by the Secretary of the Treasury as to whether such loss had as one of its principal purposes the avoidance of taxes.

Estate tax rules with respect to expatriates

Nonresident noncitizens generally are subject to estate tax on certain transfers of U.S.-situated property at death.[7] Such property includes real estate and tangible property located within the United States. Moreover, for estate tax purposes, stock held by nonresident noncitizens is treated as U.S.-situated if issued by a U.S. corporation.

Special rules apply to U.S. citizens who relinquish their citizenship and long-term residents who terminate their U.S. residency within the 10 years prior to the date of death, unless the loss of status did not have as one its principal purposes the avoidance of tax (sec. 2107). Under these rules, the decedent's estate includes the proportion of the decedent's stock in a foreign corporation that the fair market value of the U.S.-situs assets owned by the corporation bears to the total assets of the corporation. This rule applies only if (1) the decedent owned, directly, at death 10 percent or more of the combined voting power of all voting stock of the corporation and (2) the decedent owned, directly or indirectly, at death more than 50 percent of the total voting stock of the corporation or more than 50 percent of the total value of all stock of the corporation.

Taxpayers are deemed to have a principal purpose of tax avoidance if they meet the 5-year tax liability test or the net worth test, discussed above. Exceptions from this tax avoidance treatment apply in the same circumstances as those described above (relating to certain dual citizens and other individuals who submit a timely

[7] The Economic Growth and Tax Relief Reconcilation Act of 2001 (the Act) repealed the estate tax for estates of decedents dying after December 31, 2009. However, the Act included a "sunset" provision, pursuant to which the Act's provisions (including estate tax repeal) do not apply to estates of decedents dying after December 31, 2010.

and complete ruling request with the IRS as to whether their expatriation or residency termination had a principal purpose of tax avoidance).

Gift tax rules with respect to expatriates

Nonresident noncitizens generally are subject to gift tax on certain transfers by gift of U.S.-situated property. Such property includes real estate and tangible property located within the United States. Unlike the estate tax rules for U.S. stock held by nonresidents, however, nonresident noncitizens generally are not subject to U.S. gift tax on the transfer of intangibles, such as stock or securities, regardless of where such property is situated.

Special rules apply to U.S. citizens who relinquish their U.S. citizenship or long-term residents of the United States who terminate their U.S. residency within the 10 years prior to the date of transfer, unless such loss did not have as one of its principal purposes the avoidance of tax (sec. 2501(a)(3)). Under these rules, nonresident noncitizens are subject to gift tax on transfers of intangibles, such as stock or securities. Taxpayers are deemed to have a principal purpose of tax avoidance if they meet the 5-year tax liability test or the net worth test, discussed above. Exceptions from this tax avoidance treatment apply in the same circumstances as those described above (relating to certain dual citizens and other individuals who submit a timely and complete ruling request with the IRS as to whether their expatriation or residency termination had a principal purpose of tax avoidance).

Other tax rules with respect to expatriates

The expatriation tax provisions permit a credit against the U.S. tax imposed under such provisions for any foreign income, gift, estate, or similar taxes paid with respect to the items subject to such taxation. This credit is available only against the tax imposed solely as a result of the expatriation tax provisions, and is not available to be used to offset any other U.S. tax liability.

In addition, certain information reporting requirements apply. Under these rules, a U.S. citizen who loses his or her citizenship is required to provide a statement to the State Department (or other designated government entity) that includes the individual's social security number, forwarding foreign address, new country of residence and citizenship, a balance sheet in the case of individuals with a net worth of at least $500,000, and such other information as the Secretary may prescribe. The information statement must be provided no later than the earliest day on which the individual (1) renounces the individual's U.S. nationality before a diplomatic or consular officer of the United States, (2) furnishes to the U.S. Department of State a statement of voluntary relinquishment of U.S. nationality confirming an act of expatriation, (3) is issued a certificate of loss of U.S. nationality by the U.S. Department of State, or (4) loses U.S. nationality because the individual's certificate of naturalization is canceled by a U.S. court. The entity to which such statement is to be provided is required to provide to the Secretary of the Treasury copies of all statements received and the names of individuals who refuse to provide such statements. A long-term resident whose U.S. residency is terminated is required to attach a similar statement to his or her U.S. income tax return for the year of such termination. An individual's failure to provide the required statement results in the imposition of a penalty for each year the failure continues equal to the greater of (1) 5 percent of the individual's expatriation tax liability for such year, or (2) $1,000.

The State Department is required to provide the Secretary of the Treasury with a copy of each certificate of loss of nationality approved by the State Department. Similarly, the agency administering the immigration laws is required to provide the Secretary of the Treasury with the name of each individual whose status as a lawful permanent resident has been revoked or has been determined to have been abandoned. Further, the Secretary of the Treasury is required to publish in the Federal Register the names of all former U.S. citizens with respect to whom it receives the required statements or whose names or certificates of loss of nationality it receives under the foregoing information-sharing provisions.

Immigration rules with respect to expatriates

Under U.S. immigration laws, any former U.S. citizen who officially renounces his or her U.S. citizenship and who is determined by the Attorney General to have renounced for the purpose of U.S. tax avoidance is ineligible to receive a U.S. visa and will be denied entry into the United States. This provision was included as an amendment (the "Reed amendment") to immigration legislation that was enacted in 1996.

REASONS FOR CHANGE

The Committee is aware that some individuals each year relinquish their U.S. citizenship or terminate their U.S. residency for the purpose of avoiding U.S. income, estate, and gift taxes. By so doing, such individuals reduce their annual U.S. income tax liability and reduce or eliminate their U.S. estate tax liability.

The Committee recognizes that citizens and residents of the United States have a right not only physically to leave the United States to live elsewhere, but also to relinquish their citizenship or terminate their residency. The Committee does not believe that the Internal Revenue Code should be used to stop U.S. citizens and residents from relinquishing citizenship or terminating residency; however, the Committee also does not believe that the Code should provide a tax incentive for doing so. In other words, to the extent possible, an individual's decision to relinquish citizenship or terminate residency should be tax-neutral.

The Committee is concerned that the present-law expatriation tax rules are difficult to administer. In addition, the Committee is concerned that the alternative method of taxation under section 877 can be avoided by postponing the realization of U.S.-source income for 10 years. The Committee believes that the expatriation tax rules are largely ineffective in taxing U.S. citizens and residents who relinquish citizenship or terminate residency with a principal purpose to avoid tax.

The Committee believes that the present-law expatriation tax rules should be replaced with a tax regime applicable to former citizens and residents that does not rely on establishing a tax avoidance motive. Because U.S. citizens and residents who retain their citizenship or residency generally are subject to income tax on accrued appreciation when they dispose of their assets, as well as estate tax on the full value of assets that are held until death, the Committee believes it fair to tax individuals on the appreciation in their assets when they relinquish their citizenship or terminate their residency. The Committee believes that an exception from such a tax should be provided for individuals with a relatively modest amount of appreciated assets. The Committee also believes that, where U.S. estate or gift taxes are avoided with respect to a transfer of property to a U.S. person by reason of the expatriation of the donor, it is appropriate for the recipient to be subject to an income tax based on the value of the property.

The Committee also believes that the present-law immigration rules applicable to former citizens are ineffective. The Committee believes that the rules should be modified to eliminate the requirement of proof of a tax avoidance purpose, and to coordinate the application of those rules with the tax rules provided under the new regime.

EXPLANATION OF PROVISION

In general

The bill generally subjects certain U.S. citizens who relinquish their U.S. citizenship and certain long-term U.S. residents who terminate their U.S. residence to tax on the net unrealized gain in their property as if such property were sold for fair market value on the day before the expatriation or residency termination. Gain from the deemed sale is taken into account at that time without regard to other Code provisions; any loss from the deemed sale generally would be taken into account to the extent otherwise provided in the Code. Any net gain on the deemed sale is recognized to the extent it exceeds $600,000 ($1.2 million in the case of married individuals filing a joint return, both of whom relinquish citizenship or terminate residency). The $600,000 amount is increased by a cost of living adjustment factor for calendar years after 2002.

Individuals covered

Under the bill, the mark-to-market tax applies to U.S. citizens who relinquish citizenship and long-term residents who terminate U.S. residency. An individual is a long-term resident if he or she was a lawful permanent resident for at least 8 out of the 15 taxable years ending with the year in which the termination of residency occurs. An individual is considered to terminate long-term residency when either the individual ceases to be a lawful permanent resident (i.e., loses his or her green card status), or the individual is treated as a resident of another country under a tax treaty and the individual does not waive the benefits of the treaty.

Exceptions from the mark-to-market tax are provided in two situations. The first exception applies to an individual who was born with citizenship both in the United States and in another country; provided that (1) as of the expatriation date the individual continues to be a citizen of, and is taxed as a resident of, such other country, and (2) the individual was not a resident of the United States for the 5 taxable years ending with the year of expatriation. The second exception applies to a U.S. citizen who relinquishes U.S. citizenship before reaching age 18½, provided that the individual was a resident of the United States for no more than 5 taxable years before such relinquishment.

Election to be treated as a U.S. citizen

Under the bill, an individual is permitted to make an irrevocable election to continue to be taxed as a U.S. citizen with respect to all property that otherwise is covered by the expatriation tax. This election is an "all or nothing" election; an individual is not permitted to elect this treatment for some property but not for other property. The election, if made, would apply to all property that would be subject to the expatriation tax and to any property the basis of which is determined by reference to such property. Under this election, the individual would continue to pay U.S. income taxes at the rates applicable to U.S. citizens following expatriation on any income generated by the property and on any gain realized on the disposition of the property. In addition, the property would continue to be subject to U.S. gift, estate, and generation-skipping transfer taxes. In order to make this election, the taxpayer would be required to waive any treaty rights that would preclude the collection of the tax.

The individual also would be required to provide security to ensure payment of the tax under this election in such form, manner, and amount as the Secretary of the Treasury requires. The amount of mark-to-market tax that would have been owed but for this election (including any interest, penalties, and certain other items) shall be a lien in favor of the United States on all U.S.-situs property owned by the individual. This lien shall arise on the expatriation date and shall continue until the tax liability is satisfied, the tax liability has become unenforceable by reason of lapse of time, or the Secretary is satisfied that no further tax liability may arise by reason of this provision. The rules of section 6324A(d)(1), (3), and (4) (relating to liens arising in connection with the deferral of estate tax under section 6166) apply to liens arising under this provision.

Date of relinquishment of citizenship

Under the bill, an individual is treated as having relinquished U.S. citizenship on the earliest of four possible dates: (1) the date that the individual renounces U.S. nationality before a diplomatic or consular officer of the United States (provided that the voluntary relinquishment is later confirmed by the issuance of a certificate of loss of nationality); (2) the date that the individual furnishes to the State Department a signed statement of voluntary relinquishment of U.S. nationality confirming the performance of an expatriating act (again, provided that the voluntary relinquishment is later confirmed by the issuance of a certificate of loss of nationality); (3) the date that the State Department issues a certificate of loss of nationality; or (4) the date that a U.S. court cancels a naturalized citizen's certificate of naturalization.

Deemed sale of property upon expatriation or residency termination

The deemed sale rule of the bill generally applies to all property interests held by the individual on the date of relinquishment of citizenship or termination of residency. Special rules apply in the case of trust interests, as described below. U.S. real property interests, which remain subject to U.S. tax in the hands of nonresident noncitizens, generally are excepted from the bill. Regulatory authority is granted to the Treasury to except other types of property from the bill.

Under the bill, an individual who is subject to the mark-to-market tax is required to pay a tentative tax equal to the amount of tax that would be due for a hypothetical short tax year ending on the date the individual relinquished citizenship or terminated residency. Thus, the tentative tax is based on all income, gain, deductions, loss, and credits of the individual for the year through such date, including amounts realized from the deemed sale of property. The tentative tax is due on the 90th day after the date of relinquishment of citizenship or termination of residency.

Retirement plans and similar arrangements

Subject to certain exceptions, the provision applies to all property interests held by the individual at the time of relinquishment of citizenship or termination of residency. Accordingly, such property includes an interest in an employer-sponsored retirement plan or deferred compensation arrangement as well as an interest in an individual retirement account or annuity (i.e., an IRA).[8] However, the provision contains a special rule for an interest in a "qualified retirement plan." For purposes of the provision, a "qualified retirement plan" includes an employer-sponsored qualified plan (sec. 401(a)), a qualified annuity (sec. 403(a)), a tax-sheltered annuity (sec. 403(b)), an eligible deferred compensation plan of a governmental employer (sec. 457(b)), or an IRA (sec. 408). The special retirement plan rule applies also, to the extent provided in regulations, to any foreign plan or similar retirement arrangement or program. An interest in a trust that is part of a qualified retirement plan or other arrangement that is subject to the special retirement plan rule is not subject to the rules for interests in trusts (discussed below).

Under the special rule, an amount equal to the present value of the individual's vested, accrued benefit under a qualified retirement plan is treated as having been received by the individual as a distribution under the plan on the day before the individual's relinquishment of citizenship or termination of residency. It is not intended that the plan would be deemed to have made a distribution for purposes of the tax-favored status of the plan, such as whether a plan may permit distributions before a participant has severed employment. In the case of any later distribution to the individual from the plan, the amount otherwise includible in the individual's income as a result of the distribution is reduced to reflect the amount previously included in income under the special retirement plan rule. The amount of the reduction applied to a distribution is (1) the excess of the amount included in income under the special retirement plan rule over (2) the total reductions applied to any prior distributions. However, under the provision, the retirement plan, and any person acting on the plan's behalf, will treat any later distribution in the same manner as the distribution would be treated without regard to the special retirement plan rule.

[8] Application of the provision is not limited to an interest that meets the definition of property under section 83 (relating to property transferred in connection with the performance of services).

It is expected that the Treasury Department will provide guidance for determining the present value of an individual's vested, accrued benefit under a qualified retirement plan, such as the individual's account balance in the case of a defined contribution plan or an IRA, or present value determined under the qualified joint and survivor annuity rules applicable to a defined benefit plan (sec. 417(e)).

Deferral of payment of tax

Under the bill, an individual is permitted to elect to defer payment of the mark-to-market tax imposed on the deemed sale of the property. Interest is charged for the period the tax is deferred at a rate 2 percentage points higher than the rate normally applicable to individual underpayments. Under this election, the mark-to-market tax attributable to a particular property is due when the property is disposed of (or, if the property is disposed of in whole or in part in a nonrecognition transaction, at such other time as the Secretary may prescribe). The mark-to-market tax attributable to a particular property is an amount which bears the same ratio to the total mark-to-market tax for the year as the gain taken into account with respect to such property bears to the total gain taken into account under these rules for the year. The deferral of the mark-to-market tax may not be extended beyond the individual's death.

In order to elect deferral of the mark-to-market tax, the individual is required to provide adequate security to the Treasury to ensure that the deferred tax and interest will be paid. Other security mechanisms are permitted provided that the individual establishes to the satisfaction of the Secretary that the security is adequate. In the event that the security provided with respect to a particular property subsequently becomes inadequate and the individual fails to correct the situation, the deferred tax and the interest with respect to such property will become due. As a further condition to making the election, the individual is required to consent to the waiver of any treaty rights that would preclude the collection of the tax.

The deferred amount (including any interest, penalties, and certain other items) shall be a lien in favor of the United States on all U.S.-situs property owned by the individual. This lien shall arise on the expatriation date and shall continue until the tax liability is satisfied, the tax liability has become unenforceable by reason of lapse of time, or the Secretary is satisfied that no further tax liability may arise by reason of this provision. The rules of section 6324A(d)(1), (3), and (4) (relating to liens arising in connection with the deferral of estate tax under section 6166) apply to liens arising under this provision.

Interests in trusts

Under the bill, detailed rules apply to trust interests held by an individual at the time of relinquishment of citizenship or termination of residency. The treatment of trust interests depends on whether the trust is a qualified trust. A trust is a qualified trust if a court within the United States is able to exercise primary supervision over the administration of the trust and one or more U.S.

persons have the authority to control all substantial decisions of the trust.

Constructive ownership rules apply to a trust beneficiary that is a corporation, partnership, trust, or estate. In such cases, the shareholders, partners, or beneficiaries of the entity are deemed to be the direct beneficiaries of the trust for purposes of applying these provisions. In addition, an individual who holds (or who is treated as holding) a trust instrument at the time of relinquishment of citizenship or termination of residency is required to disclose on his or her tax return the methodology used to determine his or her interest in the trust, and whether such individual knows (or has reason to know) that any other beneficiary of the trust uses a different method.

Nonqualified trusts.—If an individual holds an interest in a trust that is not a qualified trust, a special rule applies for purposes of determining the amount of the mark-to-market tax due with respect to such trust interest. The individual's interest in the trust is treated as a separate trust consisting of the trust assets allocable to such interest. Such separate trust is treated as having sold its net assets as of the date of relinquishment of citizenship or termination of residency and having distributed the assets to the individual, who then is treated as having recontributed the assets to the trust. The individual is subject to the mark-to-market tax with respect to any net income or gain arising from the deemed distribution from the trust.

The election to defer payment is available for the mark-to-market tax attributable to a nonqualified trust interest. Interest is charged for the period the tax is deferred at a rate 2 percentage points higher than the rate normally applicable to individual underpayments. A beneficiary's interest in a nonqualified trust is determined under all the facts and circumstances, including the trust instrument, letters of wishes, and historical patterns of trust distributions.

Qualified trusts.—If an individual has an interest in a qualified trust, the amount of unrealized gain allocable to the individual's trust interest is calculated at the time of expatriation or residency termination. In determining this amount, all contingencies and discretionary interests are assumed to be resolved in the individual's favor (i.e., the individual is allocated the maximum amount that he or she could receive). The mark-to-market tax imposed on such gains is collected when the individual receives distributions from the trust, or if earlier, upon the individual's death. Interest is charged for the period the tax is deferred at a rate 2 percentage points higher than the rate normally applicable to individual underpayments.

If an individual has an interest in a qualified trust, the individual is subject to the mark-to-market tax upon the receipt of distributions from the trust. These distributions also may be subject to other U.S. income taxes. If a distribution from a qualified trust is made after the individual relinquishes citizenship or terminates residency, the mark-to-market tax is imposed in an amount equal to the amount of the distribution multiplied by the highest tax rate generally applicable to trusts and estates, but in no event will the tax imposed exceed the deferred tax amount with respect to the trust interest. For this purpose, the deferred tax amount is equal to (1) the tax calculated with respect to the unrealized gain allocable to the trust interest at the time of expatriation or residency termination, (2) increased by interest thereon, and (3) reduced by any mark-to-market tax imposed on prior trust distributions to the individual.

If any individual's interest in a trust is vested as of the expatriation date (e.g., if the individual's interest in the trust is non-contingent and non-discretionary), the gain allocable to the individual's trust interest is determined based on the trust assets allocable to his or her trust interest. If the individual's interest in the trust is not vested as of the expatriation date (e.g., if the individual's trust interest is a contingent or discretionary interest), the gain allocable to his or her trust interest is determined based on all of the trust assets that could be allocable to his or her trust interest, determined by resolving all contingencies and discretionary powers in the individual's favor. In the case where more than one trust beneficiary is subject to the expatriation tax with respect to trust interests that are not vested, the rules are intended to apply so that the same unrealized gain with respect to assets in the trust is not taxed to both individuals.

Mark-to-market taxes become due if the trust ceases to be a qualified trust, the individual disposes of his or her qualified trust interest, or the individual dies. In such cases, the amount of mark-to-market tax equals the lesser of (1) the tax calculated under the rules for nonqualified trust interests as of the date of the triggering event, or (2) the deferred tax amount with respect to the trust interest as of that date.

The tax that is imposed on distributions from a qualified trust generally is deducted and withheld by the trustees. If the individual does not agree to waive treaty rights that would preclude collection of the tax, the tax with respect to such distributions is imposed on the trust, the trustee is personally liable for the tax, and any other beneficiary has a right of contribution against such individual with respect to the tax. Similar rules apply when the qualified trust interest is disposed of, the trust ceases to be a qualified trust, or the individual dies.

Coordination with present-law alternative tax regime

The bill provides a coordination rule with the present-law alternative tax regime. Under the bill, the expatriation income tax rules under section 877, and the expatriation estate and gift tax rules under sections 2107 and 2501(a)(3) (described above), do not apply to a former citizen or former long-term resident whose expatriation or residency termination occurs on or after September 12, 2002.

Treatment of gifts and inheritances from a former citizen or former long-term resident

Under the bill, the exclusion from income provided in section 102 (relating to exclusions from income for the value of property acquired by gift or inheritance) does not apply to the value of any property received by gift or inheritance from a former citizen or former long-term resident (i.e., an individual who relinquished U.S. citizenship or terminated U.S. residency), subject to the exceptions described above relating to certain dual citizens and minors. Accordingly, a U.S. taxpayer who receives a gift or inheritance from such an individual is required to include the value of such gift or inheritance in gross income and is subject to U.S. tax on such amount. Having included the value of the property in income, the recipient would then take a basis in the property equal to that value. The tax does not apply to property that is shown on a timely filed gift tax return and that is a taxable gift by the former citizen or former long-term resident, or property that is shown on a timely filed estate tax return and included in the gross U.S. estate of the former citizen or former long-term resident (regardless of whether the tax liability shown on such a return is reduced by credits, deductions, or exclusions available under the estate and gift tax rules). In addition, the tax does not apply to property in cases in which no estate or gift tax return is required to be filed, where no such return would have been required to be filed if the former citizen or former long-term resident had not relinquished citizenship or terminated residency, as the case may be. Applicable gifts or bequests that are made in trust are treated as made to the beneficiaries of the trust in proportion to their respective interests in the trust.

Information reporting

The bill provides that certain information reporting requirements under present law (sec. 6039G) applicable to former citizens and former long-term residents also apply for purposes of the bill.

Immigration rules

The bill amends the immigration rules that deny tax-motivated expatriates reentry into the United States by removing the requirement that the expatriation be tax-motivated, and instead denies former citizens reentry into the United States if the individual is determined not to be in compliance with his or her tax obligations under the bill's expatriation tax provisions (regardless of the subjective motive for expatriating). For this purpose, the bill permits the IRS to disclose certain items of return information of an individual, upon written request of the Attorney General or his delegate, as is necessary for making a determination under section 212(a)(10)(E) of the Immigration and Nationality Act. Specifically, the bill would permit the IRS to disclose to the agency administering section 212(a)(10)(E) whether such taxpayer is in compliance with section 877A and identify the items of noncompliance. Recordkeeping requirements, safeguards, and civil and criminal penalties for unauthorized disclosure or inspection would apply to return information disclosed under this provision.

EFFECTIVE DATE

The bill generally is effective for U.S. citizens who relinquish citizenship or long-term residents who terminate their residency on or after September 12, 2002. The provisions of the bill relating to gifts and inheritances are effective for gifts and inheritances received from former citizens and former long-term residents on or after September 12, 2002, whose expatriation or residency termination occurs on or after such date. The provisions of the bill relating to former citizens under U.S. immigration laws are effective on or after the date of enactment.

B. Extension of IRS User Fees

PRESENT LAW

The IRS provides written responses to questions of individuals, corporations, and organizations relating to their tax status or the effects of particular transactions for tax purposes. The IRS generally charges a fee for requests for a letter ruling, determination letter, opinion letter, or other similar ruling or determination. Public Law 104–117 [9] extended the statutory authorization for these user fees [10] through September 30, 2003.

REASONS FOR CHANGE

The Committee believes that it is appropriate to provide a further extension of these user fees.

EXPLANATION OF PROVISION

The bill extends the statutory authorization for these user fees through September 30, 2012. The bill also moves the statutory authorization for these fees into the Internal Revenue Code.

EFFECTIVE DATE

The provision, including moving the statutory authorization for these fees into the Code and repealing the off-Code statutory authorization for these fees, is effective for requests made after the date of enactment.

III. BUDGET EFFECTS OF THE BILL

A. Committee Estimates

In compliance with paragraph 11(a) of rule XXVI of the Standing Rules of the Senate, the following statement is made concerning the estimated budget effects of the provisions of the committee amendment to the bill as reported.

The bill, as reported is estimated to have the following budget effects for fiscal years 2003–2012.

[9] An Act to provide that members of the Armed Forces performing services for the peacekeeping efforts in Bosnia and Herzegovina, Croatia, and Macedonia shall be entitled to tax benefits in the same manner as if such services were performed in a combat zone, and for other purposes (March 20, 1996).

[10] These user fees were originally enacted in section 10511 of the Revenue Act of 1987 (Public Law 100–203, December 22, 1987).

ESTIMATED BUDGET EFFECTS OF H.R. 5063, THE ''ARMED FORCES TAX FAIRNESS ACT OF 2002,'' AS REPORTED BY THE COMMITTEE ON FINANCE

[Fiscal years 2003–2012, in millions of dollars]

Provision	Effective	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2003–07	2003–12
Improving tax equity for military personnel:													
1. Exclusion from gross income of certain death gratuity payments	doa 9/10/01	−1	−1	−1	−1	−1	−1	−1	−1	−1	−1	−5	−9
2. Exclusion of gain on sale of a principal residence by a member of the uniformed services or the foreign service	sa DOE	−2	−14	−14	−15	−15	−16	−16	−18	−19	−21	−59	−149
3. Exclusion for amounts received under Department of Defense Homeowners Assistance Program	pma DOE	([1])	−2	−2	−2	−2	−2	−2	−2	−2	−2	−9	−19
4. Expansion combat zone filing rules to contingency operations	([2])	−9	([1])	([1])	([1])	([1])	−1	−1	−1	−1	−1	−11	−14
5. Above-the-line deduction for oversight travel expenses of national guard and reserve members	apoli tyba 12/31/01	−83	−71	−73	−75	−76	−78	−80	−82	−84	−86	−377	−788
6. Modification of membership requirement for exemption from tax for certain veterans' organizations	tyba DOE	−1	−1	−1	−1	−2	−2	−2	−2	−2	−2	−7	−16
7. Clarification of treatment of certain dependent care assistance programs provided to members of the uniformed services of the United States	tyba 12/31/01	No Revenue Effect											
Total of improving tax equity for military personnel		−96	−89	−91	−94	−96	−100	−102	−106	−109	−113	−468	−995
Other provisions:													
1. Impose mark-to-market on individuals who expatriate	([3])	5	102	85	80	74	71	67	61	57	54	346	656
2. Extension of IRS user fees (through 9/30/12 [4]	rma DOE	....	33	34	35	36	38	39	41	42	44	138	341
Total of other provisions		5	135	119	115	110	109	106	102	99	98	484	997
Net total		−91	46	28	21	14	9	4	−4	−10	−15	16	2

[1] Loss of less than $500,000.

[2] The provisions applies to any period for performing an act that has not expired before the date of enactment.

[3] Generally effective for U.S. citizens who relinquish citizenship or long-term residents who terminate their residency on or after September 12, 2002.

[4] Estimate provided by Congressional Budget Office.

Legend for ''Effective'' column: apoli = amounts paid or incurred in; doa = deaths occurring after; DOE = date of enactment; pma = payments made after; rma = requests made after; sa = sales after; tyba = taxable years beginning after.

Note.—Details may not add to totals due to rounding.

Source: Joint Committee on Taxation.

B. Budget Authority and Tax Expenditures

Budget authority

In compliance with section 308(a)(1) of the Budget Act, the Committee states that the revenue provisions of the committee amendment to the bill do not involve new or increased budget authority.

Tax expenditures

In compliance with section 308(a)(2) of the Budget Act, the Committee states that the revenue-reducing provisions of the committee amendment to the bill involve increased tax expenditures (see revenue table in Part III.A., above). The revenue increasing provisions of the Committee amendment to the bill generally involve reduced tax expenditures (see revenue table in Part III.A., above).

C. Consultation With Congressional Budget Office

In accordance with section 403 of the Budget Act, the Committee advises that the Congressional Budget Office submitted the following statement on this bill.

U.S. Congress,
Congressional Budget Office,
Washington, DC, September 13, 2002.

Hon. Max Baucus,
Chairman, Committee on Finance,
U.S. Senate, Washington, DC.

Dear Mr. Chairman: The Congressional Budget Office has prepared the enclosed cost estimate for H.R. 5063, the Armed Forces Tax Fairness Act of 2002.

If you wish further details on this estimate, we will be pleased to provide them. The CBO staff contact is Annie Bartsch.

Sincerely,

Barry B. Anderson
(For Dan L. Crippen, Director).

Enclosure.

H.R. 5063—Armed Forces Tax Fairness Act of 2002

Summary: H.R. 5063 would raise the exclusion for death gratuity payments for the military, provide military and foreign service homeowners with relief from capital gains taxes, impose a mark-to-market tax on individuals who expatriate, and extend Internal Revenue Service (IRS) user fees through September 30, 2012. In addition, H.R. 5063 would provide individual taxpayers serving in the National Guard and Reserve with a deduction for certain overnight travel expenses, including meals and overnight lodging, incurred while attending National Guard and Reserve meetings. The deduction would be "above the line." Such deductions are statutorily allowed subtractions from gross income that are used to compute adjusted gross income and may be taken by both taxpayers who itemize the deductions and those who do not.

The Joint Committee on Taxation (JCT) and the Congressional Budget Office (CBO) estimate that enacting H.R. 5063 would reduce revenues by $91 million in 2003 and increase revenues by $16 million over the 2003–2007 period and by $2 million over the 2003–

2012 period. Because the act would affect receipts, pay-as-you-go procedures would apply.

JCT has determined that H.R. 5063 contains no intergovernmental mandates as defined in the Unfunded Mandates Reform Act (UMRA), and would not affect the budgets of state, local, or tribal governments. JCT has also determined that the provision imposing mark-to-market taxes or expatriates contains a private-sector mandate. The total cost of complying with the mandate would not exceed the threshold established by UMRA ($115 million in 2002, adjusted annually for inflation).

Estimated cost to the Federal Government: The estimated budgetary impact of H.R. 5063 is shown in the following table.

	By fiscal year, in millions of dollars—				
	2003	2004	2005	2006	2007
CHANGES IN REVENUES					
Market-to-market tax on expatriates	5	102	85	80	74
Above-the-line deduction for travel expenses	−83	−71	−73	−75	−76
Extension of IRS user fees	0	33	34	35	36
Tax relief from capital gains for military and foreign service homeowners	−2	−14	−14	−15	−15
Other provisions	−11	−4	−4	−4	−5
Total changes	−91	46	28	21	14

Note.—Components may not sum to totals because of rounding.

Sources: CBO and the Joint Committee on Taxation.

Basis of estimate: All estimates, with the exception of the provision affecting IRS user fees, were provided by JCT. A number of provisions would reduce revenues if enacted, and several would increase revenues. All together, the act's provisions would reduce revenues by $91 million in 2003, and would increase revenues by $16 million over the 2003–2007 period and by $2 million over the 2003–2012 period.

Most of the revenue reductions would incur from the provisions providing reservists with an above-the-line deduction allowance for travel expenses and providing military and foreign service homeowners relief from taxation of capital gains. The provisions raising the exclusion for death gratuity payments for individuals in the military, providing an exclusion for amounts received under the Department of Defense Homeowners Assistance Program, expanding combat zone filing rules to contingency operations, and extending section 501(c)(19) membership to certain relatives of military personnel would also decrease governmental receipts. As estimated by JCT, all of these provisions together would reduce revenues by $96 million in 2003, by about $468 million over the 2003–2007 period, and by about $995 million over the 2003–2012 period.

JCT estimates that the provision imposing a mark-to-market tax on individuals who expatriate would increase revenues by $5 million in 2003, by $346 million over the 2003–2007 period, and by $656 million over the 2003–2012 period.

The act also would extend the period during which the IRS may charge fees on businesses for providing ruling, opinion, and determination letters. Under current law, the IRS's authority to charge such fees will expire at the end of the fiscal year 2003. The act would extend the authority to charge such fees until September 30, 2012. Based on the amount of fees collected in recent years and on information from the IRS, CBO estimates that extending the fees would increase governmental receipts by a total of $341 million over the 2004–2012 period.

JCT and CBO estimate that combined, these two provisions would increase revenues by $5 million in 2003, by about $484 million over the 2003–2007 period, and by about $997 million over the 2003–2012 period.

Pay-as-you-go considerations: The Balanced Budget and Emergency Deficit Control Act sets up pay-as-you-go procedures for legislation affecting direct spending or receipts. The net changes in governmental receipts that are subject to pay-as-you-go procedures are shown in the following table. For the purposes of enforcing pay-as-you-go procedures, only the effects through 2006 are counted.

	By fiscal year, in millions of dollars—										
	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012
Changes in outlays	Not applicable										
Changes in receipts	0	−91	46	28	21	14	9	4	−4	−10	−15

Estimated impact on state, local, and tribal governments: JCT has determined that H.R. 5063 contains no intergovernmental mandates as defined in UMRA and would not affect the budgets of state, local, or tribal governments.

Estimated impact on the private sector: JCT has determined that the provision relating to mark-to-market taxes on expatriates contains a private-sector mandate, and that the direct cost of complying with the mandate would not exceed the threshold established by UMRA ($115 million in 2002, adjusted annually for inflation).

Estimate prepared by: Annie Bartsch.

Estimate approved by: G. Thomas Woodward, Assistant Director for Tax Analysis.

IV. VOTES OF THE COMMITTEE

In compliance with paragraph 7(b) of rule XXVI of the Standing Rules of the Senate, the Committee states that H.R. 5063 was, with a quorum present, ordered favorably reported, as amended, by unanimous voice vote on September 12, 2002.

V. REGULATORY IMPACT AND OTHER MATTERS

A. Regulatory Impact

Pursuant to paragraph 11(b) of rule XXVI of the Standing Rules of the Senate, the Committee makes the following statement concerning the regulatory impact that might be incurred in carrying out the provisions of the bill as amended.

Impact on individuals and businesses

The bill includes provisions relating to the exclusion from gross income of certain death gratuity payments, gain on certain sales of principal residence by a member of the uniformed services or the Foreign Service, and certain amounts received under the Department of Defense Homeowners Assistance Program. The bill also extends the combat zone filing rules to contingency operations and modifies the exemption rules for certain tax-exempt veterans' organizations. Most of these provisions are not expected to impose additional administrative requirements on individuals or businesses. The bill also creates an above-the-line deduction for overnight travel expenses of National Guard and Reserve member. Finally the bill imposes a mark-to-market tax on certain individuals who expatriate and extends certain IRS user fees. These provisions may increase regulatory burdens on individuals and businesses.

Impact on personal privacy and paperwork

The provisions of the Committee amendment to the bill do not impact personal privacy.

Some provisions of the bill relating to the exclusion of death gratuities and homeowners assistance payments will reduce paperwork burdens on certain individuals. Other provisions may impose additional burdens on certain individuals. For example, the provision regarding the imposition of a mark-to-market tax on individuals who expatriate will impose some such additional paperwork.

B. Unfunded Mandates Statement

This information is provided in accordance with section 423 of the Unfunded Mandates Reform Act of 1995 (P.L. 104–4).

The Committee has determined that one of the revenue provisions of the bill does impose a Federal mandate on the private sector. That provision relates to the imposition of a mark-to-market tax on individuals who expatriate. The Committee has determined that the revenue provisions of the bill do not impose a Federal intergovernmental mandate on State, local, or tribal governments.

C. Tax Complexity Analysis

Section 4022(b) of the Internal Revenue Service Reform and Restructuring Act of 1998 (the IRS Reform Act) requires the Joint Committee on Taxation (in consultation with the Internal Revenue Service and the Department of the Treasury) to provide a tax complexity analysis. The complexity analysis is required for all legislation reported by the Senate Committee on Finance, the House Committee on Ways and Means, or any committee of conference if the legislation includes a provision that directly or indirectly amends the Internal Revenue Code (the Code) and has widespread applicability to individuals or small businesses.

The staff of the Joint Committee on Taxation has determined that a complexity analysis is not required under section 4022(b) of the IRS Reform Act because the bill contains no provisions that amend the Code and that have "widespread applicability" to individuals or small businesses.

VI. CHANGES IN EXISTING LAW MADE BY THE BILL, AS REPORTED

In the opinion of the Committee, it is necessary in order to expedite the business of the Senate, to dispense with the requirements of paragraph 12 of rule XXVI of the Standing Rules of the Senate (relating to the showing of changes in existing law made by the bill as reported by the Committee).